SECTION 1

Introduction

During the past few years, "third-party" financing of litigation activity in the United States has grown considerably and attracted attention from journalists, researchers, and policy advocates. The phenomenon of interest is provision of capital (money) by nontraditional sources to civil plaintiffs, defendants, or their lawyers to support litigation-related activities. Because *third-party financing* does not accurately describe the phenomenon of interest, particularly in the United States, in this paper I propose and use a new term that is more descriptive of the phenomenon: *alternative litigation financing* (ALF).

The term *third-party financing* invites confusion, particularly in the U.S. context, for the following reasons. The first two parties in a civil lawsuit are the plaintiff and the defendant. In the United States, it is has become traditional for other parties to be involved in financing civil litigation. Most important in this regard are funding of plaintiffs' legal costs by their attorneys under contingency-fee agreements[1] and funding of defendants' legal costs by insurers.[2] In short, some forms of "third-party" financing are so familiar and ubiquitous that they have come to be widely accepted and in many cases not even recognized as litigation financing by nonparties to the litigation. The subject of this paper is litigation financing in the United States[3] by entities other than plaintiffs, defendants, their lawyers, and defendants' insurers.

As emphasized and elaborated in this paper, ALF in the United States involves diverse types of litigation financing.[4] More specifically, there are three forms of ALF that are currently fairly common in the United States. These are (1) consumer legal funding, which involves provision of non-recourse loans directly to consumer (i.e., individual) plaintiffs with pending lawsuits; (2) subprime lending to plaintiffs' law firms (i.e., firms whose litigation work is largely concentrated in representing individuals with personal-injury claims); and (3) investments in commercial (i.e., business-against-business) lawsuits or their proceeds.[5]

There is almost no systematic empirical information about U.S. ALF activities or their effects on outcomes of social concern. Nonetheless, some have argued that ALF is unethical,

1 An excellent source on plaintiffs' law firms in the United States is Kritzer (2004).

2 See Yeazell (2001) for a history of civil litigation financing in the United States.

3 Developments in other countries are not addressed in this paper.

4 The term *litigation* is used throughout this paper to refer to legal disputes even if they might be or are destined to be resolved through forms of alternative dispute resolution, such as arbitration.

5 This paper focuses on these three types of ALF. I do not consider other business models that may emerge for companies that finance litigation. I also do not consider other types of transactions that might be viewed as nontraditional or alternative means of financing pursuit of legal claims, such as plaintiffs' attorneys pooling their resources to pursue a large class action or a mass tort, or transfer of legal claims as part of a bankruptcy proceeding.

have predicted that ALF will lead to various socially undesirable outcomes, or both. Accordingly, they have called for extensive regulation or prohibition of ALF (e.g., Beisner, Miller, and Rubin, 2009; Presser, 2009; Rubin, 2009).

In this paper, I consider ethical and economic issues related to ALF in the United States and provide an overview of its current status and potential futures. My main goals are to help public policymakers,[6] legal practitioners, legal scholars, and social scientists understand the current status of ALF in the United States, the growing literature, and the emerging policy debate. More specifically, this paper provides perspectives and analyses of (1) the ethics (a term with various meanings) of ALF, (2) the ethics of litigation-related activities that might accompany ALF, (3) the plausibility of various claims about the effects of ALF to date, and (4) how future developments in ALF markets—such as growth and increasing competition—may affect its social costs and benefits.

[6] Several types of policymaking institutions seem important in shaping the future of ALF in the United States, namely, bar associations; courts; legislatures; law-enforcement officials, such as state attorneys general; and regulators of companies that might wish to supply capital to finance litigation, such as banks and insurance companies.