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Litigation Finance and Crypto Tokens: How a Blockchain Startup Seeks to Create Financing Marketplaces for Disputes

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A recent [VICE Motherboard article](#) highlights an intriguing innovation at the intersection of crypto tech and litigation finance. The topic has caused quite a stir, including a thought-provoking discussion on [ArbTech](#), an [online forum](#) on technology and dispute resolution. This post reports on this innovation, and expands upon the ArbTech discussion.

The innovation concerns [Ryval](#), a law firm-backed crypto project with an ambitious vision of creating the “stock market of litigation financing,” via the purchase and trade of crypto tokens that fund civil lawsuits. The project is a collaboration between Kyle Roche, a partner in the New York law firm, Roche Freedman LLP; [Republic](#), an investment platform providing access to startups, real estate, crypto, and video game investments; and [Ava Labs](#), creator of the [Avalanche](#) smart contracts platform. Ryval calls this crypto offering the world’s first “[Initial Litigation Offering](#),” or ILO – taking inspiration from the mechanics of the most known crypto fundraising process called an initial coin offering (ICO).

The particulars of Ryval’s offering generate serious doubts about its viability and attractiveness for potential investors. However, the broader tokenization concept raises fascinating possibilities for the litigation finance space, potentially creating entirely new funding markets and classes of investors.

Ryval’s Initial Litigation Offering, Explained

Ryval’s concept is to create a marketplace for crypto tokens that represent shares in a litigation claim, in the process granting non-accredited individual investors access to litigation financing as an investment class. The crypto tokens created (using the Avalanche blockchain) represent tokenized shares in a funded claim, and that tokenization/capital-raising crypto-economic structure has been termed an ILO.

As noted above, the ILO concept mirrors the ICO structure that has been utilized in crypto fundraising since around 2013. High-profile and successful ICO examples include [Ethereum](#), [Tezos](#), and [EOS](#). In turn, the underlying structure of an ICO often resembles an initial public offering (IPO) in traditional equity finance, in the sense that legal tender is exchanged by investors for a project’s token, in the same way traditional investors would for a newly publicly traded stock.

Depending on the jurisdiction, crypto tokens may be considered securities. In the case of Ryval, the ILO crypto tokens appear to meet the classic definition of a security, in that it would be merely a publicly traded, tokenized interest in a fund that is in turn funding a lawsuit. Ryval's ILO meets U.S. securities law requirements by leveraging the Obama-era [Jumpstart Our Business Startups \(JOBS\) Act](#). The Act allows for a crowdfunding exemption for private companies to raise up to \$5 million from the public, dispensing with the requirement to seek funding only from accredited investors.

In theory, the tokenization process involved in an ILO should allow investors to leverage the benefit of the technology to maximize returns. A first benefit would be the transparency of all transactions and smart contract processes on the blockchain. This auditability would ensure that the funding fee structures themselves make investment sense. A second benefit would be automation and flexibility: allowing embedded options for investors based on various case outcomes (e.g., partial refunds for early dismissal), and self-executing payouts to investors in the event of successful recovery, bypassing payout risks in traditional funding. A third benefit would be liquidity: because crypto structures easily allow for the creation of marketplaces to buy and sell tokens, market makers can create large liquidity pools very quickly. This, in turn, would enable token holders to enter or exit a litigation fund very quickly with reduced risk and value loss (for example, the ability to sell stakes to another bidder at any point in the proceedings), and, possibly, hedge risk by buying or selling derivatives against the value of the interest.

Expanding the Investor Pool for Litigation Finance

Roche Freedman and Republic have already rolled out the ILO concept in a [real-world lawsuit](#). The lawsuit pits [Apothio LLC](#), a hemp and cannabis company, against Kern County in California, arising out of the County's alleged destruction of Apothio's crops, valued at U.S. \$1 billion. Roche Freedman represents Apothio, and Roche Freedman and Republic issued the \$5 million ILO on Republic's [platform](#). Ryval appears to be the next step in the collaboration between Roche Freedman and Republic, creating a standalone platform for crowdsourced, tokenized litigation funding for future litigations.

Criticism of the Apothio ILO and Ryval

Allowing the general public to invest in the outcome of disputes is one of the key pillars to the project's appeal, but so too is profit for those investors. Ryval claims a rather ambitious (and wholly unverified) projection of "50%+ Annual Returns." When pressed by VICE Motherboard, Mr. Freedman [admitted](#) that the figure "may be a little high."

[Criticism](#) of Ryval's approach has not been sparing, based on readings of the Apothio ILO [investment funding contract](#) (and annexes [here](#) and [here](#)). Commentators have pointed out the ILO's highly problematic and one-sided terms, relative to current market terms in the litigation finance space. This includes the low position of unaccredited investors in terms of priority of investment returns: in the ILO's investment return waterfall, the lawyers get paid before the investors, which is not current market practice in litigation funding. The terms of the ILO further fix the maximum recovery for investors at 3.5x the initial investment (after a 3-year lockup period), which are, again, inferior to market terms current litigation funders negotiate for

themselves. Finally, the terms of the ILO contain a largely undefined procedure for investors to receive notification of a successful recovery and claim a return on said recovery. This last criticism is particularly notable, as the ILO fails to realize a major potential benefit of tokenization mentioned above – automation and self-executing payouts in case of successful recovery.

Thus, the terms of the Apothio litigation ILO appear to be heavily one-sided for the benefit of the law firm representing the client – which is not surprising, given that Roche Freedman both created the ILO and is the beneficiary of such funding as counsel in the Apothio litigation. Perhaps equally unsurprising, the \$5 million ILO has only raised about [\\$372,232](#) to date. On the whole, the Apothio ILO feels like a Kickstarter wrapped in a crypto bow: it fails to capitalize on the fundamental benefits of crypto, even as its marketing leans heavily on the popularity of crypto as an investment asset class.

The Future of Tokenized Litigation Finance?

While Ryval’s offering may be heavily criticized due to the terms of its funding arrangement, the tokenization of litigation finance, as a concept and innovation, raises a number of intriguing possibilities. Future endeavors may better harness the full potential of tokenization applied to litigation finance. The following are just a few of the crypto technology’s possibilities:

- Tokenization creates the possibility of a highly liquid and widely dispersed marketplace for the trading of stakes (including derivatives) in litigation claims. This creates efficiencies of scale and the spreading of investor risk. Each claim could potentially have tens of thousands of investors, or more. Moreover, as noted above, individual investors could cash out of their investments at any point in the proceedings, even post-judgment or post-enforcement (while others could buy in), allowing a fluid market that would evolve along with the prospects of a claim and its recovery.
- The security afforded by blockchain and potential automatic payout via smart contract could create efficiencies around one of the more fraught periods of litigation funding – the payout. This would cut down on time, cost and potential further disputes between investors due to the transparency of assets and processes on the blockchain, and the finality of self-executing smart contracts.
- The reduced risk associated with fund diversification – in this case, funding portfolios of claims – is already [well-known](#) and applied by [many](#) litigation funders. Tokenization could create further efficiencies and opportunities vis-à-vis diversification via portfolio funding, as individual investors can easily fund multiple portfolios, or multiple claims.
- Tokenization may create entirely new players, including ancillary markets. One example is that of prediction markets like [Augur](#). The Augur platform allows users to wager against each other on the outcome of any objectively verifiable result. This type of prediction market could allow litigation funds to not only enhance their prediction models, but also potentially hedge risk in the same way that financial derivatives allow in other markets.
- Blockchain efficiencies and automation could lower the barriers to entry for funding of smaller, “plain vanilla” arbitration claims, creating entirely new categories of fundable claims. As long as a given claim has a claim value that is substantially greater than the costs of prosecuting such a claim, there is theoretically a possibility to fund via tokenization.
- Perhaps most intriguingly, tokenization might disrupt the environmental, social, and governance (ESG) space, by providing greater capital access and liquidity to fund such claims. Tokenization,

combined with strong public awareness of a given litigation effort, could theoretically provide access to funds from large pools of individual investors-activists, allowing the latter to purchase a stake in claims where the return is not only advancement of an ESG cause, but also a potential upside in case of success. Current litigation crowdfunding platforms such as [CrowdJustice](#) (which funds a number of cases with an ESG dimension) could benefit from the technology. In short, tokenization may make it easier for activists to back ESG-related litigation or arbitration, with or without expectation of a ROI.


As with many emerging technologies, the initial version of tokenized litigation funding, as presented in the Ryval offering, is far from optimal. But, as the examples above demonstrate, tokenization could unlock considerable efficiencies in the litigation finance space. As future players enter this market, competition should help drive innovation and lead toward a more serious and mature market.

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