

Summer 2012

Litigation Loansharks: A History of Litigation Lending and a Proposal to Bring Litigation Advances Within the Protection of Usury Laws

Jenna Wims Hashway

Follow this and additional works at: http://docs.rwu.edu/rwu_LR

Recommended Citation

Hashway, Jenna Wims (2012) "Litigation Loansharks: A History of Litigation Lending and a Proposal to Bring Litigation Advances Within the Protection of Usury Laws," *Roger Williams University Law Review*: Vol. 17: Iss. 3, Article 2.
Available at: http://docs.rwu.edu/rwu_LR/vol17/iss3/2

This Article is brought to you for free and open access by the Journals at DOCS@RWU. It has been accepted for inclusion in Roger Williams University Law Review by an authorized administrator of DOCS@RWU. For more information, please contact mwu@rwu.edu.

Litigation Loansharks:

A History of Litigation Lending and a Proposal to Bring Litigation Advances Within the Protection of Usury Laws

Jenna Wims Hashway*

INTRODUCTION¹

On the night of February 20, 2003, a rock band set off unlicensed pyrotechnics in a poorly maintained, overcrowded nightclub, igniting the highly flammable foam that club owners had glued to the walls. One hundred patrons died in the ensuing inferno, and hundreds more were injured, some catastrophically.² The Station Nightclub fire was the fourth worst nightclub fire in U.S. history—an enormous mass casualty event in the nation's

* JD, Roger Williams University School of Law; Bachelor of Business Administration, Hofstra University. Judicial Law Clerk, U.S. Bankruptcy Court, District of Rhode Island. Member of the Rhode Island and Massachusetts Bars, and the Federal Bar for the District of Rhode Island. The author wishes to thank the staff of the Roger Williams University Law Review, past and present, and attorney John P. Barylick for background information and direction. In particular, the author would like to thank her husband, the late Fred S. Hashway, Jr., for doing the math, but most of all, for his firm conviction that she could accomplish anything—including law school in midlife.

1. Excerpts of this article originally appeared in the March/April 2011 Edition of the Rhode Island Bar Journal. John P. Barylick & Jenna Wims Hashway, *Litigation Financing: Preying on Plaintiffs*, R.I. B. J., Mar./Apr. 2011, at 5.

2. Angie Cannon, *Looking for Answers in the Ashes*, U.S. NEWS & WORLD REP., Feb. 8, 2004, at 32, 32.

smallest state.³

Lawsuits follow tragedy as night, the day. Overnight, the Station fire created not only widows, widowers, and orphans, but also a large pool of economically disadvantaged plaintiffs in what promised to be a lengthy litigation. Where most would see only tragedy, one industry spotted opportunity. Late night television ads offering easy cash advances to needy plaintiffs began airing on local television stations. Thus were Rhode Island viewers introduced to the concept of “litigation financing.”

During the last decade, a new industry was born. Litigation financing, the brainchild of a former loan shark,⁴ offers cash advances to plaintiffs during the pendency of their litigation, with the promise that if plaintiffs do not win a judgment or settlement, they owe nothing. If they do win, the loan is repaid from the proceeds of the lawsuit—at interest rates of up to 280%.⁵ If the amount of the judgment is less than the sum owed, the plaintiff ends up with nothing. It is a lousy deal. But plaintiffs who are unable to work in the aftermath of their injuries are at a distinct disadvantage when it comes to waiting years for their cases to be resolved. Litigation Financing Companies (LFCs) argue, not without basis, that their services help level the playing field by allowing plaintiffs to wait out lowball settlement offers from deep-pocketed defendants. But this service comes at an exorbitant cost.

Despite calls for regulation, LFCs operate with no licensing or oversight. Their lending agreements are carefully worded to avoid application of state usury statutes. Some plaintiffs have succeeded in having their loan agreements rescinded in state court⁶ but, to date, LFCs have been able to adapt, and to lobby for legislation that allows them to operate with impunity. The playing field upon which an injured plaintiff and an intransigent defendant meet may be leveled somewhat by cash in the plaintiff's pocket, but the ground beneath LFCs and plaintiff-borrowers is

3. *Id.*

4. Richard B. Schmitt, *Staking Claims: A Las Vegas Lender Tests Odds in Court*, WALL ST. J., Sept. 15, 2000, at A1.

5. See Susan Lorde Martin, *Financing Litigation On-Line: Usury and Other Obstacles*, 1 DEPAUL BUS. & COM. L.J. 85, 98 (2002) [hereinafter Martin, *Usury*].

6. See, e.g., *Echeverria v. Lindner*, 7 Misc. 3d 1019(A), No. 018666/2002, 2005 WL 1083704, at *9 (N.Y. Sup. Ct. Mar. 2, 2005).

far from level or smooth. Legislation is needed to protect plaintiffs from being further victimized as they await the outcome of their litigation. But plaintiffs have no lobbyists.

This article proposes both a model remedial statute to bring litigation lending within the purview of state usury statutes, and a strategy for developing the political will necessary to pass such a statute.

In the wake of mass casualty events like 9/11, the Station Fire, and Hurricane Katrina, there will always be predators who seek to profit from the tragedy of others. It took seven years for the parties in the Station Fire civil litigation to reach a final settlement. In the two years between settlement in principle and disbursement of proceeds, a number of Station Fire victims resorted to litigation advances to make ends meet.⁷ While most took only one or two advances, one widow received thirteen separate advances, totaling \$80,500.⁸ When she received her settlement check, seventeen months after taking the first advance, she was obliged to repay \$137,777, yielding an effective annual percentage rate of 64.7%.⁹

Fortunately, political will can also grow from tragedy. Just as charitable contributions rise in the wake of a tragedy, legislators sometimes rise to propose laws that protect victims. After the Station Nightclub fire, when the scope of liability became apparent, the Rhode Island legislature passed an amendment to the state's joint tortfeasor contribution statute.¹⁰ The statute, in its prior incarnation, posed a substantial impediment to settlement by providing that if one tortfeasor settled, any judgment later obtained against remaining defendants would be reduced by the greater of *either* the dollar amount of the settlement *or* the settling defendant's percentage of fault.¹¹ Because it would be impossible for plaintiffs to predict the eventual percentage-of-fault set-off, it would be too risky for plaintiffs in a lawsuit with scores of defendants to settle with less

7. JOHN BARYLICK, *KILLER SHOW: THE STATION NIGHTCLUB FIRE, AMERICA'S DEADLIEST ROCK CONCERT 227* (forthcoming Sept. 2012).

8. *Id.*

9. *Id.*

10. See R.I. GEN. LAWS § 10-6-8 (Supp. 2011).

11. R.I. GEN. LAWS § 10-6-8 (1997), *amended* by R.I. GEN. LAWS § 10-6-8 (Supp. 2011).

than all of them. To resolve this Catch-22 and enable settlement, the Rhode Island legislature modified the statute so that, in cases where more than twenty-five deaths occur, settlement with one of several joint tortfeasors results in a straight dollar-for-dollar set-off from any future judgment.¹² This statute made it possible for Station Fire plaintiffs to negotiate \$176 million in settlements.¹³

In a similar remedial spirit, this Article discusses the need for bringing litigation financing within the purview of state usury statutes. It begins with a detailed look at the history of this fairly new industry and an overview of how litigation funding works. Part II reviews the recent line of cases challenging litigation loan agreements, attempts at industry regulation, and an agreement made between the New York Attorney General and a consortium of LFCs. Part III examines several litigation loan agreements as a means of assessing how well the industry lives up to its much-touted self-regulation, and reviews the reaction of the litigation financing industry to any attempt to rein in its excesses. Part IV proposes a model remedial statute for addition to states' existing usury statutes, which would clearly define litigation lending as "loans" and bring them within the purview of each state's usury law. This Article concludes by reviewing the recent lobbying efforts of the LFCs and suggesting that state legislators harness the political will created by recent tragedies in order to pass much-needed legislation to protect their constituents from these predatory lenders.

I. BACKGROUND

A. The History of Litigation Financing

Litigation financing is a relatively new industry: born in the 1990's, it grew rapidly, in part due to the effectiveness of internet advertising.¹⁴ Because LFCs are not regulated like banks,

12. See R.I. GEN. LAWS § 10-6-8 (Supp. 2011).

13. Tracy Breton, *Judge Approves Settlement for Fire Victims; Station Fire*, PROVIDENCE J., Jan. 8, 2010, at 5; see also Alexandria E. Baez, Comment, *Joint Tortfeasors, Full Compensation, and the 1,800 Degree Crucible: Rekindling Rhode Island's Uniform Contribution Among Tortfeasors Act in the Aftermath of the Station Nightclub Fire*, 12 ROGER WILLIAMS U. L. REV. 386, 387 (2007).

14. Susan Lorde Martin, *Litigation Financing: Another Subprime Industry that has a Place in the United States Market*, 53 VILL. L. REV. 83, 83

industry figures are hard to come by.¹⁵ The American Legal Finance Association (ALFA), a trade group that represents twenty of the largest LFCs does not disclose industry figures beyond claiming that their members have originated ninety percent of currently outstanding legal funding.¹⁶

The origins of the industry are perhaps more illuminating. Perry Walton, a Las Vegas entrepreneur, is the godfather of litigation financing. Following a career that included stints as a rock musician and mobile-home park developer, Walton made his first foray into extortionate lending with a business he named Wild West Funding.¹⁷ In 1997, after several of Walton's borrowers complained that they were threatened when they fell behind in their loans, a police investigation resulted in Walton's pleading guilty to "extortionate collection of debt."¹⁸ Walton drew a sentence of eighteen months of probation, and by the following year, he had hit upon a somewhat more legitimate lending opportunity.¹⁹

Dubbing his new business Future Settlement Funding Corp., Walton began loaning money to plaintiffs, structuring these advances as "contingent obligations" in order to sidestep usury laws.²⁰ He then invited would-be lenders to seminars, charging as much as \$12,400 to impart the secret of his lucrative new scheme.²¹ Two years later, 400 people had been trained by Walton, and a new subprime industry was born.²²

The precise size of this industry today is impossible to gauge.²³ Barriers to entry are almost nonexistent: with no

(2008) [hereinafter Martin, *Subprime*].

15. *See id.* at 101.

16. *Facts About ALFA*, AM. LEGAL FIN. ASS'N, <http://www.americanlegalfin.com/FactsAboutALFA.asp> (last visited Mar. 11, 2012).

17. Schmitt, *supra* note 4.

18. *Id.*

19. *Id.*

20. *Id.*

21. *Id.*

22. *See id.* Walton has engaged in litigation financing under several business names, including: Law Finance Group, Inc., Resolution Settlement Corp., and Future Settlement Funding. *See* Julia H. McLaughlin, *Litigation Funding: Charting a Legal and Ethical Course*, 31 VT. L. REV. 615, 619 & n.11 (2007); Yifat Shaltiel & John Cofresi, *Litigation Lending for Personal Needs Act: A Regulatory Framework to Legitimize Third Party Litigation Finance*, 58 CONSUMER FIN. L. Q. REP. 347, 347 (2004); Schmitt, *supra* note 4.

23. McLaughlin, *supra* note 22, at 622.

licensing requirements, all a prospective lender needs is a website and fairly modest capitalization.²⁴ A Google search of the phrase “litigation financing company” returns over 100,000 hits. Clearly, in the years since Walton began his seminars, the number of LFCs has grown exponentially.

B. How Litigation Financing Works

A plaintiff who is short on cash is only a few keystrokes away from what can appear to be an easy, painless solution to his problem. A visit to ALFA-member LawCash’s website features a television ad that promises that a call to 1-800-LAW-CASH “will get you money right now.”²⁵ Oasis Legal Finance asks “do you need cash today?” and promises that “no one can get you cash faster.”²⁶ The U.S. Claims site offers plaintiffs a “no risk agreement – no recovery means no repayment.”²⁷ All of these sites offer pre-settlement and pre-judgment cash advances, which plaintiffs can use to cover personal expenses. These loans are later repaid from the proceeds of the judgment or settlement, and if the case is lost or does not settle, the plaintiff owes nothing.²⁸

To begin the process, a plaintiff need only fill out a short online application. The lender then evaluates the plaintiff’s case by assessing the following factors: the presence of a skilled plaintiff’s attorney; access to the litigation file; the plaintiff’s potential liability; in car accident cases, the extent of damage to the vehicle; “bright blood injuries;” medical bills; and a proprietary statistical analysis of jury verdicts in comparable cases.²⁹ The plaintiff must waive her attorney-client privilege in order for the lender to contact her attorney to obtain information necessary to assess the strength of her case.³⁰ If the loan is approved, the

24. Martin, *Subprime*, *supra* note 14, at 104-05.

25. LAW CASH, <http://www.lawcash.net> (click “LawCash As Seen On TV” to play video on homepage) (last visited Apr. 9, 2012).

26. OASIS LEGAL FINANCE, <http://www.oasislegal.com> (last visited Mar. 11, 2012).

27. U.S. CLAIMS, <http://www.usclaims.com/how-we-work> (last visited Mar. 11, 2012).

28. Courtney R. Barksdale, Note, *All That Glitters Isn’t Gold: Analyzing the Costs and Benefits of Litigation Finance*, 26 REV. LITIG. 707, 712-13 (2007).

29. Shaltiel & Cofresi, *supra* note 22, at 348.

30. See Barksdale, *supra* note 28, at 714.

lender generates a litigation lending agreement (LLA), and once the LLA is executed by the plaintiff and her attorney, the lender expedites funds to the plaintiff.³¹ Then, the meter begins to run.

The ease and speed with which a plaintiff can enter into an LLA has caused at least one commentator to observe that this “instant gratification” may “encourage or facilitate poor financial management.”³² This is particularly troubling when one compares the plain language and short form of a typical LFC’s online application to the fine print of the multi-page LLA.³³ The LawCash online application is straightforward and, in addition to name, address, and attorney information, requests basic information about the plaintiff’s accident claim.³⁴ The language in the LLA, however, is far less clear:

The monthly use fee shall be a charge in an amount equal to 3.10% monthly of the amount funded to me herein. This funded amount includes the Application Fee that I agreed to when first applying for this funding. . . . The monthly use fee is charged from this date until the end of the 5 month interval during which payment of proceeds is made to LAWCASH. In the case of multiple fundings, then these fees shall accrue on each funded sum from the date of each individual funding.³⁵

Plaintiff/borrowers familiar with credit card agreements would be surprised to learn that for many borrowers the above paragraph would be the closest they would come to learning the Annual Percentage Rate (APR) of their loan.

The federal Truth in Lending Act (TILA) was enacted with the goal of protecting consumers by giving them access to information necessary to making informed decisions about acquiring and using credit.³⁶ LFCs are not required to adhere to

31. Lauren J. Grous, Note, *Causes of Action for Sale: The New Trend in Legal Gambling*, 61 U. MIAMI L. REV. 203, 210 (2006).

32. Shaltiel & Cofresi, *supra* note 22, at 349.

33. See *LawCash Advance Application*, LAWCASH, <http://www.lawcash.net/html/application.html> (last visited Mar. 11, 2012); *LawCash Funding Agreement* (Aug. 27, 2009) (on file with author).

34. See *LawCash Advance Application*, LAWCASH, <http://www.lawcash.net/html/application.html> (last visited Mar. 11, 2012).

35. *LawCash Funding Agreement*, *supra* note 33.

36. Truth in Lending Act (TILA), 15 U.S.C. § 1601(a) (2006).

TILA because they are not considered “creditors,” as defined by the Act.³⁷ If LFCs, like credit card companies, were required to follow TILA regulations, the APR paid by the borrower would need to be spelled out clearly in the LLA.³⁸ It is highly doubtful that a plaintiff could divine the APR from the paragraph quoted above. Given the familiarity consumers have with APRs from their widespread use in advertising and on credit card billing statements, it is even possible that a plaintiff/borrower could mistake the 3.10% *monthly* rate for an APR. This would be a dire mistake, as the actual APR for these loans, which would vary greatly depending on when the loan is repaid, could amount to anywhere between 58% and 120%.³⁹ APRs from other LFCs can exceed 200%.⁴⁰

Given the promise of “no risk”⁴¹ and the fact that the plaintiff will not be obligated to pay unless there is a judgment or settlement, it is unlikely that the plaintiff will worry too much about the rapidly accruing interest rate until the case has ended. By that time, when she discovers that a large portion (or even the entirety of her award) is payable to the LFC, she will have little recourse. LLAs are structured so that the LFC is paid by the plaintiff’s attorney before any other funds are disbursed from the client’s portion of the settlement or judgment.⁴² This is possible because, as previously noted, the attorney, as well as the plaintiff, is a signatory to this agreement.⁴³

The litigation financing industry attempts to rationalize the enormous interest charged by claiming that it provides a much-needed service to plaintiffs and, in so doing, LFCs assume a high degree of risk that justifies their reaping a high profit. Proponents of the industry argue that this funding helps “level[] the playing field” for plaintiffs.⁴⁴ “We look at ourselves as the

37. *See id.* § 1602(f).

38. *Id.* § 1632.

39. LawCash Funding Agreement, *supra* note 33.

40. *See* Fausone v. U.S. Claims, Inc., 915 So. 2d 626, 627 (Fla. Dist. Ct. App. 2005); McLaughlin, *supra* note 22 at 621.

41. *See, e.g.*, U.S. CLAIMS, <http://www.usclaims.com/how-we-work> (last visited Mar. 11, 2012).

42. LawCash Funding Agreement, *supra* note 35.

43. *See id.*

44. Martin, *Subprime*, *supra* note 14, at 85.

guys with the white hats," said industry founder Perry Walton.⁴⁵ White hats and level playing fields aside, what lurks beneath is far from commendable.

The LawCash Funding Agreement solicits the borrower's agreement with the LFCs' justification for the interest rate commanded. Recital C of the agreement states: "I have been advised that I should not accept this funding if I have any other alternative to meet my immediate economic needs. Because LAW CASH is taking a high risk in giving me this funding, I understand that LAW CASH may make a large profit."⁴⁶

But how can we quantify, or even verify, this "high risk?" Unlike credit cards, this is not unsecured debt; the LFC holds a security interest in the proceeds of the lawsuit.⁴⁷ The risk, therefore, is not whether the borrower will default on the loan, but whether the lawsuit will result in a settlement or judgment. At first glance, lending on the basis of a lien against litigation proceeds may appear to be risky, but the industry's unregulated status makes assessing the actual risk difficult.⁴⁸ There are clues, however, that the risk is far lower than portrayed by the industry. First, LFCs carefully analyze applicants' cases and accept only those that they deem to have a high likelihood of recovery.⁴⁹ Furthermore, because plaintiffs' attorneys who work on a contingent fee basis screen their potential cases and accept only those with a high likelihood of success; the LFC is actually performing a secondary credit determination.⁵⁰ LFCs mitigate their risk considerably through this process. One LFC funded only ten percent of the \$250 million in loan applications it received over a two-year period.⁵¹

Perhaps the most revealing information regarding LFCs' actual level of risk was imparted by Harvey Hirschfeld, President of LawCash and Chairman of ALFA, in an interview with Crain's New York Business.⁵² LawCash targets lawsuits in the

45. Schmitt, *supra* note 4.

46. LawCash Funding Agreement, *supra* note 33.

47. *Id.*

48. Martin, *Subprime*, *supra* note 14, at 101.

49. See Barksdale, *supra* note 28, at 726.

50. See Shaltiel & Cofresi, *supra* note 22, at 348.

51. Barksdale, *supra* note 28, at 727.

52. See Christina Merrill, *Judgment Call: Firms That Lend to Personal-Injury Plaintiffs Take Steps to Improve Their Bad-Guy Image*, CRAIN'S N.Y.

“midresolution” stage, thereby increasing the likelihood that the case will be resolved in less than two years.⁵³ Cases in which at least initial settlement offers have been made are much more likely to eventually settle than are those with no offers pending. It is doubtful that LFCs fund many “must-be-tried” cases.

LawCash limits its exposure to advancing up to ten percent of the settlement value of a case.⁵⁴ But the one disclosure that shed the most light on the actual level of risk involved was the admission that LawCash “uses strict underwriting screening rules that ensure only about 4% of the cases it advances money on are lost in court.”⁵⁵ Another industry figure, Michael Douglas, CEO of ExpertFunding.com, put his company’s default even lower, at only two percent.⁵⁶

Despite such caution (or perhaps because of it), LawCash has prospered. The LFC projected that its case portfolio of three million dollars in 2001 would swell to between twenty-five and thirty million dollars in 2004.⁵⁷ More recent figures are unavailable, and in the wake of the Crain’s report, industry leaders now find that it is wiser not to comment about their relatively low loss history. Anecdotally, plaintiffs’ lawyers in Massachusetts note that litigation financing is booming there, possibly due to the recent economic downturn.⁵⁸

What seems clear is that the bloated profits available to LFCs, and the low barriers to entry, have transformed the business once termed “the Wild West of finance”⁵⁹ from a fringe industry into an established branch of the financing sector (albeit one that enjoys freedom from regulation). At last count, there

BUS., Jan. 27, 2003, at 1.

53. *Id.*

54. *Id.*

55. *Id.*

56. Mike France, *The Litigation Machine*, BUS. WK. (Jan. 29, 2001), http://www.businessweek.com/2001/01_05/b3717011.htm?scriptFramed.

57. Diane E. Lewis, *With Interest Accident Victims Get Money from “Advance Funders”*, BOS. GLOBE, Oct. 2, 2003, at C1.

58. See generally Julia Reischel, *As Pre-Settlement Financing Takes Hold in Massachusetts, Lawyers Spar Over Pros and Cons*, MASS. LAW. WKLY, July 28, 2008.

59. Susan Lorde Martin, *The Litigation Financing Industry: The Wild West of Finance Should be Tamed Not Outlawed*, 10 FORDHAM J. CORP. & FIN. L. 55, 55 (2004) [hereinafter Martin, *Wild West*] (citation omitted) (internal quotation marks omitted).

were at least a hundred LFCs operating in the United States,⁶⁰ and, if Google is any indicator, far more than that. As the litigation financing industry grows, so will the number of plaintiffs who find themselves handing over most or all of their awards in return for having fairly brief use of a cash advance—only slightly over a year according to LawCash’s Hirschfeld.⁶¹ The time has come to protect injured plaintiffs from LFCs’ excesses. In order to design a workable means of reining in these purported white hats, it is useful to take a look at recent developments in case law and state law.

II. THE DEBATE OVER REGULATING LITIGATION FINANCING

Commentators have proposed various approaches for dealing with the litigation financing industry. Professor Susan Lorde Martin has called it “a new business worth preserving” and advocates licensing LFCs, requiring full disclosure of their fees, and allowing competition to bring down the rates.⁶² Others assert that usury laws should not apply to LFCs because these loans leave plaintiffs “no-worse-off” (no more likely to become a burden on the state).⁶³ Some caution that LLAs, which require the signature of the plaintiff’s attorney as well as a waiver of attorney-client privilege, expose lawyers to potential ethical and malpractice issues.⁶⁴ Still others advocate bringing LFCs under the umbrella of TILA or crafting comprehensive regulations that would specifically target the litigation financing industry.⁶⁵

60. Grous, *supra* note 31, at 236.

61. Lewis, *supra* note 57.

62. Martin, *Usury*, *supra* note 4, at 102; *see generally* Martin, *Subprime*, *supra* note 14; Martin, *Wild West*, *supra* note 59.

63. George Steven Swan, *The Economics of Usury and the Litigation Funding Industry: Rancman v. Interim Settlement Funding Corp.*, 28 OKLA. CITY U.L. REV. 753, 783 (2003).

64. Richard H. Braun, *Settle Now, Pay Later: A Caution About Personal Injury Loans*, OR. ST. B. BULL. May 2002, at 9, 9; *see also* COMM’N ON ETHICS, AM. BAR ASS’N, INFORMATIONAL REPORT TO THE HOUSE OF DELEGATES 4 (2012), available at http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111212_ethics_20_20_alf_white_paper_final_hod_informational_report.authcheckdam.pdf (noting that “lawyers must approach transactions involving alternative litigation finance with care, mindful of several core professional obligations” including the obligations to exercise independent judgment, safeguard against waiver of attorney-client privilege, and fully explain the terms and risks of funding transactions).

65. *See* Shaltiel & Cofresi, *supra* note 22; *see also* Martin, *Subprime*,

Efforts to use the common law proscriptions against champerty and maintenance have met with mixed results.⁶⁶ After considering attempts to challenge LLAs in state and federal courts, this article advocates amending usury statutes to bring LFCs within their purview. A review of recent case law will be helpful in crafting a statute that will allow plaintiffs continued access to funding, while protecting them from the predatory excesses of the industry.

A. From *Rancman* to *Odell*, an Overview of Recent Caselaw

The Supreme Court of Ohio fired the first successful shot in the battle against LFCs' triple digit interest rates. In *Rancman v. Interim Settlement Funding Corp.*, a plaintiff who had been injured in a car accident received an advance from the defendant while she awaited the resolution of her case.⁶⁷ Within a year of taking out the advance, she settled her case.⁶⁸ When her settlement arrived, instead of remitting payment according to the terms in her LLA, she tendered the principal plus eight percent interest and filed suit seeking rescission of the LLA on grounds of "unfair, deceptive, and unconscionable sales practices."⁶⁹ The trial court found that the transaction violated Ohio's usury statute and the Court of Appeals affirmed.⁷⁰

On appeal to the Supreme Court of Ohio, the defendant argued that the transaction was not a loan, but an "investment," and thus did not fall under the usury statute.⁷¹ The court ducked the usury question altogether, turning instead to the doctrine of champerty. Champerty is a form of maintenance in which someone with no personal interest in a lawsuit gives financial support to a plaintiff in exchange for part of the proceeds of the litigation.⁷² Champerty was prohibited at common law because it was feared that such arrangements would foster frivolous lawsuits

supra note 14, at 114-116.

66. See generally *Saladini v. Righellis*, 687 N.E.2d 1224 (Mass. 1997); *Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217 (Ohio 2003).

67. 789 N.E.2d at 218-19.

68. *Id.* at 219.

69. *Id.*

70. *Id.*

71. *Id.*

72. *Barksdale*, *supra* note 28, at 716.

and protracted litigation.⁷³ The *Rancman* court stated, “[i]t is unnecessary for the resolution of this case to determine the threshold level of risk necessary for a contingent advance to be treated as an investment rather than a loan. The advances here are void as champerty and maintenance regardless of whether they are loans or investments.”⁷⁴

This holding sent a shockwave through the industry. After *Rancman*, LFCs would continue to argue that their advances are not loans, but rather, “investments;” however, in the future, LLAs would also be carefully drafted to account for *Rancman*’s change to the legal landscape. One such LLA attempts to avoid *Rancman*’s pitfall by reciting:

Certain jurisdictions prohibit “Champerty”. Basically, champerty makes it illegal for an individual or company to acquire someone else’s right to sue. In entering into this agreement, the parties acknowledge that LAWCASH is in no way acquiring my right to sue; that I have already started the Lawsuit; that the Lawsuit absolutely belongs to me and no one else; and that LAWCASH will in no way be involved in the decisions that me and my attorney(s) make in connection with the Lawsuit. This is an investment and not a loan, but should a Court of competent jurisdiction construe it to be the latter, then I agree that interest shall accrue at the maximum rate permitted by law.⁷⁵

Notwithstanding *Rancman*, the promise of applying the nineteenth century doctrine of champerty to plaintiffs/borrowers seeking rescission of LLAs remains uncertain. Some states, including Massachusetts and South Carolina, have expressly held that champerty is no longer recognized.⁷⁶ Others, like Florida and Mississippi, have declined to hold that LLAs constitute champerty.⁷⁷ While Alabama, Minnesota and Nevada have found LLAs to be champertous, the majority of states have not yet

73. *Id.*

74. 789 N.E.2d at 219.

75. LawCash Funding Agreement, *supra* note 33.

76. Barksdale, *supra* note 28, at 717-720.

77. *Id.* at 718.

addressed the issue.⁷⁸

In cases brought after *Rancman*, other state courts addressed the issue that the Ohio Supreme Court sidestepped, namely, the definition of “loan” for purposes of a usury statute. In *Lawsuit Financial, LLC v. Curry*, the defendant was injured in a car accident, sued the responsible party, and received a verdict in her favor in the amount of twenty-seven million dollars.⁷⁹ After the verdict, and while awaiting proceedings regarding a motion for remittitur, the tort plaintiff sought and received three contingent advances from Lawsuit Financial for a total of \$177,500.⁸⁰ The first advance was made on April 19, 2000, and the last on October 19 of that year.⁸¹ In exchange for the use of these funds, under its LLA, Lawsuit Financial would receive either \$887,500 or ten percent of the proceeds of the lawsuit, whichever was greater.⁸² Final judgment for \$4.79 million was entered on December 22, 2000.⁸³ For the tort plaintiff’s use of \$177,500 over nine months, Lawsuit Financial demanded \$887,500.⁸⁴

When Curry’s attorney failed to remit these funds, Lawsuit Financial sued Curry for conversion, and her attorney for abetting that conversion.⁸⁵ Curry moved for summary judgment, claiming that the transactions were usurious loans with interest rates between 200% and 370%.⁸⁶ Lawsuit Financial argued that the advance was not a loan (and therefore, not usurious) because the lender bore at least some risk of nonpayment due to the \$1.2 million Ms. Curry owed to a superior lienholder, as well as her attorney’s contingent fee.⁸⁷ The court expressly rejected the LFC’s argument, and granted defendant Curry’s motion.⁸⁸

On appeal, the Michigan court took a closer look at the

78. *Id.* at 721-23.

79. 683 N.W.2d 233, 236-37 (Mich. Ct. App. 2004).

80. *Id.* at 236.

81. *Id.*

82. *Id.*

83. *Id.* at 239.

84. *Id.* at 236.

85. *Id.* The claim against Curry’s attorney was dismissed because the attorney had lawfully received the judgment proceeds and “property that rightfully comes into a defendant’s possession is not converted just because another claims a right to it.” *Id.* at 237.

86. *Id.*

87. *Id.* at 238.

88. *Id.*

definition of loan. It stated that the word “loan” implies an absolute right of repayment.⁸⁹ While the plaintiff LFC argued that the transaction was a contingent advance, the court concluded that “[d]espite that language in the agreements . . . the right to repayment was absolute because the parties entered into those agreements long after the defendants in the underlying personal injury suit admitted liability and after the jury returned a verdict of \$27 million in damages.”⁹⁰ The court further observed that Curry was certain to recover some damages and that the agreement did not make plain that Lawsuit Financial would receive nothing unless Curry recovered over \$2.3 million (an amount sufficient to pay off the superior lienholder as well as her attorney’s contingent fee).⁹¹ Judgment for the defendant/borrower was affirmed, and the LFC was barred by Michigan’s usury statute from recovering interest, fees, late charges, and attorney’s fees.⁹²

What seemed clear after *Lawsuit Financial LLC* was that courts would make a fact-specific inquiry in determining whether a contingent advance is a loan. New York followed this path in *Echeverria v. Lindner*, when the Supreme Court of Nassau County assessed whether a LawCash advance was a loan.⁹³ The plaintiff in *Echeverria*, a day laborer, was severely injured in a workplace accident.⁹⁴ He was not covered by his employer’s worker’s compensation insurance.⁹⁵ In order to pay for the surgery necessitated by his injuries, the plaintiff borrowed \$25,000 from LawCash at the rate of 3.85% per month, compounded monthly.⁹⁶ After three of the defendants settled and the fourth defaulted, a hearing was held to assess damages.⁹⁷ The plaintiff argued that by failing to provide him with Worker’s Compensation insurance,

89. *Id.* at 239.

90. *Id.*

91. *Id.* at 240.

92. *Id.*

93. 7 Misc. 3d 1019(A), No. 018666/2002, 2005 WL 1083704, at *1 (N.Y. Sup. Ct. Mar. 2, 2005).

94. *Id.*

95. *Id.* at *2.

96. *Id.* The interest on this advance accrued at a rate of \$48.94 per day. Mr. Echeverria, prior to his injury, earned between seventy-five and eighty dollars per day. *Id.* at *4.

97. *Id.* at *1.

the defendants forced him to seek a lender of last resort to pay for his medical bills, and thus the cost of his funding should be included in his damages.⁹⁸

Referencing *Rancman*, the *Echeverria* court noted that while the transaction in that suit was champertous in Ohio, due to a difference in the New York champerty statute, the *Echeverria* advance did not constitute champerty.⁹⁹ Unlike Ohio, which tolerates “no lien . . . which . . . encourages, promotes, or extends litigation,” New York law permits assignments as long as their primary purpose is profit, not bringing suit.¹⁰⁰ However, the New York court looked askance at the argument that LLAs are “an investment” rather than a loan, stating:

While there may be no cap on the return on an investment, most investors do not get to set the amount of that return. Usually, either the party receiving the investment tells the investor what the rate of return will be, or nobody knows. In this latter case investors will forecast their return, but they can’t demand it. Banks set the return they expect from their loans, through interest rates, which is more comparable to what we have here.¹⁰¹

In finding that the transaction was a loan, the court stated that “it is ludicrous to consider this transaction anything else but a loan unless the court was to consider it legalized gambling.”¹⁰² The court further noted that, because the case at bar was a strict liability labor law action, there was a “very low probability” that the plaintiff would not recover; thus, LawCash bore almost no risk, rendering the transaction less a gamble than a “sure thing.”¹⁰³

Mindful that LawCash “justified” its high interest rates by claiming to bear a high risk, the court held that LawCash was lending money at an “obviously usurious rate.”¹⁰⁴ The court vitiated the agreement and held that LawCash could recover only

98. *Id.* at *3.

99. *Id.* at *6.

100. *Id.*

101. *Id.* at *5 n.1.

102. *Id.* at *8.

103. *Id.*

104. *Id.* at *1.

the principal and costs of the transaction, as well as a (non-usurious) interest rate of 16% per annum.¹⁰⁵ Further, these funds would be recoverable from the tort defendant because it was the defendant's failure to furnish Worker's Compensation insurance that caused the plaintiff to take out the loan.¹⁰⁶

After *Echeverria*, the question in similar cases would turn from, "is this champerty?" to, "what is a loan?" In particular, courts would consider the actual risk involved in these putative high risk investments to determine whether the advances were truly contingent and whether the LFC bore any significant risk of nonpayment.

The Circuit Court of Michigan addressed this issue in *Vinch v. Lawsuit Financing, Inc.*, where the plaintiff argued that the defendants' access to documents regarding the underlying litigation allowed them to be assured that their advance would be repaid.¹⁰⁷ The defendant LFC argued that, at the time it entered the agreement, the outcome of the underlying litigation was unknown.¹⁰⁸ Under the terms of the LLA, in exchange for an advance of \$10,000, the LFC would receive 100% of the plaintiff's recovery up to a maximum of \$50,000.¹⁰⁹ Eleven months after signing the LLA, the plaintiff received an arbitration award of only \$65,867.15.¹¹⁰

In enforcing the LLA, the *Vinch* court referenced *Lawsuit Financial, LLC v. Curry*, holding that the transaction was a "contingent advance," and not a loan.¹¹¹ The *Curry* court had earlier said that "the hallmark of a loan is the *absolute* right to repayment."¹¹² The Michigan court distinguished *Vinch* from *Curry* because a verdict had already been rendered in the plaintiff's litigation in *Curry*, whereas liability was still at issue in the underlying case in *Vinch* at the time the advance was made.¹¹³ Therefore, because there was still a possibility that the defendant

105. *Id.* at *8.

106. *Id.*

107. No. 2004-3963-CK, slip op. at 2-3 (Mich. Cir. Ct. Aug. 26, 2005).

108. *Id.* at 2.

109. *Id.* at 3.

110. *Id.* at 2.

111. *Id.* at 4-5.

112. *Id.* at 4. (quoting *Lawsuit Financial, LCC v. Curry*, 683 N.W.2d 233, 239 (Mich. Ct. App. 2004)).

113. *Id.*

LFC in *Vinch* would recover nothing under the LLA, the court held that the LLA was a “contingency agreement and not a loan.”¹¹⁴ The careful construction of the LLA as a “contingency agreement” put the transaction outside the reach of Michigan’s usury statute, which, under Michigan law, required a transaction to be absolutely repayable in order for the statute to apply.

It seemed that Perry Walton’s scheme, propounded to would-be litigation funders at a number of seminars, would prove to be a workable end-run around the usury statute, as long as the circumstances of the transactions were such that, at least arguably, the LFC bore some risk that its advance would not be repaid.

Walton’s brainchild would see its next test in *Fausone v. U.S. Claims, Inc.*¹¹⁵ The plaintiff in *Fausone* was injured when the bicycle she was riding was struck by a dump truck.¹¹⁶ During the pendency of her litigation, the plaintiff sought several advances in small amounts from different LFCs.¹¹⁷ She then contacted defendant U.S. Claims and consolidated her earlier loans at more favorable terms.¹¹⁸ She later sought additional advances from the defendant, for a total amount of \$30,000.¹¹⁹ The plaintiff settled her personal injury claim for an amount in excess of \$200,000.¹²⁰ According to her repayment schedule at the time, she then owed U.S. Claims \$50,937.¹²¹

The plaintiff instructed her attorney not to remit payment to the defendant, who then initiated arbitration in accordance with the terms of the LLA.¹²² In response, the plaintiff sought a declaratory judgment in Florida that the LLA was unconscionable, that the interest rate was usurious and that she should not be compelled to arbitrate.¹²³ The trial court stayed her claim, pending arbitration.¹²⁴ Despite being offered the opportunity to

114. *Id.* at 5.

115. 915 So.2d 626 (Fla. Dist. Ct. App. 2005).

116. *Id.* at 627.

117. *Id.*

118. *Id.* at 628.

119. *Id.*

120. *Id.* at 629.

121. *Id.*

122. *Id.*

123. *Id.*

124. *Id.*

appear via telephone, the plaintiff failed to participate in the arbitration and U.S. Claims was awarded \$72,117.¹²⁵ Plaintiff first sought to vacate the arbitration award, but then declined to proceed with her motion to vacate.¹²⁶ After the court confirmed the arbitration award, the plaintiff appealed.¹²⁷

Noting that there were few, if any issues preserved for appeal, and no demonstration by the plaintiff that the LLA could be invalidated under Florida law, there was little the court could do.¹²⁸ However, the court was clearly uncomfortable with the concept of litigation funding, explaining that the opinion would delve into the facts of the case in some detail “because this method of litigation funding may warrant regulation in Florida.”¹²⁹

The *Fausone* court noted the need for personal injury plaintiffs to be able to access money to support themselves and their families while litigation is pending, but made clear its concern that plaintiffs could be victimized by LFCs charging interest rates that are greatly in excess of their level of risk.¹³⁰ Referring to U.S. Claims, the court stated, “a company that only loaned money when it was secured by high-grade personal injury claims would seem to be able to charge a lower interest rate than some of the rates described in this opinion, even when the arrangement is a nonrecourse loan.”¹³¹

The court expressed similar displeasure with the mandatory arbitration clause, (which is common to many LLAs), stating:

The purchase agreement in this case is one-sided and designed to prevent a Florida citizen from having access to a local court or another local dispute resolution forum. Such agreements create confusion concerning the party who actually owns and controls the lawsuit, and creates risks that the attorney-client privilege will be waived

125. *Id.*

126. *Id.*

127. *Id.* The court noted that throughout the arbitration proceeding, the plaintiff had not been represented by a lawyer but had instead been assisted by a nonlawyer doing business under the name, “Cheaper than a Lawyer.” *Id.* A dubious moniker, given the outcome of this case.

128. *Id.*

129. *Id.* at 627.

130. *Id.* at 630.

131. *Id.*

unintentionally.¹³²

The court ended its opinion by calling on the legislature to “examine this industry to determine whether Florida’s citizens are in need of any statutory protection.”¹³³

While seemingly another victory for the LFCs, *Fausone* can be seen as a warning to the litigation funding industry. Confronted with perhaps not the most sympathetic plaintiff, in affirming the award to the defendant, the Florida court still went to great lengths to express its concerns regarding litigation funding, and its hope that the Florida state legislature would rein in the excesses of the industry.¹³⁴

Perhaps Walton’s invention is not entirely bullet-proof. North Carolina, a state with one of the more consumer-protective usury statutes, would see the next challenge to LFCs. In *Odell v. Legal Bucks, LLC*, a plaintiff injured in a car accident expected to realize at least \$30,000 from her claim, but as with many personal injury plaintiffs, she had an immediate need for a small amount of money to tide her over until her case was settled.¹³⁵ The plaintiff sought \$3000 from the defendant LFC, and signed an LLA on March 28, 2003, in which she agreed to the following repayment schedule: \$4200 prior to July 1, 2003, or after that date, \$4200 plus \$234 for each month thereafter until the advance was repaid, up to a maximum of \$9750 (which would amount to 325% of the principal advanced).¹³⁶ As with other LLAs, if the plaintiff recovered nothing in her suit, she would not owe the defendant LFC anything.¹³⁷

The tort plaintiff’s claim was settled in May 2005 for \$18,000; at that time she owed the LFC \$9582—just shy of the contractual maximum.¹³⁸ Instead of repaying the loan, the plaintiff filed a claim against the defendant LFC alleging, *inter alia*, that the LLA

132. *Id.*

133. *Id.*

134. *Id.* at 627-630. After all, the plaintiff there had sought and received a number of advances and failed to participate in the arbitration of her claim. *Id.* at 627, 629.

135. 665 S.E.2d 767, 770 (N.C. Ct. App. 2008).

136. *Id.* at 770-71.

137. *Id.* at 771.

138. *Id.*

was both champertous and usurious.¹³⁹ Both the plaintiff and the defendant filed motions for summary judgment and the trial court found for the defendant LFC.¹⁴⁰ The court awarded the defendant \$29,250 plus post-judgment interest, and the plaintiff appealed.¹⁴¹

On appeal, the plaintiff first argued that the LLA was champertous because it gave the LFC a level of control over borrowers' lawsuits.¹⁴² The defendant appeared to accede to this reasoning when its representative testified that the LFC had reduced the amount of its lien in prior cases in order to facilitate settlement when parties were otherwise unable to reach agreement due to the size of the LFC's lien.¹⁴³ However, the court held that there is a distinction between the assignment of a claim for personal injury and the assignment of the *proceeds* of the claim, and that an assignment of the proceeds does not give the assignee sufficient control over the case to constitute champerty.¹⁴⁴

The plaintiff fared better with her second argument, however, that the advance fell within the ambit of the North Carolina usury statute, despite the fact that repayment was contingent upon recovery on her claim.¹⁴⁵ To prevail on a claim of usury in North Carolina, a plaintiff must prove four elements:

1. A loan or forbearance of money, either express or implied.
2. An understanding between the parties that the principal *shall be or may be* returned.
3. That for such loan or forbearance a greater profit than is authorized by law shall be paid or agreed to be paid.
4. That the contract is entered into with an intention to violate the law.¹⁴⁶

139. *Id.*

140. *Id.* at 772.

141. *Id.*

142. *Id.* at 774. The plaintiff argued that control was established because borrowers would likely reject any settlement offer that amounted to less than the amount owed to the LFC. *Id.*

143. *Id.*

144. *Id.*

145. *Id.* at 776-77.

146. *Id.* at 778.

The defendant LFC, relying on early North Carolina case law, argued that usury is involved only in transactions where the obligation to make repayment is not subject to any contingency.¹⁴⁷ Under the defendant's theory, North Carolina usury law required an absolute obligation to repay the lender.¹⁴⁸ However, the court cited cases from the same period defining the second element of usury as "[a]n understanding between the parties that the principal *shall be or may be returned*."¹⁴⁹ The court noted that, unlike the usury statutes in some other states, North Carolina's statute specifically covered loans in which repayment may be conditional.¹⁵⁰ The court further referenced the legislature's inclusion in the statute of both the terms "loan" and "advance" to imply "at least two distinct types of transaction."¹⁵¹ In holding that the LLA was a usurious transaction, the appellate court noted that the contract did not excuse the plaintiff/borrower from paying the amount owed, but simply provided that if she were to recover less than the sum advanced, the "money owed' under the Agreement would be as little as zero dollars."¹⁵²

Thus, with that neat bit of linguistic gymnastics, the court reversed the trial court's grant of summary judgment for the defendant and found the LLA to be invalid and unenforceable.¹⁵³ Reading between the lines of the opinion, it seems clear that the North Carolina court was bending over backward to read the usury statute in a manner that would protect the plaintiff from the excesses of LFCs.

More recently, the usurious nature of LLAs was addressed by a U.S. Bankruptcy Court. There, a bankruptcy trustee sought authorization to compromise a Chapter 7 debtor's personal injury claim.¹⁵⁴ In the wake of an auto accident, the debtor had taken four advances from Pre-Settlement Finance ("PSF") totaling \$18,600.¹⁵⁵ By the time her case settled, the debtor owed PSF over \$32,000, with interest calculated at an annual rate of

147. *Id.* at 777.

148. *Id.*

149. *Id.* at 778.

150. *Id.*

151. *Id.*

152. *Id.*

153. *Id.* at 781.

154. *In Re Minor*, 443 B.R. 282, 284 (Bankr. W.D.N.Y. 2011).

155. *Id.*

42.5%.¹⁵⁶ The bankruptcy court refused to find that the settlement was reasonable and in the best interests of the bankruptcy estate, stating that “[e]ven outside bankruptcy, the validity of PSF’s legal argument is highly suspect for at least three reasons”: first, the LLA was ambiguous as to whether the transaction was an assignment or a loan; second, New York courts, following *Echeverria* look to the “underlying essence of the transaction” in determining whether an agreement is usurious; and third, the LLA “suggests the potential defense of unconscionability.”¹⁵⁷ Noting that “[o]n their face, the pre-settlement loan agreements are troublesome and perhaps even predatory,” and describing the debtor as “an individual with limited income and few resources,” the court invoked the doctrine of unconscionability as “primarily a means with which to protect the commercially illiterate consumer beguiled into a grossly unfair bargain by a deceptive vendor or finance company.”¹⁵⁸ It is unclear whether an Article III court would take up unconscionability in a future challenge to an LLA, but it seems likely that pro-consumer bankruptcy courts will view these lending agreements with a jaundiced eye.

In reviewing the landscape from *Rancman* to *In Re Minor*, two features stand out: the poor fit of champerty as a means to void LLAs, and the judiciary’s disdain for these loans. Perhaps the specter of greedy LFCs charging injured plaintiffs triple-digit interest rates for loans to meet their basic financial needs while they await justice is so distasteful that judges are willing to be creative in interpreting usury statutes. Several courts have called for legislators to address the problem. Legislation would ideally give plaintiffs some measure of protection while also giving courts clearer guidelines, thus avoiding the need for creative interpretation. Commentators have called for the litigation financing industry to be regulated since at least 2004.¹⁵⁹ Unfortunately, the success of the litigation financing industry in avoiding regulation makes clear that any proposed comprehensive regulatory scheme would face a pitched battle from deep-pocketed interests.

156. *Id.* at 284-85.

157. *Id.* at 287.

158. *Id.* at 287-88 (citation omitted) (internal quotation marks omitted).

159. *See, e.g.,* Martin, *Wild West*, *supra* note 59, at 77.

B. Regulation Proposed and Avoided

Litigation financing is a relatively new industry, but one that is rapidly growing. As an unregulated industry, there are no reliable figures available with which to gauge the size of the industry, its level of risk or its profitability.¹⁶⁰ To date, both borrowers and judges have had to take on faith LFCs' assertions that they assume a "high risk" and thus should be allowed to "make a large profit."¹⁶¹ This assertion, absent figures to back it up, is meaningless. What is high risk? In order to justify triple digit interest rates, well in excess of those charged for unsecured credit card debt, one would surmise that the rate of default would be higher than the two to four percent quoted by industry leaders in the mainstream press.¹⁶²

Several commentators have called for greater transparency in the industry. This could be accomplished in several ways. Professor Susan Lorde Martin, who has written a number of articles supporting litigation financing, suggested amending the federal Truth in Lending Act to bring LFCs within its purview.¹⁶³ This could be accomplished by expanding the statute's definition of "debt" to include contingent obligations when financing is made to support litigation.¹⁶⁴ Assuming this could be accomplished,¹⁶⁵ it would force LFCs to make full disclosure of the costs involved in entering an LLA.¹⁶⁶ Unfortunately, while greater clarity is always welcome, it is doubtful that this measure would truly protect plaintiffs. A plaintiff who is in such dire need as to be willing to borrow from a lender of "last resort"¹⁶⁷ is unlikely to be

160. A New York Times article states that the industry "lends plaintiffs more than \$100 million a year," and refers to LFCs' claims to losing money "in a significant share of cases, from 5 to 20 percent," but notes that "there is no way to verify those numbers." Binyamin Appelbaum, *Lawsuit Loans Add New Risk for the Injured*, N.Y. TIMES Jan. 16, 2011, at A1.

161. See LawCash Funding Agreement *supra* note 35.

162. See Merrill, *supra* note 52; France, *supra* note 56.

163. Martin, *Wild West*, *supra* note 59, at 69.

164. *Id.*

165. Several years after Martin's proposal, TILA still does not cover LFCs. *Id.* at 68-69.

166. Martin, *supra* note 59, at 69.

167. One LFC cautions in its agreement that "selling a portion of the Proceeds to Purchaser is potentially expensive and should only be used as a last resort . . ." CaseFunding Contingent Proceeds Purchase Agreement (April 10, 2009) (on file with author).

deterred by the sort of fine print which is included in credit card statements.

Authors Shaltiel and Cofresi proposed the Litigation Lending for Personal Needs Act (LLPNA), a comprehensive regulatory framework that would require LFCs to be licensed and post a bond.¹⁶⁸ The LLPNA would give plaintiff/borrowers a three-day cooling-off period and the option to pay off all or part of the loan prior to the resolution of their case.¹⁶⁹ It is worth noting that at least some LFCs already provide such options to their borrowers.¹⁷⁰ The LLPNA would also limit the fees charged to either a fixed interest calculated over the life of the loan (not in excess of state usury law) or a contingency fee not to exceed twenty-five percent.¹⁷¹ This last measure would certainly provide more protection to borrowers, but would require each state to pass a comprehensive act targeting the LFC industry.

In the years since Shaltiel and Cofresi proposed their model act, there has been no legislative movement toward true regulation. Instead, LFCs have lobbied for self-regulation, advocating licensing and disclosure requirements that amount to mere window dressing, yet firmly opposing attempts to place a meaningful cap on interest rates.¹⁷² Perhaps the deep pockets of the LFCs are the reason why few legislators have introduced their own bills to regulate this industry. In Texas alone, legal finance groups spent between \$360,000 and \$1,000,000 in a single year to oppose a bill that would have subjected litigation financing to the same standards as other loans.¹⁷³ By contrast, disadvantaged plaintiffs are hardly a powerful lobbying force.

Concerns that LFCs were exploiting consumers did cause former New York State Attorney General Eliot Spitzer to take a closer look at the practices of the litigation financing industry.¹⁷⁴

168. Shaltiel and Cofresi, *supra* note 22, at 351.

169. *Id.*

170. *See, e.g.*, U.S. Claims Purchase Agreement (May 13, 2009) (on file with author).

171. Shaltiel and Cofresi, *supra* note 22, at 355.

172. *See* Appelbaum, *supra* note 160.

173. Benjamin Hallman & Caitlin Ginley, CTR. PUB. INTEGRITY, *Betting on Justice: States are Battleground in Drive to Regulate Lawsuit Funding*, NAT'L L.REV. (Feb. 2, 2011), <http://www.natlawreview.com/article/betting-justice-states-are-battleground-drive-to-regulate-lawsuit-funding>.

174. Press Release, Office of N.Y. State Attorney Gen., Personal Injury

While his investigation of one LFC did not result in charges of wrongdoing, the Attorney General “determined that more could be done to protect consumers.”¹⁷⁵ In response to Spitzer’s investigation, a consortium of LFCs formed the American Legal Finance Association (“ALFA”), a trade association.¹⁷⁶ Following the investigation, the New York Attorney General’s office entered into an “Assurance of Discontinuance” with the group of LFCs that then comprised ALFA.¹⁷⁷ The details of the Assurance will be discussed *infra*. Time would tell whether that agreement would protect plaintiff/borrowers, or merely allow LFCs to operate free from regulation while circumventing the spirit, if not the letter, of the agreement.

C. The Agreement with the New York Attorney General

Spitzer’s investigation, pursued under Executive Law section 63-12 (authorizing the Attorney General to investigate repeated fraudulent or illegal acts), was prompted by concerns that consumers could not adequately understand the terms of the LLAs that they were signing.¹⁷⁸ The LLAs could be confusing to plaintiff/borrowers for several reasons: some failed to provide an APR or a breakdown of the amount owed depending upon when repayment was made, the documents were not always translated into the native language of the borrower, and an opportunity for the borrower to cancel the transaction within a reasonable time was not routinely provided.¹⁷⁹

Under New York state law, in cases where the Attorney General has authority to bring a civil action, he may, at his discretion, opt to accept an assurance of discontinuation of the act that constitutes a violation of the law, from any person or persons

Cash Advance Firms Agree to Reforms (Feb. 28, 2005), *available at* <http://www.ag.ny.gov/press-release/personal-injury-cash-advance-firms-agree-reforms>.

175. Dee McAree, *Legal Cash-Advance Businesses Form Group*, NAT’L L. J., Mar. 28, 2005, at 4.

176. *Id.*

177. Attorney Gen. of N.Y., Bureau of Consumer Frauds & Prot., Assurance of Discontinuance Pursuant to Executive Law § 63(15) (Feb. 17, 2005) at 1, 3 [hereinafter Assurance of Discontinuance].

178. *See id.* at 3.

179. *Id.*

engaged in such an act.¹⁸⁰ Spitzer accepted an agreement with nine LFCs to “settle and resolve” his concerns “without admitting that the Companies have violated any law or otherwise committed any wrongful or improper act”¹⁸¹

The Assurance of Discontinuance provides, *inter alia*, that LLAs would disclose the APR, display the total amount to be repaid broken down in six month increments, include a five-day right to rescission, and be translated into the borrower’s native language.¹⁸² The agreement also stated that “[n]o contract may require mandatory arbitration to resolve disputes under the contract.”¹⁸³ In accord with section 63(15), which provides for “voluntary payment by the alleged violator of the reasonable costs and disbursements incurred by the attorney general during the course of his investigation,” the settling LFCs agreed to pay a total of \$45,000 in costs to the state.¹⁸⁴

The newly minted industry group, ALFA, followed Spitzer’s announcement of the agreement by trumpeting it as an effort to raise industry standards by embracing “best practices.”¹⁸⁵ Harvey Hirschfeld, Chairman of ALFA and President of LawCash (one of the Assurance of Discontinuance signatories), bemoaned the “concern in the industry that people are charging exorbitant rates and giving the industry a bad name.”¹⁸⁶ Hirschfeld described the litigation financing industry as “an industry of last resort for people who have exhausted all financial means and cannot borrow from family, friends or traditional lenders.”¹⁸⁷ In defending LFCs as a resource for needy plaintiffs, he noted that about seventy percent of LawCash borrowers sought their loans to halt a foreclosure or eviction.¹⁸⁸

Trade group ALFA trumpeted the agreement as “the first agreement of its kind in the nation” and vowed “[t]o establish and maintain the highest ethical standards and fair business practices

180. N.Y. EXEC. LAW § 63(15) (Consol. 2009).

181. Assurance of Discontinuance, *supra* note 177, at 3-4

182. Press Release, *supra* note 174.

183. Assurance of Discontinuance, *supra* note 177, at 6.

184. See N.Y. EXEC. LAW § 63(15); Assurance of Discontinuance, *supra* note 177, at 7; Press Release, *supra* note 174.

185. See McAree, *supra* note 175.

186. *Id.*

187. *Id.*

188. *Id.*

within the legal funding industry.”¹⁸⁹ It seemed that after entering the Assurance of Discontinuance, LFCs, or at least those LFCs that had joined ALFA, would work to repair the industry’s image. An advertisement on the ALFA website encourages attorneys to look for the ALFA logo, stating “If your funding source does not display the ALFA logo, it is not a member. Be sure. Be safe.”¹⁹⁰ The ad urges lawyers to “[o]nly trust an ALFA member company” because “member companies adhere to best practices for the industry according to guidelines created with the New York Attorney General.”¹⁹¹

It would appear that, according to ALFA’s ads, Spitzer’s reforms would extend beyond New York citizens to benefit all plaintiff-borrowers. But would this fast-growing, highly profitable industry change its ways and treat its borrowers fairly? Or would the changes be merely cosmetic, and the heralded agreement only a means to forestall true regulation? Some of the answers can be found in an overview of the industry today and a close look at a few sample LLAs.

III. LITIGATION FINANCING IN THE WAKE OF THE DISCONTINUANCE AGREEMENT WITH THE NEW YORK ATTORNEY GENERAL

ALFA membership has now grown to include twenty-one LFCs, including CaseFunding, U.S. Claims, and Hirschfeld’s LawCash.¹⁹² The industry continues to thrive yet, as evidenced by the case law in Part II, challenges to LLAs continue to be brought, and won. In the *Echeverria* opinion, which Professor Susan Lorde Martin termed “an excellent example of judicial antipathy to litigation financing arrangements,”¹⁹³ the court called upon the New York Attorney General to go further and issue an “opinion letter,” rather than merely allow the LFCs to operate pursuant to an “agreement” that makes their operation safer for consumers.¹⁹⁴

189. *Facts about ALFA*, AM. LEG. FIN. ASS’N, <http://www.americanlegalfin.com/FactsAboutALFA.asp> (last visited Mar. 11, 2012).

190. *ALFA Advertisements*, AM. LEG. FIN. ASS’N, <http://www.americanlegalfin.com/press/ALFA%20NY%20Law%20Journal%20ad.pdf> (last visited May 9, 2012).

191. *Id.*

192. *ALFA Member Companies*, AM. LEG. FIN. ASS’N, <http://www.americanlegalfin.com/OfficersAndMembers.asp> (last visited May 9, 2012).

193. Martin, *Subprime*, *supra* note 14, at 93.

194. *Echeverria v. Lindner*, 7 Misc.3d 1019(A), No. 018666/2002, 2005

No such opinion letter issued.

The requirements outlined in the Assurance of Discontinuance that LLAs grant a five-day right of rescission, contain no mandatory arbitration clause, and clearly state the APR while displaying the total repayment amounts at six-month intervals, would be the best (and only) protection for plaintiffs who sought loans from these lenders of last resort. Unfortunately, however, these requirements are not followed as closely as ALFA's advertising would suggest, and at least one LFC would find a cunning way to twist one of the Attorney General's terms to wring even greater profits from its hapless borrowers.

A. A Closer Look at Litigation Lending Agreements

Despite the arrival of ALFA, and the industry-image polishing that it promised, the as-yet-unregulated litigation financing industry still lacks the degree of transparency necessary for a complete overview. Professor Martin explained that a comparison of LFCs to other subprime lending industries cannot be performed, because LFCs are privately held and members of ALFA were "unwilling to provide information about the interest rate they charge, how they assess risk, how often they do not recover funds advanced or any other information that would allow a realistic assessment about whether or not they are overcharging their borrowers."¹⁹⁵

Fortunately, however, some LLAs themselves provide a glimpse into current industry practice. The view is not pretty. The author reviewed three such agreements (with personal information redacted) from ALFA members CaseFunding, U.S. Claims and LawCash.

In comparing the LLAs and the degrees to which they follow the Assurance of Discontinuance, it is important to note that the agreement with the New York Attorney General applies specifically to contracts with New York residents.¹⁹⁶ The sample LLAs referenced here were entered into by borrowers who are residents of other states. However, ALFA advertising indicates that their members adhere to the guidelines created by the New

WL 1083704, at *8 (N.Y. Sup. Ct. 2005).

195. Martin, *Subprime*, *supra* note 14, at 101.

196. Assurance of Discontinuance, *supra* note 177, at 4.

York Attorney General.¹⁹⁷

The one requirement that was included in all three LLAs was the five-day right of rescission. Although it is unknown how often a borrower actually exercises this right, it was plainly stated in each of the sample LLAs.¹⁹⁸

Strict adherence to the ALFA guidelines and Attorney General agreement disappears when it comes to the Assurance of Discontinuance's prohibition against mandatory arbitration clauses. The U.S. Claims LLA is the only one of the three with no mention of arbitration.¹⁹⁹ CaseFunding does not call for mandatory arbitration, and its LLA contain choice of law and choice of venue clauses indicating that New York will have exclusive jurisdiction.²⁰⁰ However, that same document also provides that "[a]ny controversy or claim arising out of or relating to this contract . . . may be settled by final, binding arbitration . . ." ²⁰¹ LawCash goes the furthest in flouting the Assurance of Discontinuance's terms. Its LLA states that "at the sole and exclusive option of LAWCASH, any controversy or claim arising out of or relating to this contract . . . shall be settled by final, binding arbitration . . ." ²⁰² While the same LLA provides for the application of New York law and jurisdiction in a New York court, one must assume that if arbitration can be compelled at the sole and exclusive option of the LFC, arbitration is, in reality, mandatory.

Both CaseFunding and U.S. Claims express the interest to be charged on an annualized basis and clearly display the APR (fifty-one percent and twenty-seven percent, respectively).²⁰³ The LawCash agreement, however, contains absolutely no mention of

197. See *ALFA Advertisements*, AM. LEG. FIN. ASS'N, <http://www.americanlegalfin.com/press/ALFA%20NY%20Law%20Journal%20ad.pdf> (last visited May 9, 2012).

198. CaseFunding Contingent Proceeds Purchase Agreement, *supra* note 167; LawCash Funding Agreement, *supra* note 33; U.S. Claims Purchase Agreement, *supra* note 170.

199. See U.S. Claims Purchase Agreement, *supra* note 170.

200. See CaseFunding Contingent Proceeds Purchase Agreement, *supra* note 167.

201. *Id.*

202. See LawCash Funding Agreement, *supra* note 33.

203. CaseFunding Contingent Proceeds Purchase Agreement, *supra* note 167; U.S. Claims Purchase Agreement, *supra* note 170.

an APR.²⁰⁴ Moreover, the language regarding the cost is purposely obtuse. The term “interest rate” does not appear in this clause. Instead, the interest is referred to as an “accrued use fee, compounded monthly,” and a “monthly use fee” of 3.10%.²⁰⁵ It is impossible, with the information provided, for any plaintiff/borrower to determine the APR.

The impossibility of this determination illustrates how LawCash turned a seemingly innocuous requirement of the Assurance of Discontinuation, into a trap for unwary borrowers. The Assurance of Discontinuation further calls for an itemization of all fees, with the total amount to be repaid broken down into six-month increments.²⁰⁶ Both the U.S. Claims and CaseFunding LLAs express these payoff amounts in a straightforward manner, with both LFCs breaking the payoff numbers down further into monthly totals (thus meeting both the letter and the spirit of the agreement with the Attorney General).²⁰⁷ LawCash, however, twists the purpose behind these six-month “windows,” to yield not the intended transparency for the consumer but a lucrative hidden fee for the LFC. In the sample LLA, the windows appear as follows:

<u>Date of Payment to LAWCASH</u>	<u>Amount Due</u>
If payment is made on 2/26/2010	\$64,512.73
If payment is made on 8/26/2010	\$75,377.88
If payment is made on 2/26/2011	\$87,896.38
If payment is made on 8/26/2011**	\$102,699.78

**After this date, monthly fees continue to accrue until LAWCASH is paid in full. This chart includes example dates only. Dates in-between and after those shown may reflect other pay-off amounts. Always contact LAWCASH for your exact pay-off amount.²⁰⁸

The language following the asterisks is deceptively simple. A fair reading would suggest that interest and payoff amounts are

204. See LawCash Funding Agreement, *supra* note 33.

205. *Id.*

206. Press Release, *supra* note 174.

207. See CaseFunding Contingent Proceeds Purchase Agreement, *supra* note 167; U.S. Claims Purchase Agreement, *supra* note 170.

208. LawCash Funding Agreement, *supra* note 33.

calculated on a linear basis and that payments made between the window dates will be pro-rated. The clue to how LawCash's "windows" trap works is contained in this clause, which follows one paragraph later: "[t]he monthly use fee is charged from [the date of the advance] *until the end of the 5 month interval during which payment of proceeds is made to LawCash.*"²⁰⁹ This carefully buried language derogates from the seemingly clear disclosure page. In effect, what happens is this: if the borrower pays anytime during the first six-month period, she will pay the amount contained within the "6 month" window. If she pays *one day* later (thus tipping her over into the "12 month" window), she will owe the *entire* amount in that window, just as if she had had the use of the money for twelve months, rather than six months and one day. And the difference in the effective interest rate is stunning. A plaintiff in this scenario, who borrowed \$47,000, would repay \$64,512 on the last day of the six-month window, and \$75,377 just one day later, taking the APR from 74.5% to nearly 120%.²¹⁰ Because the APR is wholly dependent on the timing of when the loan is repaid, it is impossible for a plaintiff/borrower (or her attorney or accountant) to calculate the APR at the time she signs the LLA.

There are other terms in the reviewed LLAs that also violate the spirit, if not the letter, of the ALFA guidelines and Assurance of Discontinuation. For example, both the CaseFunding and LawCash LLAs contain waivers of any defense to payment.²¹¹ Additionally, CaseFunding's LLA calls for liquidated damages of two times the amount due in the event that the plaintiff/borrower breaches the agreement.²¹² LawCash's LLA contains an express waiver of the right to consolidate actions or participate in a class action.²¹³

209. *Id.* (emphasis added).

210. *See id.*

211. CaseFunding Contingent Proceeds Purchase Agreement, *supra* note 167; LawCash Funding Agreement, *supra* note 33.

212. CaseFunding Contingent Proceeds Purchase Agreement, *supra* note 167.

213. LawCash Funding Agreement, *supra* note 33. By contrast, the U.S. Claims LLA contains none of these provisions and, in fact, expressly allows the borrower to "pay USC money to reduce the amount of USC's Interest" prior to final verdict, award, or settlement. U.S. Claims Purchase Agreement, *supra* note 170.

Finally, there are two curious terms buried in the language of the LawCash LLA that raise questions regarding the lengths to which LawCash would go to collect from a borrower in the event the plaintiff/borrower's lawsuit were not successful. LawCash's LLA, in contrast to those of U.S. Claims and CaseFunding, defines "proceeds" as including "any money paid as a consequence of the Lawsuit, whether by settlement, judgment or otherwise."²¹⁴ Just what is covered by the words "consequence" and "otherwise?" If a plaintiff/borrower were to, say, write a book about the lawsuit she lost, could LawCash collect from her? The LawCash LLA goes on to state that, in the event that the lawsuit is not successful, it will not attempt to collect *directly* from the borrower.²¹⁵ It never explains what *indirect* collection might be.

Despite the promise of ALFA's advertising that its members "adhere to best practices for the industry according to guidelines created with the New York Attorney General,"²¹⁶ it is clear that there is still reason for concern that plaintiffs are being preyed upon by LFCs. It is equally clear that, instead of "establish[ing] and maintain[ing] the highest ethical standards and fair business practices within the legal funding industry," ALFA members are working to avoid regulation and maintain astronomical interest rates.²¹⁷

B. Industry Practices Today

When Professor Martin wrote about the nascent litigation financing industry,²¹⁸ she touted LFCs as fulfilling a need, and urged that, rather than "regulate the litigation financing industry out of business, whether through legislation or court decisions," we should instead encourage competition as the means of lowering costs.²¹⁹ While Martin also advocated requiring greater transparency within the industry, she opposed bringing LLAs within the purview of usury statutes claiming that this would

214. LawCash Funding Agreement, *supra* note 33.

215. *Id.*

216. *ALFA Advertisements*, AM. LEG. FIN. ASS'N, <http://www.americanlegalfin.com/press/ALFA%20NY%20Law%20Journal%20ad.pdf> (last visited May 9, 2012).

217. *Facts about ALFA*, AM. LEG. FIN. ASS'N, <http://www.americanlegalfin.com/FactsAboutALFA.asp> (last visited Mar. 11, 2012).

218. Martin, *Wild West*, *supra* note 59, *passim*.

219. *See id.* at 77.

limit funds available to plaintiffs, presumably because the risk involved is so high that no one would offer these loans at lower rates.²²⁰

Martin's assertion, however, is not factually grounded. Aside from claiming high risk, LFCs have not, to date, provided any means of assessing their actual level of risk. With industry leaders admitting default rates between two and four percent, it is difficult to justify allowing this industry to operate free from the constraints of usury laws.

Professor Martin continues to maintain that LFCs are part of a subprime industry that should be exempt from usury laws.²²¹ However, after LFCs began to scrupulously guard information regarding their actual level of risk (industry leaders no longer comment for attribution on the subject), Martin shifted her justification for the usury exemption from the LFCs' practices, to their borrowers' actions.²²² "[S]tate legislatures should define litigation financing as investments, not loans, to eliminate the threat of plaintiffs/borrowers accepting funds and then reneging, arguing usury, on their agreements to pay the stipulated fees out of the proceeds of their lawsuits."²²³

One would think after reading Professor Martin's *apologia* for the LFCs that the problem here is plaintiffs who will not pay up. If that were the case, the litigation financing industry would be shrinking, not expanding. Rather, it is the disadvantaged plaintiffs, with no lobbyists or political power, who need protecting, not the LFCs.

ALFA has proven itself to be a powerful lobbying force. In the wake of *Rancman*, ALFA brought that force to bear on the Ohio state legislature, and succeeded in getting legislation passed to overturn that case's bar on litigation funding.²²⁴ ALFA issued a press release trumpeting the new law as a measure that "like ALFA's own internal 'Best Practices' policy, is geared to further

220. *Id.*

221. *See generally* Martin, *Subprime*, *supra* note 14.

222. *See id.* at 115.

223. *Id.*

224. *See Ohio Legislation*, AM. LEG. FIN. ASS'N (June 7, 2008), <http://www.americanlegalfin.com/PressReleases.asp>. Unlike Texas, Ohio does not require disclosure of money spent on lobbying efforts. Hallman & Ginley, *supra* note 173.

protect consumers from legal financing companies that do not follow industry standards.”²²⁵ But when the LFC run by the Chairman of ALFA fails to follow the guidelines embraced in ALFA advertising, it is hard to believe that “consumer protection” is at the heart of ALFA’s efforts.

The litigation financing industry’s reaction to attempts to rein in its excesses have been consistent. There is no greater transparency today than there was when Perry Walton made his first loan. When courts in states like Ohio or North Carolina rule for the plaintiff over an LLA, instead of complying with that state’s law, LFCs either opt not to do business there,²²⁶ or lobby for “self-regulation” that would preserve the status quo.²²⁷ Competition has not served to bring down costs for the simple reason that borrowers need adequate information in order to choose between vendors. When APRs are difficult, if not impossible, to calculate, and terms vary greatly from LLA to LLA, there is no meaningful way for a plaintiff to comparison shop.

Even the language used in LFC advertising is designed to mislead plaintiff/borrowers. On their websites, LFCs offer “litigation funding” or “plaintiff financing,” words that would certainly indicate “loan” to a plaintiff (as opposed to “investment”). When it is time to sign on the dotted line, however, the LLA will be titled a “contingent proceeds purchase agreement”²²⁸ or some similarly obscure term. The word “lender” will not appear in the LLA, and instead, the LFC will be dubbed the “purchaser.”²²⁹ These contracts are carefully drafted to sidestep usury statutes, but their language further serves to keep their borrowers in the dark. “Litigation funding” is not lending in the same way that “gaming” is not gambling. These are distinctions without a difference. It is time for state legislatures to step in and act to protect their constituents from those members of the litigation financing industry who prey on them.

225. See *Ohio Legislation*, AM. LEG. FIN. ASS’N (June 7, 2008), <http://www.americanlegalfin.com/PressReleases.asp>.

226. See OASIS LEGAL FINANCE, <http://www.oasislegal.com> (last visited Mar. 13, 2012). (“Not Available in Arkansas, Colorado, Kansas, Maryland or North Carolina”).

227. See Appelbaum, *supra* note 160.

228. See, e.g., CaseFunding Contingent Proceeds Purchase Agreement, *supra* note 167.

229. See *id.*

IV. PROPOSED MODEL REMEDIAL STATUTE

Because the litigation financing industry has proven itself unwilling to meaningfully self-regulate, this article proposes a model statute that can be incorporated as part of a state's existing usury statute. Instead of designing, whole cloth, a licensing and regulatory framework for the litigation financing industry, this model remedial statute would simply bring LFCs within the purview of each state's usury statute.

Often, the simplest solution is the best. Others have suggested implementing a federal regulatory framework for LFCs.²³⁰ That approach is unwieldy, unlikely to survive the lobbying efforts of the litigation financing industry, and ultimately unnecessary. If LFCs operated within the boundaries of each state's usury statutes, further regulation would not be needed. Loans would be available to plaintiffs at fair prices, and despite their cries to the contrary, LFCs would be able to make a decent profit. It would be a simple, effective fix, which would require only that each state's legislature amend its existing statute.

The proposed remedial statute is comprised of two parts: a definition section clearly indicating what constitutes an LLA, and a statute that requires any lending tied to litigation be construed as a loan, whether contingent or not. The definition of an LLA will resolve the uncertainty courts face when assessing whether or not an LLA is a loan. It would also prevent LFCs' from using obscure language in their LLAs. A litigation advance will be considered a loan, pure and simple. The second part of the proposed statute clearly brings these loans within the purview of the usury statute.

Proposed Model Remedial Statute to Bring LFCs Within
the Purview of Usury Regulations:

WHEREAS, parties to civil litigation are, during the pendency of such litigation, particularly vulnerable to predatory lending practices, and

WHEREAS, lending by litigation financing companies has, to date, gone largely unregulated,

the following statute is intended to bring litigation

230. See generally Shaltiel & Cofresi, *supra* note 22.

financing agreements within the regulatory framework of this state's usury statute(s).

Definitions: "Litigation Lending Agreement" (LLA): Any agreement whereby monies are paid to parties to civil litigation (litigants) in consideration for those litigants' agreement to repay such monies (with or without interest, one-time charges, use fees, or any other add-on charges) from proceeds of the litigation. Not included in the definition of an LLA are advancements of expenses of litigation made by attorneys on behalf of their clients, as permitted by Rule 1.8(e) of the Model Rules of Professional Responsibility.

Regardless of:

(a) whether an LLA characterizes itself as a "loan," an "advance," an "investment," an "assignment of proceeds," or any other characterization,

(b) whether monies to be repaid under an LLA are called "interest," "use fees," or any other term,

(c) whether the amount paid to the litigant under the LLA otherwise exceeds any monetary threshold for the amount of loans falling within this state's usury statute, and

(d) whether the obligation on the part of the litigant to repay monies is contingent upon the outcome of the litigation or absolute,

all LLAs shall be considered loans within the purview of this state's laws [reference specific statutes] intended to protect individual borrowers from usurious loans.²³¹

The proposed remedial statute has the beauty of simplicity.

231. This proposed remedial statute was incorporated into proposals introduced in the Rhode Island General Assembly during the January 2011 session. *See* H. 5533, 2011 Gen. Assemb., Jan. Sess. (R.I. 2011); S. 0366, 2011 Gen. Assemb., Jan. Sess. (R.I. 2011).

By utilizing a state's existing usury statute, the remedial statute implicitly embodies the public policy of that state towards lending. Usury statutes vary greatly from state to state. Most states set interest rate ceilings, with the limit established by the legislature. A handful of states, including Idaho, Oregon, Nevada, New Hampshire, and Wyoming, have no laws at all against usury.²³² It is fair to view these differences as an expression of each state's public policy intentions. By bringing litigation financing within the existing framework of each state's usury statute, the remedial statute merely extends the existing public policy. Because there is no change to public policy, passage of the remedial statute should be far easier than attempting to establish an entirely new regulatory framework. Importantly, unlike a regulatory program, this statute will rein in the excesses of litigation financing without costing a dime to administer.

Unlike proposals to bring litigation financing under the federal restrictions of TILA, this statute does not have a consumer education aspect. That is because the concept of "consumer education" is a red herring. All of the disclosures in the world will not serve to protect a disadvantaged plaintiff who is in no position to comparison shop. This Article's overview of LLAs should be sufficient to suggest that plaintiffs will never have adequate information to make a truly informed choice. Absent adequate information, and lacking any real bargaining power, plaintiffs will always be at the mercy of LFCs. Holding LFCs to the same maximum rate as other types of lenders is the only real way to protect plaintiffs.

Finally, in decision after decision, courts have called upon legislatures to give them clearer guidance regarding litigation financing. By bringing litigation financing within the purview of the usury statutes, state legislatures can stop the semantic game LFCs play in the wording of their LLAs. At the same time, courts will be relieved of the obligation to play a parallel semantic game in seeking to grant an equitable resolution to injured plaintiffs. With clearer guidance from state law, courts can return to the business of enforcing previously established public policy.

The litigation financing industry is sure to decry this proposal as the end of litigation funding. Any prior attempt to construe

232. Barksdale, *supra* note 28, at 725.

LLAs as usurious has been met with strong resistance and the assertion that plaintiff-borrowers will be denied access to financing. However, a look at the history of the industry belies this argument. After *Rancman*, which cited interest rates of 180% to 280%, it was claimed that efforts to regulate LFCs would result in plaintiffs being denied access to financing.²³³ However, years later, U.S. Claims is entering LLAs at an APR of 27%,²³⁴ and the number of LFCs has increased substantially. Even absent the sort of industry statistics that would be available if LFCs were regulated, it stands to reason that litigation lending can still be profitable if conducted in accordance with usury statutes.

It is true, though, that under this model remedial statute, LFCs will not rake in the enormous gains they once saw. The threat to those profits will motivate ALFA to lobby hard, with all the financial capital it can muster, to prevent passage of this statute.²³⁵ Plaintiffs have no such lobbying group. Sadly, not even the plaintiffs' bar can be counted on to lobby in favor of such a proposal, as some of its members are the very people profiting by their association with LFCs: many LFCs are owned and operated by lawyers.²³⁶ In fact, the court in *Fausone* noted the danger of plaintiff attorneys using LFCs as means of funding each others' clients in order to circumvent the ethical rule prohibiting such funding:

[A] person who is the victim of an accident should not be

233. See Martin, *Subprime*, *supra* note 14, at 116.

234. See U.S. Claims Purchase Agreement, *supra* note 170.

235. During the 2011 session of the Rhode Island General Assembly, ALFA paid former Senate Finance Chairman Stephen Alves over \$29,000 to lobby against S 0366. The bill was not voted out of committee. Peter Phipps, *Former Legislators Russo and Alves are Cashing in as Lobbyists*, PROVIDENCE J. (July 31, 2011, 10:32 AM), <http://news.providencejournal.com/politics/2011/07/former-legislat.html>. Oasis Legal Funding paid a Rhode Island-based lobbyist \$30,000, presumably to oppose the same bill, while at the same time paying its own in-house lobbyist. *Lobby Tracker*, OFF. SECRETARY ST., http://sos.ri.gov/ltpublic/index.php?page=entity_detail&entityId=1518&sessionId=8 (last visited Mar. 30, 2012). It is worth noting that Rhode Island is the smallest state in the union, there are no LFCs incorporated there and the size of the market for litigation lending is tiny. The disproportionate spending on lobbying efforts can only signal the importance of preventing the precedent of *any* state construing LLAs as usurious.

236. George Steven Swan, *Economics and the Litigation Financing Industry: How Much Justice Can You Afford?*, 35 NEW ENG. L. REV. 805, 823 (2001).

further victimized by loan companies charging interest rates that are higher than the risks associated with the transaction. . . . Especially if lawyers establish litigation loan companies to “service” one another’s clients, these high interest loans may actually be a method to increase the lawyers’ contingency fees.²³⁷

With such deep-pocketed concerns opposed to any attempt to limit the excesses of the litigation financing industry, it is incumbent upon state legislatures to stand up for their constituents. To muster the political will to take on this industry, legislators should be reminded that, like sharks to shipwrecks, LFCs often arrive in the wake of tragedy, drawn by the unconscionably high rates of interest to be reaped from disadvantaged plaintiffs who are in no position to bargain. Legislators need only look to the recent history of tragic events, from 9/11 to the Station Fire to Hurricane Katrina and act now to protect the citizens of their own states against the predators who are sure to arrive when future tragedy strikes.

V. CONCLUSION

It has become clear to even the litigation lenders that judges view their practices with distaste. Dimitri Mishiev, of Alliance Claim Funding, sums it up thusly: “[e]verything that might have to go before a judge, you stay away because you don’t want the judge to be in the position of saying, ‘I don’t want that level of payment. I think it’s unreasonable.’ . . . We don’t want judges to shine a light on us.”²³⁸ These same judges have called upon legislators to take a closer look at litigation lending.

Given the growth of the litigation financing industry, and the inadequate attempts to curb its excesses, the time has come to bring litigation funding within the purview of state usury statutes. Large-scale tragedies like the Station Nightclub fire can help focus the attention of legislators on the plight of disadvantaged plaintiffs. Sadly, mass tort plaintiffs are not the only victims of the predatory lending practices of LFCs. Every day, in every state, individual plaintiffs, injured by the negligence,

237. *Fausone v. U.S. Claims, Inc.*, 915 So.2d 626, 630 & n.6 (Fla. Dist. Ct. App. 2005).

238. Appelbaum, *supra* note 160.

recklessness, and intentional acts of others, often unable to work and in danger of losing their homes, turn to LFCs for desperately needed funds. Is it too much to ask that such plaintiffs not be further victimized in the form of usurious interest? Legislators must act now to protect their constituents from predatory LFCs. It is time to tame the "Wild West" of lending, and thereby protect the most vulnerable of our citizens.²³⁹

239. See Martin, *Wild West*, *supra* note 59.