

## **POLICY BRIEF**

# **Third-Party Litigation Funding: How Foreign Capital Is Weaponizing America's Courts Against Its Energy Sector**

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### **Summary**

Third-party litigation funding (TPLF) has transformed U.S. civil litigation into a high-return alternative asset class, placing the American energy industry in the crosshairs of America's geopolitical rivals. TPLF entails outside investors providing nonrecourse financing to plaintiffs or plaintiffs' attorneys in exchange for a share of any settlement or judgment, fueling a multibillion-dollar industry. Yet this practice rests on a glaring tax loophole. By structuring deals as prepaid forward contracts that qualify as derivatives, funders treat their profits as long-term capital gains rather than ordinary income.<sup>1</sup> For foreign nationals and foreign corporations with no U.S. presence, those gains are exempt from U.S. withholding tax and are not treated as effectively connected income. Foreign investors can therefore extract tax-free profits from American court outcomes, while domestic plaintiffs are taxed at ordinary income rates on the full recovery. The result is a profound distortion of both the tax code and the civil justice system as offshore capital is subsidized to chase high-stakes U.S. lawsuits, inflating settlements, prolonging cases, and injecting foreign influence directly into American courthouses.

The scale and sophistication of the TPLF market only amplify these risks. A December 2022 Government Accountability Office (GAO) report documented a diverse ecosystem of funders, private specialist firms, multistrategy asset managers, publicly traded companies such as Burford Capital, and smaller operations backed by family offices or high-net-worth individuals.<sup>2</sup> Many raise capital from institutional investors, including university endowments and pension funds. Trade associations such as the International Legal Finance Association and the American Legal Finance Association further professionalize the industry by lobbying legislators, regulators, and courts to protect and expand TPLF.

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<sup>1</sup> Jim Carter, "End the Third-Party Litigation Funding Tax Loophole," *Legal Backgrounder*, Washington Legal Foundation, June 2, 2025, <https://www.wlf.org/2025/06/02/publishing/end-the-third-party-litigation-funding-tax-loophole/>.

<sup>2</sup> U.S. Government Accountability Office, *Third-Party Litigation Financing: Market Characteristics, Data, and Trends*, GAO-23-105210 (December 2022), <https://www.gao.gov/assets/gao-23-105210.pdf>.

## TPLF Targets American Energy Industry

Nowhere are the dangers more acute than in the energy sector. High-stakes disputes over climate claims, intellectual property in new technologies, mergers, joint ventures, and environmental regulations have proliferated.<sup>3</sup> With the commercial litigation funding market already estimated at roughly \$16 billion and still growing, most deals remain secret as courts, defendants, and the public rarely learn who is truly bankrolling the suit or directing strategy. Foreign sovereign wealth funds and entities linked to geopolitical competitors have poured capital into U.S. energy-related litigation, creating clear national-security vulnerabilities. While a few conservative TPLF supporters claim that TPLF is a tool to fight ESG policies, it is more likely that the opposite is true. Anti-US energy interests are far more likely to use TPLF as a way to stymie US energy production. Environmental activists have openly embraced TPLF as a strategic lever; a 2025 *Nature Sustainability* article by Masaki Iwasaki of Seoul National University outlined how third-party funding can “powerfully support environmental causes.”<sup>4</sup> Since the 2015 Paris Agreement, the annual number of climate lawsuits against the world’s largest oil, gas, and coal companies has nearly tripled, with at least 86 major actions worldwide. Many of these suits are quietly underwritten by the very offshore capital that benefits from the TPLF tax loophole.<sup>5</sup>

Funded lawsuits can harass American producers, impose crippling legal costs, force disclosure of proprietary information through discovery, weaken domestic production capacity, and advance external agendas, all while the funders reap tax-free gains.

Dozens of suits filed by states, cities, counties, and other public entities against companies like ExxonMobil, Chevron, BP, Shell, and ConocoPhillips allege that the firms knew for decades that fossil fuel emissions drive climate change, misled the public and consumers about risks, and should pay for resulting damages.<sup>6</sup> These cases are costly and protracted due to complex science, multi-jurisdictional issues, and motions practice. Funding for the lawsuits flows through large nonprofit networks or fiscal sponsors that have granted millions to plaintiffs’ firms like Sher Edling LLP, which represents numerous jurisdictions in these suits.<sup>7</sup> Lawmakers have highlighted these as examples of opaque third-party support for climate litigation targeting the energy sector, sometimes linking it to TPLF’s tax-advantaged structure and foreign-based philanthropic capital.<sup>8</sup>

<sup>3</sup> Peter Charles Choharis, “National Security Implications of Foreign Third-Party Litigation Financing,” *Perspective*, American Security Project, May 8, 2025, <https://www.americansecurityproject.org/perspective-national-security-implications-of-foreign-third-party-litigation-financing/>.

<sup>4</sup> Masaki Iwasaki, “Leveraging third-party litigation funding for environmental litigation,” *Nature Sustainability* 8, 1426–1427 (November 4, 2025), <https://www.nature.com/articles/s41893-025-01678-7>.

<sup>5</sup> Oil Change International, “New Report: Climate lawsuits being filed against fossil fuel companies have nearly tripled,” September 12, 2024,

<https://oilchange.org/news/new-report-climate-lawsuits-being-filed-against-fossil-fuel-companies-have-nearly-tripled/>.

<sup>6</sup> Heather Mac Donald, “The Climate Litigation Swindle,” *City Journal*, April 22, 2026, <https://www.city-journal.org/article/climate-fossil-fuel-energy-lawsuits/>.

<sup>7</sup> Thomas Catenacci, “‘Anti-Energy Lawfare’: Millions in Dark Money Fueling Local Climate Lawsuits Across the Country, Congressional Investigation Finds,” *Washington Free Beacon*, October 7, 2024,

<https://freebeacon.com/latest-news/anti-energy-lawfare-congressional-investigation-uncovered-dark-money-fueling-climate-change-lawsuits-nationwide/>.

<sup>8</sup> Gabe Kaminsky, “Exclusive: Republicans Accuse Climate Groups of Doing China’s ‘Dirty Work’ in the U.S.,” *The Free Press*, December 16, 2025, <https://www.thefp.com/p/exclusive-republicans-accuse-climate>.

A stark example emerged in early 2025 when ExxonMobil filed a federal countersuit in Texas against California Attorney General Rob Bonta, several U.S. environmental nonprofits, and the Intergenerational Environment Justice Fund (IEJF), an Australian nonprofit affiliated with billionaire Andrew Forrest's Minderoo Foundation and his hydrogen competitor, Fortescue.<sup>9</sup> The underlying 2024 California suit had accused ExxonMobil of misleading the public on plastic recyclability as part of broader low-carbon attacks. ExxonMobil alleged that foreign funding from IEJF orchestrated both the litigation and public criticism to gain a competitive advantage. The Justice Department responded by requiring the plaintiffs' law firm to register under the Foreign Agents Registration Act (FARA). The countersuit asserts defamation, business disparagement, tortious interference, and civil conspiracy, charges that highlight how TPLF can turn U.S. courts into tools against Americans.

The broader geopolitical threat from TPLF fits a well-documented strategy of foreign malign influence. As Daniel Byman of the Center for Strategic and International Studies has defined it, such influence involves subversive, undeclared, coercive, or criminal activities by foreign governments, non-state actors, or proxies to shape another country's attitudes and behaviors.<sup>10</sup> Russia has long funneled money through U.S. environmental nonprofits to oppose fracking and pipelines, aiming to

preserve Europe's dependence on Russian gas. Additionally, TPLF has provided a means for foreign entities to exploit the U.S. legal system, potentially to evade sanctions or gain access to sensitive information. As Bloomberg reported, Russian oligarchs closely tied to Vladimir Putin are using the litigation-finance industry to pour millions of dollars into lawsuits in New York and London, sidestepping Western sanctions imposed after Russia's 2022 invasion of Ukraine.<sup>11</sup>

More recently, attention has turned to China-linked entities. A June 2025 State Armor report on the Energy Foundation China (EF-China), a San Francisco-based 501(c)(3) with deep ties to Beijing, revealed that the organization funneled hundreds of millions into U.S. climate and energy projects while maintaining operational supervision by China's National Development and Reform Commission.<sup>12</sup> Its grants to groups such as the Rocky Mountain Institute, Natural Resources Defense Council, and others have supported research, litigation, and advocacy that seek to force fossil-fuel phase-outs, precisely the outcomes that bolster China's dominance in solar, batteries, EVs, and critical minerals. In December 2025, a multi-state coalition of attorneys general led by Montana's Austin Knudsen and Iowa's Brenna Bird urged the Justice Department to investigate EF-China and the Center for Climate Integrity for potential FARA violations, citing their role in funding U.S. litigation against oil and gas companies.

<sup>9</sup> Alexander Stevens, "Foreign Billionaires Are Investing in American Energy Lawsuits," *Institute for Energy Research*, January 5, 2026, <https://www.instituteforenergyresearch.org/regulation/foreign-billionaires-are-investing-in-american-energy-lawsuits/>.

<sup>10</sup> Daniel Byman, "Foreign Malign Influence Targeting U.S. and Allied Corporations," *CSIS Brief*, Center for Strategic and International Studies, March 20, 2025, <https://www.csis.org/analysis/foreign-malign-influence-targeting-us-and-allied-corporations>.

<sup>11</sup> Emily R. Siegel and John Holland, "Putin's Billionaires Dodge Sanctions by Financing Lawsuits," *Bloomberg Law*, March 28, 2024, <https://news.bloomberglaw.com/litigation-finance/putins-billionaires-sidestep-sanctions-by-financing-lawsuits>.

<sup>12</sup> "Who Is Energy Foundation China," *State Armor*, June 11, 2025, <https://statearmor.org/who-is-energy-foundation-china/>.

## **Policy Remedies**

Congress now has a straightforward opportunity to end this distortion. The tax treatment of TPLF violates core principles of neutrality, consistency, and fairness and runs counter to the intent of long-standing provisions meant to encourage constructive investment in the United States. Profits from TPLF are wholly extractive. Thus, closing the loophole would remove the tax preference that makes these deals uniquely attractive to foreign capital, thereby reducing the incentive for offshore investors to weaponize American courts. This step would also curb the broader harms of TPLF, including prolonged litigation, inflated settlement demands, strained attorney-client relationships, and national-security risks.

A broad coalition already supports action to close the tax loophole. Last year, there was a push to reform the tax treatment of TPLF in the One Big Beautiful Bill Act, as eighteen consumer, free-market, and taxpayer organizations sent an open letter to House Speaker Mike Johnson and Senate Majority Leader John Thune, urging Congress to fix the tax treatment in the reconciliation bill.<sup>13</sup> The reforms were ultimately not included in the final package due to a last-minute decision by the Senate Parliamentarian, a major setback that would have improved the bill's impact on the federal budget and addressed this loophole that raises national security concerns.

In February 2026, Senate Judiciary Committee Chairman Chuck Grassley and

Senators Thom Tillis, John Kennedy, and John Cornyn introduced the Litigation Funding Transparency Act.<sup>14</sup> The bill would require public disclosure of third-party funding (including foreign sources) in mass-tort and class-action cases, bar funders from controlling strategy or settlement decisions, and prohibit access to protected discovery materials. Though currently pending without hearings, the legislation provides a critical transparency backstop and should be considered as part of a package of reforms.

TPLF has quietly converted America's judicial system into a tax-advantaged investment vehicle for foreign entities, with the energy sector bearing the brunt. Secret capital flows from sovereign wealth funds, and adversarial nations are fueling lawsuits that harass U.S. producers, extract sensitive information, and advance geopolitical objectives. Congress should close the tax loophole and enact reforms to reclaim the integrity of American courts and protect the nation's critical energy infrastructure, while reducing the negative economic impact on U.S. consumers.

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<sup>13</sup> "Coalition Letter: Creating Tax Fairness in Litigation Funding," *The American Consumer Institute*, May 28, 2025, <https://www.theamericanconsumer.org/2025/05/coalition-letter-creating-tax-fairness-in-litigation-funding/>.

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<sup>14</sup> "Grassley Proposes Third-Party Litigation Funding Reform, Foreign Reporting Requirements," Press Release, Office of U.S. Senator Chuck Grassley, February 11, 2026, <https://www.grassley.senate.gov/news/news-releases/grassley-proposes-third-party-litigation-funding-reform-foreign-reporting-requirements>.