Coronavirus will lead to litigation funding boom

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By now, COVID-19's immediate and direct impacts on the business and legal communities are obvious and well known. However, the secondary affects on those industries will continue to ripple for months and years ahead. Among those is the likely surge in litigation funding that will result from the coronavirus fallout.

Stated briefly, litigation funding is a form of specialty financing whereby third parties (called litigation funders) provide money to parties to litigation (generally plaintiffs) and their lawyers in exchange for a portion of proceeds from a settlement or judgment. With litigation funding, a litigation funder invests in the litigation on a non-recourse basis and provides capital to pay litigation costs. If the litigation is resolved successfully, the proceeds received by the plaintiff are shared with the litigation funder. If the litigation is unsuccessful, the litigation funder is not owed anything from the plaintiff or its lawyers.

There are numerous reasons litigation funding is likely to spike as a result of the COVID-19 outbreak. This article considers a few of the most notable items that will fuel that growth: increased litigation, unresolved questions of law, and reduced access to capital.

Increased litigation

First, and most simply, the fallout from coronavirus is going to cause an increase in litigation generally. During difficult economic times, companies tend to look for any revenue they can find, including the pursuit of litigation that they may have otherwise let pass during boom times. Historically, litigation also tends to increase when the economy exits a recession based on events that occurred during the recession. When the economy rebounds from the sharp downturn caused by the pandemic, we can expect a correlating rise in litigation.

In addition to a general increase in litigation, coronavirus-specific impacts will also escalate litigation. The quarantining of the country and much of the world has cut off supply lines to businesses. As a result, many companies have stopped performing, are experiencing difficulties in delivering on the requirements of their contracts, are not paying rent, are not paying suppliers, and the list goes on. With those problems affecting businesses in nearly all industries, it is likely there will be an onslaught of lawsuits involving the failure to perform on those contracts.

Unresolved questions of law

We have never experienced an event that shuts down the world’s economy and supply chains for an extended period as has occurred with this pandemic. With a novel situation comes novel issues of law, novel issues of law create uncertainty in litigation, and uncertainty in litigation encourages risk aversion.

Businesses have been scrambling to review their contracts to determine whether the provisions therein consider a circumstance such as this that was previously given little thought. Specifically, force majeure clauses and business interruption insurance contracts are currently being thoroughly analyzed to determine their applicability and enforceability as a result of a global pandemic. Undoubtedly, parties are going to disagree on those interpretations.

While the influenza pandemic of 1918 provided some case law on these issues, those decisions are now 100 years old and provide little comfort to litigants seeking precedential certainty. Litigation funding addresses that concern by mitigating risk to both plaintiffs and law firms. Thus, we can expect that many businesses and law firms will turn to litigation funding to support claims arising from novel issues created by COVID-19.

Reduced access to capital

Companies across nearly all industries have suffered from significant reductions in revenue during the worldwide disruption and lock down. The application of greater scrutiny to capital expenditures will likely cause many businesses to determine that they do not have cash to fund litigation or just do not want to use their limited resources for litigation. Inevitably, plaintiffs will seek alternative forms of financing to reduce their own out of pocket outlays, leading to a surge in litigation funding.

Law firms are also likely to suffer short-term cash crunches as courts nationwide are delaying cases. Those delays put on hold expected revenues from the conclusion of litigation matters. Furthermore, law firms will be forced to face the reality that accounts receivable are likely to grow with payments delayed as their clients deal with a myriad of financial pressures.

With businesses’ capital spent elsewhere and law firms experiencing short-term cash shortages, litigation funders should be inundated with prospective investments.

Conclusion

With an expected growth in litigation, a reduction in access to capital, and an increase in competition for litigation funding, it is more important now than ever for plaintiffs to position themselves favorably and as they approach litigation funders. It will also be vital for litigation funders to fully investigate the prospects of potential litigation investments.

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McDonald Hopkins has the unique combination of knowledge and experience in the litigation finance industry to guide both plaintiffs seeking financing and funders looking for assistance with diligence during these turbulent times. Please contact the attorneys below for more information.

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