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A 32% Litigation Funding Tax Would Harm US Taxpayers the Most

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In recent years, it has become increasingly common for whistleblowers to rely on litigation funding to contend with the top law firms representing corporate defendants on the other side.

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Whistleblower attorney Paul Scott says litigation funding helps private whistleblowers litigate cases against government payees that commit fraud against the US.

A last-minute addition to the Senate's draft of the "big, beautiful bill" is a nearly 32% tax on most litigation financing arrangements with a prohibition on netting losses in the same taxable year. Its likely goal is to raise a few dollars while curtailing the resources behind mass tort litigation, an appealing prospect to many conservatives. But US taxpayers will be the largest group of victims if this provision passes.

The nation's chief fraud-fighting tool is the False Claims Act, which includes a whistleblower provision that permits private citizens (called relators) to file lawsuits against government payees that defraud the US, then share in the recovery. The government can either intervene in such cases and take over the litigation, or it can decline and allow private whistleblowers to pursue the cases on their own.

In recent years, it has become increasingly common for the government to rely on whistleblowers to litigate declined cases—and for whistleblowers to rely on litigation funding to contend with the top law firms representing corporate defendants on the other side.

The decision by the US Court of Appeals for the Eleventh Circuit in *Ruckh v. Salus Rehabilitation LLC* illustrates how such funding directly benefits the US. The relator in that case agreed to pay 4% of the recovery to a litigation funding firm in exchange for the immediate liquidity needed to pursue a declined False Claims Act case against a large skilled nursing management company.

With the benefit of those resources in hand, the relator was able to obtain an $85 million jury verdict in favor of the US against a defendant represented by two of the top 50 largest firms in the country. The defendant appealed the verdict to the Eleventh Circuit, challenging the whistleblower's use of litigation funding, among other things, but the verdict was upheld.

This kind of story is repeated less publicly when whistleblowers pursue declined cases with the assistance of litigation funding, and the cases are settled prior to verdict. But the benefit to the US remains the same.

Over the last four years, in declined qui tam cases alone, the US has recovered over $2.3 billion—a number substantially greater than any prior four-year period. In 2024, more qui tam cases were filed than at any point previously in the history of the False Claims Act, so it is reasonable to expect the trend to continue.

This very trend—an increase in private enforcement recoveries in a target-rich environment—is what has attracted litigation funding to the fight. Private equity firms have long provided the capital for government contractors that sometimes end up as defendants in False Claims Act cases.

Between 2013 and 2022, at least 25 private equity-owned health-care companies (and sometimes the private equity owners themselves) have entered into settlements or been subject to judgments totaling over $600 million to resolve claims that they fraudulently overcharged government payers.

Now investors are making a market decision to invest in enforcement efforts on the other side of these cases to combat fraud. Disparate tax treatment of the two types of investments—favorable capital gains taxation for fraudulent government contractors versus a super tax on whistleblower funders and a prohibition on them netting losses—would impede free markets and make no sense from a policy perspective.

The principal impact of any such provision on government programs would be to drive capital into dubious ventures (such as the skilled nursing operation described above) and away from whistleblowers' efforts to protect the US Treasury. This result would directly contradict the consistent efforts Congress has long made to incentivize whistleblowers to fight fraud on behalf of the government.

The same reasoning holds true when litigation finance firms help fund costly expert services in intervened cases, or when they provide resources for whistleblower claims targeting other government enforcement priorities. This includes large-scale tax fraud, financial fraud, money laundering, economic sanctions violations, drug kingpins, or terrorist financing.

The whistleblower laws supporting all of these programs—whether they result in the collection of taxes, penalties, damages, fines, or forfeitures—all financially benefit the US.

Whatever the government's policy priorities may be regarding the tax treatment of litigation funding involving strictly private parties, any such discrete policy choices shouldn't be executed in such a club-fisted way that they harm the US' own pecuniary interests or the parallel interests of state governments. There is nothing beautiful about that.

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