

**INVESTING IN LAWSUITS:  
“LITIGATION FINANCING”  
AND THE  
CONSUMER PROTECTION IMPERATIVE**

By

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**INTRODUCTION**

Litigation financing has gained considerable momentum over the past decade. The idea is a simple one, perhaps best portrayed in numerous Internet advertisements offering cash outside the traditional lending context for those who want to finance and pursue lawsuits. Rules of professional ethics largely prevent attorneys from providing financial assistance to their clients, so certain entrepreneurs have filled the void and made it possible for people previously unable to afford litigation to now have their day in court.<sup>1</sup> In the prototypical case, the financing company will advance funds to the would-be litigant and later collect the principal and interest (often at an exorbitant rate), but only if the litigant prevails in court. To avoid certain legal entanglements, litigation financing companies try to cast their involvement as “investments.” Each transaction is a calculated risk.

This gamble on litigation has been traced by some to Las Vegas entrepreneur, Perry Walton, the “self-proclaimed father of the modern litigation finance industry.”<sup>2</sup> After pleading guilty in 1997 to criminal charges, the “former rock

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<sup>1</sup>MODEL RULES OF PROF'L CONDUCT R. 1.8(e).

<sup>2</sup>Mariel Rodak, *It's About Time: A Systems Thinking Analysis of the Litigation Finance Industry and Its Effect on Settlement*, 155 U. PA. L. REV. 503, 505 (2006).

musician and mobile-home park developer”<sup>3</sup> decided to form Future Settlement Funding Corporation and began conducting two-day \$12,400 seminars on how others could develop their own litigation financing companies.<sup>4</sup> Many companies have followed Walton’s footprints to develop relatively small companies with modest portfolios that typically fund personal injury suits.

The growth of litigation financing remains a recent phenomenon in the United States, but is not necessarily a new concern. The legal systems of classical Greece and Rome and even Medieval England all discouraged the practice of intermeddling in the litigation of others, and did so under the guise of doctrines known as maintenance, champerty, and barratry. Born of these ancient roots, these doctrines found their place in American jurisprudence as well, enduring over the years because they addressed fundamental concerns that remain vitally important today: open access to the legal system must nonetheless be balanced by protections against the intermeddling of outsiders who might create a more litigious society, threaten the independence of lawyers, disrupt otherwise acceptable settlements, and ultimately prey on the financially vulnerable. Despite these concerns and the legal doctrines developed over centuries to address these perceived ills, the legal response in the United States has been relatively slow in managing this mushrooming litigation financing industry.

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<sup>3</sup>*Id.* (internal quotation omitted).

<sup>4</sup>Terry Carter, *Cash Up Front*, A.B.A. JOURNAL, Oct. 2004, at 36.

The relative silence of the law has left many with the impression that litigation financing is here to stay,<sup>5</sup> and even now the industry has begun developing in even more unexpected directions. For instance, Juridica Capital Management, a litigation financing company that eschews smaller clients in favor of corporate ones with the potential for larger payouts,<sup>6</sup> maintains a hedge fund—Juridica Investments—that has been traded on the London Stock Exchange since 2007. The fund has risen twenty-four percent in that time. “You don’t want to profit at the misfortune of everybody else,” said Juridica’s chief executive officer and attorney, Richard W. Fields, “but we’ve seen a serious increase in interest in light of the economy.”<sup>7</sup> In a time of economic uncertainty and strife, lawsuits have become avant garde for investors who want to profit on someone else’s claim.<sup>8</sup>

Juridica, which has offices in England and now the United States, claims to undertake a rigorous examination of a case over a thirty to ninety day period before accepting it; and, in 2008, Juridica funded only seventeen of one hundred twenty-two cases it considered.<sup>9</sup> Corporations have become a particularly natural source of clientele for Juridica because of the economic downturn: “If you are involved in major litigation but earnings are dropping and there is pressure on cash flow, funds

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<sup>5</sup>See Wayne C. Walker, *Litigation Funding Is Here to Stay*, LAWYER’S WEEKLY, Mar. 29, 2004 (“[W]e know the following: plaintiffs love it; defendants hate it; it is here to stay!”).

<sup>6</sup>Helen Avery, *Litigation is the new strategy*, EUROMONEY, Jan. 2009.

<sup>7</sup>Lauren Tara LaCapra, *Hedge Fund Hell: These Funds Sue You*, THE STREET, Jan. 23, 2009, <http://www.thestreet.com/story/10459369/1/hedge-fund-hell-these-funds-sue-you.html>.

<sup>8</sup>Telis Demos, *Cashing in on litigation*, FORTUNE, May 4, 2009, available at [http://money.cnn.com/2009/05/04/magazines/fortune/demos\\_litigation.fortune/index.htm](http://money.cnn.com/2009/05/04/magazines/fortune/demos_litigation.fortune/index.htm).

<sup>9</sup>*Id.*

like ours can fill the financing gap,” said Fields.<sup>10</sup> Ultimately, Fields estimates that the market for litigation financing in the United States could be \$33 billion.<sup>11</sup>

The boom of litigation financing and now litigation investment has occurred without a concerted or consistent response from the law. Indeed, the law has remained relatively silent on the issue, despite concerns surrounding some practices in the industry. Where the law has spoken, it has been inconsistent. While a universal approach may not be feasible or even desirable under concepts of federalism (noting federal regulation of traditional lending), lawmakers should nonetheless be more proactively innovative rather than reactive in developing parameters for this industry. The failure to do so leaves us with an industry unchecked by traditional legal norms and which would (ironically) foster even more litigation. The legal community should move ahead of the curve on this industry, appreciating perhaps first where it has been.

## **I. HISTORICAL APPROACH**

The idea of litigation financing has stirred the ire of lawmakers over centuries and the passions of literary creations as diverse as Chaucer’s *The Knight’s Tale* to Judge Taylor’s rebuke in *To Kill a Mockingbird*. The conceptual reflection of this sentiment has a long history in the legal doctrines of maintenance, champerty, and barratry, which date from ancient law and in many United States jurisdictions have lain dormant in recent years, only to come to the front lines unprepared as litigation

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<sup>10</sup>*Id.*

<sup>11</sup>Sophia Grene, *Rich pickings from legal cases*, FINANCIAL TIMES, Jan. 25, 2009, available at <http://www.ft.com/cms/s/o/20eb1686-e984-11dd-9535-0000779fd2ac.html>.

financing and investment have gained ground.<sup>12</sup> The doctrines have not matured well in the United States, nor been an effective deterrent to litigation financing.

The Supreme Court succinctly defined the doctrines in *In re Primus*: “Put simply, maintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty.”<sup>13</sup> These ancient doctrines have received a fair amount of treatment over the years.<sup>14</sup> They essentially describe an officious and opportunistic intermeddler who, without any bona fide interest or stake in a dispute, vexatiously incites litigation by assisting someone in pursuing a claim or

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<sup>12</sup>*Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217, 220 (Ohio 2003).

<sup>13</sup>*In re Primus*, 436 U.S. 412, 424 n.15 (1978).

<sup>14</sup>In addition to cases discussed *infra* and articles cited throughout, *see, e.g.*, *NAACP v. Button*, 371 U.S. 415 (1963); *Progressive Gaming Int'l v. Venturi*, 563 F.Supp.2d 321 (D.R.I. 2008); *Fausone v. U.S. Claims, Inc.*, 915 So.2d 626 (Fla. 2005); *Lawsuit Fin. v. Curry*, 683 N.W.2d 233 (Mich. Ct. App. 2004); *Johnson v. Wright*, 682 N.W.2d 671 (Minn. Ct. App. 2004); *Echeverria v. Linder*, 801 N.Y.S.2d 233 (2005); *see also* Richard L. Abel, *How the Plaintiff's Bar Bars Plaintiffs*, 51 N.Y.L. SCH. L. REV. 345 (2006-2007); Paul Bond, *Making Champerty Work: An Invitation to State Action*, 150 U. PA. L. REV. 1297 (2001-2002); John Cofresi & Yifat Shaltiel, *Litigation Lending for Personal Needs Act: A Regulatory Framework to Legitimize Third Party Litigation Finance*, 58 CONSUMER FIN. L.Q. REP. 347 (2004); Ari Dobner, *Litigation for Sale*, 144 U. PA. L. REV. 1529 (1996); Lauren J. Grous, *Causes of Action for Sale: The New Trend of Legal Gambling*, 61 U. MIAMI L. REV. 203 (2006); Andrew Hananel & David Staubitz, *The Ethics of Law Loans in the Post-Rancman Era*, 17 GEO. J. LEGAL ETHICS 795 (2003-2004); Susan Lorde Martin, *Financing Plaintiff's Lawsuits: An Increasingly Popular (and Legal) Business*, 33 U. MICH. J.L. REF. 57 (2000); Susan Lorde Martin, *Financing Litigation On-Line: Usury*, 1 DEPAUL BUS. & COM. L.J. 85 (2002); Susan Lorde Martin, *The Litigation Financing Industry: The Wild West of Finance Should Be Tamed Not Outlawed*, 10 FORDHAM J. CORP. & FIN. L. 55 (2004); Julia H. McLaughlin, *Litigation Funding: Charting a Legal and Ethical Course*, 31 VT. L. REV. 615 (2007); Richard W. Painter, *Litigating on a Contingency: A Monopoly of Champions or a Market for Champerty?*, 71 CHI-KENT L. REV. 625 (1995-1996); Douglas R. Richmond, *Other People's Money: The Ethics of Litigation Funding*, 56 MERCER L. REV. 649 (2005); Marial Rodak, *It's About Time: A Systems Thinking Analysis of the Litigation Finance Industry and Its Effects on Settlement*, 155 U. PA. L. REV. 503 (2006); George Steven Swan, *Economics and the Litigation Funding Industry: How Much Justice Can You Afford?*, 35 NEW. ENG. L. REV. 805 (2000-2001).

investing in the process for a promised return of judgment proceeds.<sup>15</sup> Rooted in classical Greek and Roman laws, these doctrines sought to bar “sycophants” and “calumniators” from participating in disputes unrelated to them.<sup>16</sup> The doctrines rose to greater prominence in Medieval England when feudal lords and wealthy noblemen supported others’ suits against their rivals in an effort to aggrandize their positions and holdings.<sup>17</sup> Maintenance, champerty, and barratry laws became a way to check such undesired practices.

Ancient doctrines do not always translate to modern times, and legal restrictions against champertous activities have not always neatly applied to the burgeoning development of modern litigation financing and investing. Indeed, it is as though two different worlds are colliding. One world makes reference to thirteenth century English laws,<sup>18</sup> the sycophants of ancient Greece,<sup>19</sup> and Justice Holmes’ thoughts on King Henry IV.<sup>20</sup> In the other world reside parties with names like Legal Bucks<sup>21</sup> and entrepreneurial investors with attractive websites rolling the dice for would-be litigants to have their day in court. Ancient lands to Las Vegas, the law simply has not kept pace. Indeed, one need not travel far from rather recent decisions of state courts that have wrestled admirably with the tension between champerty laws and litigation financing only to reach rather divergent decisions,

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<sup>15</sup>*Black’s Law Dictionary* (8th ed. 2004).

<sup>16</sup>*Osprey, Inc. v. Cabana Ltd. P’ship*, 532 S.E.2d 269, 273 (S.C. 2000).

<sup>17</sup>See Christy B. Bushnell, *Champerty is Still No Excuse in Texas: Why Texas Courts (and the Legislature) Should Uphold Litigation Funding Agreements*, 7 HOUS. BUS. & TAX L.J. 358, 358-59 (2006-2007); see also *Osprey*, 532 S.E.2d at 274.

<sup>18</sup>*Osprey*, 532 S.E.2d at 273 n.2.

<sup>19</sup>*Id.* at 273.

<sup>20</sup>*Saladini v. Righellis*, 687 N.E.2d 1224, 1227 (Mass. 1997).

<sup>21</sup>*Odell v. Legal Bucks LLC*, 665 S.E.2d 767 (N.C. Ct. App. 2008).

leaving the law too unsettled.

## II. UNSETTLED CASE LAW

The struggles of many states over the last few years begins in Ohio with *Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217 (Ohio 2003). One year after sustaining injuries in an auto accident, Roberta Rancman filed suit against State Farm Insurance to collect uninsured motorist benefits. As she awaited an outcome, two litigation financing companies, Interim and Perry Walton's Future Settlement Funding Corporation, advanced her payments of \$6000 and \$1000. In exchange, Rancman agreed to return the advances according to a scheme resulting in inflated interest rates of 180 percent per year for the \$6000 and 280 percent for the \$1000; however, her repayment obligation would only become effective if she prevailed in her suit against State Farm. She did indeed prevail, but then refused to pay according to the contractual terms and instead tendered return of the money at an annual percentage rate of eight percent.

When unaccepted, Rancman filed suit seeking a declaratory judgment that the agreements were loans in violation of an Ohio usury law requiring lenders of certain amounts to be licensed and to abide fair lending standards.<sup>22</sup> Interim and Future Settlement Funding argued that the advances were not *loans* (since there was no guarantee of repayment) but rather *investments*. At both the trial and intermediate appellate level, the courts held that the advances were loans in

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<sup>22</sup>OHIO REV. CODE § 1321.02.

violation of Ohio law. Interim and Future Settlement Funding appealed to the Ohio Supreme Court.

The Ohio Supreme Court devoted a mere four sentences on whether the advances were loans rather than investments. Without resolving that issue, the court instead turned its attention to the “ancient practices of champerty and maintenance.”<sup>23</sup> Applying a strict approach to champerty, the court held that, even if the advances constituted mere investments, the agreements should be declared void as champertous:

The advances sub judice constitute champerty because FSF and Interim sought to profit from Rancman’s case. They also constitute maintenance because FSF and Interim each purchased a share of a suit to which they did not have an independent interest; and because the agreements provided Rancman with a disincentive to settle her case.<sup>24</sup>

This case applied champerty laws in traditional fashion.

Although its holding has since been ostensibly overturned by state statute,<sup>25</sup> *Rancman* has been influential in presenting a strong argument for the broad application of champerty laws. The Ohio Supreme Court approached its case with a vigorous—and frankly honest—interpretation of champerty laws. Unlike other courts, the Ohio Supreme Court was not interested in drawing fine distinctions between loans and investments. The simple act of intermeddling in another person’s lawsuit for profit was enough to have constituted champerty. Equally unconcerned that “champerty and maintenance ha[d] lain dormant” in Ohio for

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<sup>23</sup>789 N.E.2d at 220.

<sup>24</sup>789 N.E.2d at 220.

<sup>25</sup>See OHIO REV. CODE §1349.55, discussed *infra*.

years,<sup>26</sup> the Court's solicitude remained not with would-be litigation financiers but rather with the interests of the legal system. Litigation financing "impedes the settlement of the underlying case" because clients become less likely to settle unless the settlement will cover the terms of the financing agreement.<sup>27</sup> Moreover, allowing litigation financing agreements "promotes speculation in lawsuits," which the Court viewed as an obvious social ill.<sup>28</sup>

The highest courts of Massachusetts and South Carolina have taken radically different approaches when applying champerty laws to litigation financing. Both have chosen to abolish their respective champerty laws. In *Saladini v. Righellis*, 687 N.E.2d 1224 (Mass. 1997), Lisa Saladini advanced \$19,229 to George Righellis so that he could pursue certain legal claims arising from his interest in real property. If he prevailed, Righelli would reimburse Saladini the advance plus fifty percent of his net recovery. Righelli achieved a favorable settlement of \$130,000 in the real estate litigation, but never informed Saladini of the settlement. When Saladini eventually learned of the settlement, she brought suit to enforce the financing agreement.

The trial court voided the agreement as champertous, but on appeal the Massachusetts Supreme Judicial Court vacated that decision, despite its acknowledgment that there was "little doubt that the agreement" was a champertous one.<sup>29</sup> The Court stated that the doctrine, which "arose in feudal

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<sup>26</sup>*Id.*

<sup>27</sup>*Id.* at 221.

<sup>28</sup>*Id.*

<sup>29</sup>687 N.E.2d at 1226.

England,” was no longer needed now that courts have such concepts as “unconscionability, duress, and good faith” at their disposal.<sup>30</sup> *Saladini* offered little explanation for how these doctrines might sufficiently address what for centuries had been considered illegal, not just undesirable.

Likewise, in *Osprey, Inc. v. Cabana Limited Partnership*, 532 S.E.2d 269 (S.C. 2000), Osprey, a real estate company, provided \$50,000 to sustain Cabana’s ongoing lender liability suit in federal court in exchange for a return of not more than \$150,000, but not less than \$50,000. The idea to seek financing from Osprey came from Cabana’s attorney, whose firm had represented Osprey in other matters. After Cabana received a settlement of \$650,000 in its federal case, it refused to pay Osprey. Osprey brought suit.

Again, as in Massachusetts, the trial court held that the agreement was champertous and thus unenforceable. On appeal, the South Carolina Supreme Court outrightly decided to “abolish champerty as a defense because we believe it no longer is required to prevent the evils traditionally associated with the doctrine as it developed in medieval times.”<sup>31</sup> After citing to *Saladini*, but without much commentary, the court found that the doctrines of unconscionability, duress, and good faith provided adequate defenses to unfair litigation financing agreements.

Neither court acted carelessly in setting aside long-established legal doctrines. The Massachusetts Court argued that there has been a “fundamental change in society’s view of litigation—from a social ill which . . . should be

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<sup>30</sup>*Id.* at 1225, 1227.

<sup>31</sup>532 S.E.2d at 279.

minimized to a socially useful way to resolve disputes.”<sup>32</sup> In other words, agreements that were once considered champertous could be viewed as actually *helping* to promote justice in society because those too poor to bring suit could now pursue financing and so have their day in court.<sup>33</sup> Moreover, the Massachusetts court argued, champerty law could actually promote injustice. If Righellis could void his obligation to pay Saladini, he would “be permitted to retain the full benefit of the positive result achieved . . . while he would not have to honor his obligations to Saladini, the person whose support made pursuit of the lawsuit possible.”<sup>34</sup> In the Court’s eyes, a robust application of unconscionability, duress, and good faith would prevent unfair litigation financing and also provide a more flexible set of tools for dealing with the changing world of litigation financing.

The reasoning in *Saladini* and *Osprey* has a certain appeal. On its face it supports concepts such as flexibility, egalitarianism, and a concern for fairness. Furthermore, when juxtaposed with *Rancman*, the decisions in *Saladini* and *Osprey* seem more in tune with modern realities, though under closer examination raising their own share of concerns.

Orderly resolution of disputes through courts of law certainly has more

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<sup>32</sup>687 N.E.2d at 1226 (internal quotations omitted).

<sup>33</sup>See Lauren Tara LaCapra, *Hedge Fund Hell: These Funds Sue You*, THE STREET, Jan. 23, 2009 (quoting attorney Paul Fischer: “if you have a litigant with a very just cause and valuable claim, who is drowned out because it’s far too daunting to pursue a claim against a very moneyed defendant, [litigation financing] might encourage more justice.”). Note, however, that access to the court system is not an absolute right under the Constitution. See, e.g., *Bodie v. Connecticut*, 401 U.S. 371, 382 (1971) (holding that a poor couple seeking divorce had a right to court access, but also noting “We do not decide that access for all individuals to the courts is a right that is, in all circumstances, guaranteed” by the Constitution); *United States v. Kras*, 409 U.S. 434, 450 (1973) (holding that indigent must pay filing fee in bankruptcy case and stating that *Boddie* “obviously stopped short of an unlimited rule that an indigent at all times and in all cases has the right to relief without the payment of fees.”).

<sup>34</sup>687 N.E.2d at 1226 n.6.

“social usefulness” than trial by combat or renegade justice, but the idea that the market and legal system should encourage and prolong lawsuits through third-party intermeddling flies in the face of universally promoted preferences of judicial economy, lawyer independence, alternate dispute resolution, and settlement. The practical effect of any litigation financing or calculated investment is to *sustain* litigation, and at a price that must be taken into account for any resolution to occur to a claimant’s satisfaction. The Ohio Supreme Court was not wrong when it suggested that litigation financing will force plaintiffs to raise the low end of what they might consider an acceptable settlement offer, especially when repayments must occur at 180 or 280 percent interest. These are not often-compromised liens, and now, rather than being illegal, enjoy an imprimatur in some states.

The observation in *Saladini* that the abolition of champerty will keep the unscrupulous from obtaining financing without paying the money back strikes more of a preference for modernizing a perceived old law than a reason. There are many agreements in American jurisprudence that are unenforceable because society has decided that it wants to proscribe that conduct. For instance, a contract to commit a crime remains unenforceable though an unfair benefit might inure to one party. The question is really one of societal preference, and an answer perhaps more appropriately reached through the legislature than judicial abolition, though certainly some champerty laws originate in the common law.

Moreover, there remains serious question whether the doctrines of duress, unconscionability, and good faith, which arguably have a history of less than

vigorous application by the courts, will serve as suitable or effective replacements for champerty. They have not been on their own effective deterrents for problems that invaded traditional lending practices at one time, and which remain carefully regulated.<sup>35</sup> We should not assume that litigation financing—that at times approaches its “investments” as requiring the financially distressed to repay 200 percent or more in interest—will be any better deterred in its practices. Indeed, it could well be assumed that the courts that have abolished champerty have concluded that exorbitant interest rates of this magnitude would not be considered unconscionable or lacking in good faith, and that the very act of entering a litigation financing agreement does not presuppose a situation of financial duress or unequal bargaining power, though really underpinnings to these arrangements.<sup>36</sup>

However appealing the concepts of greater access to courts and a more level litigation field, investing in other people’s quarrels for profit seems inherently unsavory. Should we encourage the practice of scouring the papers and trolling the courthouse for lucrative fights to finance, or offering to others the opportunity to gamble on or invest in outcomes that will inevitably affect some of the judicial system’s objective process and outside subjective settlements?

The North Carolina Court of Appeals recently struck more of a middle ground between Ohio’s vigorous application of champerty laws and the outright abolition of

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<sup>35</sup>See, e.g., 15 U.S.C. §§ 1601-1667; MASS. GEN. LAWS ch. 140D, §§ 1-35 (2009); N.C. GEN. STAT. §§ 24-1--24-11.2 (2009); OHIO REV. CODE ANN. §§ 1321.01-1321.99 (2009).

<sup>36</sup>See also *Anglo-Dutch Petroleum Int’l v. Haskell*, 193 S.W.3d 87, 104 (Tex. Ct. App. 2006) (litigation financing agreement not usurious or void against public policy, though interest rates reached 200 percent, saying that the rates varied from transaction to transaction “suggesting that the amount of the returns was bargained for by the parties”).

the doctrine by sister states. In *Odell v. Legal Bucks, LLC*, 665 S.E.2d 767 (N.C. Ct. App. 2008), Legal Bucks advanced car accident victim Nancy Odell \$3000 as she awaited the outcome of her personal injury suit. If she prevailed, depending on the date of resolution, Odell would owe Legal Bucks between \$4200 and \$9750, more than triple the advance. Odell obtained a favorable settlement of \$18,000 but then sought to void the agreement with Legal Bucks on a variety of grounds, including usury and champerty. On cross-motions for summary judgment, the trial court held that the agreement was not champertous, and the appellate court agreed.

Under North Carolina law, an agreement constitutes champerty only if it is “clearly officious and for the purpose of stirring up strife and continuing litigation,” said the court.<sup>37</sup> Though Legal Bucks had no stake in the suit other than a financial interest and though its involvement could have impeded settlement, North Carolina required “a higher level of intermeddling for a lender’s actions to be considered champertous.”<sup>38</sup> The court stated:

While the existence of Defendants’ lien on the proceeds of Plaintiff’s recovery may have influenced some of Plaintiff’s decision regarding her personal injury claim, Plaintiff simply has not demonstrated that Defendants attempted to control the resolution of her claim for the purpose of stirring up strife and continuing litigation.<sup>39</sup>

Rather than apply Ohio’s strict approach of finding nearly any financial intermeddling to be champertous, North Carolina cautiously interpreted its champerty laws to require some evidence of malice or ill intent by litigation

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<sup>37</sup>665 S.E.2d at 775.

<sup>38</sup>*Id.*

<sup>39</sup>*Id.*

financiers before such laws would apply. At the same time, North Carolina showed conservative restraint by not wholly abolishing champerty and instead accommodating modern realities within an arguably contemporary filter of once strict champerty laws.

In the end, one might accuse Massachusetts and South Carolina of maintaining, in the words of C.S. Lewis, a certain “chronological snobbery:” because the doctrine of champerty is old, it must also be irrelevant. The language in both *Saladini* and *Osprey* betrays a note of disdain for things ancient and medieval in suddenly abolishing a long-established legal doctrine.<sup>40</sup> On the other hand, while the Ohio decision is a model of clarity—nearly any involvement by a third party will constitute champerty—such an approach fails to account for the reality that litigation financing is rapidly becoming a mainstay of the legal system. The *Rancman* approach could leave a jurisdiction ill-prepared to deal with emerging developments in legal financing. The North Carolina approach represents more of a middle ground but is relatively toothless; it is hard to imagine many cases where “stirring up strife” would be the actual motivation for litigation financing.<sup>41</sup> The end result could well be a legal no-man’s land: there is a doctrine of champerty, but it almost never applies.

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<sup>40</sup>See, e.g., *Osprey*, 532 S.E.2d at 279 (“[w]e abolish champerty as a defense because we believe it no longer is required to prevent the evils traditionally associated with the doctrine as it developed in medieval times”).

<sup>41</sup>There are still cases nonetheless. A month ago, in *Del Webb Communities, Inc. v. Partington*, 2009 U.S. Dist. LEXIS 85616 (D. Nev. Sept. 17, 2009), a home contractor sued home inspectors who, after conducting their inspections, advised homeowners of their rights, provided information on how to file complaints for defects in construction, spent their own money to help finance these suits, coordinated hiring of a law firm, and all for a return of the judgment proceeds

Even this small sampling of recent cases reflects an ongoing struggle with litigation financing and champerty, and an unsettled state of the law from jurisdiction to jurisdiction that leaves us uncomfortably without a practical solution.<sup>42</sup> Over the years, courts have often been faced with tough situations in which old laws and modern realities collide in their courtrooms to await a judicial marrying of philosophies. The Ancient Greeks could never have fathomed modern entities such as Legal Bucks and Juridica, though certainly they had their versions of Legal Bucks, though perhaps not their iteration of Juridica. This makes the application of these laws to these new corporate creations especially difficult, but we must not forget that they remain laws. For those opposed to modern judicial activism, the legislature presents a better forum for balancing the competing interests of litigation financing.

### **III. EMERGING STATUTORY APPROACH**

In many ways, the competing interests between champerty and litigation financing—access for all to the legal system, settlement of cases, respect for legal

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collected by the homeowner. Under those circumstances, the district court granted partial summary judgment for the home builder on its theory of champerty. *See id.* at 9-16.

<sup>42</sup>Some additional recent cases involving discussion of champerty in other contexts include the following: *Carter v. Ozoeneh*, No. 3:08cv614-RJC, 2009 U.S. Dist. LEXIS 84441 (W.D.N.C. Sept. 16., 2009) (denying leave to amend to add maintenance claim based on futility); *Riggs v. Peschong*, No. 06-cv-366-JD, 2009 WL 604369 (D.N.H. Mar. 5, 2009) (granting motion in limine to preclude use of word “champerty” at trial in referring to money received under purchase agreement); *Merrill Lynch Mortgage Investors Inc. v. Love Funding Co.*, 2009 WL 3294928 (N.Y. Oct. 15, 2009) (answering certified questions from the U.S. Court of Appeals for the Second Circuit about New York’s statutory prohibition against champerty, saying a corporation that takes an assignment of a claim does not violate champerty if its purpose is to collect damages for losses on a debt instrument in which it holds a preexisting proprietary interest).

tradition, and adaptability of the legal system to modern businesses—can best be addressed legislatively. At least two jurisdictions have just pioneered this path.<sup>43</sup>

In 2008, Ohio legislators essentially overturned the champerty holding in *Rancman* by enacting House Bill 248 (codified at Ohio Revised Code § 1349.55) to address “non-recourse civil litigation advance contracts.” The legislation offers a model meant to deal directly with many concerns raised by recent state cases. Under the statute, to ensure that financing agreements are not unconscionable, they must include on their front page the dollar amount advanced, the total amount to be repaid in six-month intervals, and the applicable annual percentage rate. Also, the contract must include a right to cancel without penalty within five days and a written acknowledgement by the attorney representing the litigant that the attorney has reviewed the contract. Contracts must include in boldface type the statement that the financing company “shall have no right to and will not make any decisions with respect to the conduct of the underlying civil action . . . and that the right to make those decisions remains solely with you and your attorney.”<sup>44</sup>

Maine has adopted a similar law.<sup>45</sup> Its statute contemplates a typical litigation financing transaction: “If no proceeds in the civil claim or action are

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<sup>43</sup>Similar legislation is also under consideration in Connecticut. *See* Connecticut S.B. 534 (2008).

<sup>44</sup>OHIO REV. CODE ANN. §1349.55(B)(3) (2009).

<sup>45</sup>ME. REV. STAT. tit. 9-A, § 12-101 et seq. (2009).

received, the consumer is not required to pay the company.”<sup>46</sup> Financing contracts must include, on the front page, itemized fees and the total payout over a forty-two month period. An attorney must sign the document, and would-be litigants can cancel without penalty within five days. Uniquely, all legal funding providers must register with the state and appear on a website that allows consumers to “obtain comparative rate quotes.”<sup>47</sup> To register, a company must pay \$500, pass an “evaluation of the character, fitness, and financial responsibility” of the company, and then pay \$200 to renew its license every two years.<sup>48</sup>

Ohio and Maine demonstrate how a statutory approach might address the various issues raised in recent cases. For example, the disclosure of fees, interest rates, and the right of cancellation without penalty, combined with the requirement that attorneys review and acknowledge terms, should help counteract unconscionability, duress, and the like. By allowing litigation financing under these terms, the statutes enable the less fortunate or financially distressed to bring suit while at the same time protecting them from unscrupulous companies preying on their desperate circumstances.

The primary motivation behind champerty laws—that people should not stir strife in society by acquiring a financial stake in another’s litigation—becomes less compelling once the practice has the sanction of state (or potentially federal) law. With legal barriers to the fundamental transaction removed, market forces can

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<sup>46</sup>§12-102(2).

<sup>47</sup>*Id.* at § 12-104(5). The website is [www.maine.gov/pfr/consumercredit](http://www.maine.gov/pfr/consumercredit); once there, click on “Rosters.” There are only two companies listed, both based in Illinois.

<sup>48</sup>*Id.* at § 12-106(2).

intervene. Though stated a bit too hopefully, “no one is going to invest in a frivolous lawsuit because any money thus invested will be lost.”<sup>49</sup> Such thinking is consonant with Maine’s inclusion of a provision fostering competition between companies; to remain competitive, companies will need not only to offer good terms but also, like *Juridica*, avoid frivolous, “stirring-up-strife” cases in order to stay afloat financially.

Nonetheless, problems remain unaddressed by this statutory approach: aside from unhinging the backbone of lawyer independence, allowing financing agreements could drive up the lower limits of acceptable settlement offers. For example, a litigant who takes an advance of \$50,000 while hoping for a \$100,000 settlement now must seek a settlement that would cover the advance, the interest on the advance, and the original goal of \$100,000. Certain provisions in the statutes might help prevent settlements from rising too high; for example, the required disclosure of all fees and payouts up front might keep would-be litigants from accepting an advance under such bad terms that the settlement will rise to egregiously high levels. That is little reassurance, however. Ultimately, if litigation financing is sanctioned, settlements will inevitably be higher. Such is the price of abolishing champerty.

#### **IV. PRACTICAL CONCERNS AND CONSTRAINTS**

The practitioner should never be forgotten in legal philosophy. The overview of case and statutory law demonstrates that practitioners of the law face an

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<sup>49</sup>Susan Lorde Martin, *The Litigation Financing Industry: The Wild West of Finance Should be Tamed Not Outlawed*, 10 *FORDHAM J. CORP. & FIN. L.* 55, 77 (2004) (emphasis added).

uncertain landscape when it comes to litigation financing. If a client approaches an attorney with regard to litigation financing, what *can* that attorney do? What *must* he do? What must he *avoid* doing? Answers to these questions vary from jurisdiction to jurisdiction depending on the existence or vitality of champerty laws in that jurisdiction as well as professional conduct and ethical rules.<sup>50</sup>

One essential theme of the model ethical rules is the independence of the lawyer. The model rules remain particularly vigilant when third-party financing is involved. Rule 5.4(c) states that a lawyer “shall not permit a person who . . . pays the lawyer to render legal services for another to direct or regulate the lawyer’s professional judgment.”<sup>51</sup> Likewise, in the official comment to Model Rule 1.8, we read:

Because third-party payers frequently have interests that differ from those of the client, including interests in minimizing the amount spent on the representation and in learning how the representation is progressing, lawyers are prohibited from accepting or continuing such representations unless the lawyer determines that there will be no interference with the lawyer’s independent professional judgment and there is informed consent from the client.<sup>52</sup>

Furthermore, the comment to Rule 1.7 on concurrent conflicts of interest states that “if acceptance of the payment from any other source presents a significant risk that the lawyer’s representation of the client will be materially limited by the lawyer’s own interest in accommodating the person paying the lawyer’s fee,” then the lawyer

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<sup>50</sup>For a sampling of ethics opinions on litigation financing, see Arizona Opinion 91-22; Colorado Opinion 96/97-17; Connecticut Opinion 99-42; Florida Opinion 00-3; Illinois Opinion 92-9; Maryland Opinion 92-25; Michigan Opinion RI-321; New York Opinion 73-93; Nebraska Opinion 00-2; South Carolina Opinion 94-04; Tennessee Opinion 99-A-666.

<sup>51</sup>MODEL RULES OF PROF’L CONDUCT R. 5.4(c).

<sup>52</sup>*Id.* at R. 1.8 cmt. 11.

must gain the client’s informed consent and provide “adequate information about the material risks of the representation.”<sup>53</sup>

In these texts, we can discern that the legal system, even in states that openly permit litigation financing, remains wary of third-party involvement in lawsuits. These ethical rules echo the concerns raised in the case and statutory law: financing companies must have no say in the strategy of the suit, and the client must understand and freely consent to the third-party’s involvement. These texts also teach that, even if a given financing agreement is legal, an attorney must still jealously guard his independence or face an ethics sanction should the agreement affect settlement advice and strategies. In addition to the undesirable effects on settlement, litigation financing threatens this independence of lawyers, which has otherwise been zealously protected and essential to American jurisprudence.

Another area of practical concern is discovery. Procedural rules typically allow discovery of any nonprivileged matter relevant to a claim or defense. Litigation financing arrangements often require an application by the putative plaintiff, and some even mandate statements or endorsement by the representing attorney. While undoubtedly provided under the guise of a confidentiality agreement, there seems little question that these materials and statements should be held relevant. Work product protections likely will be unavailing when the third-party has not been retained to assist the attorney in providing legal advice or to provide other consulting. The rule on work product exists primarily to guard an

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<sup>53</sup>*Id.* at R. 1.7 cmt. 13.

attorney's mental impressions and pretrial strategy, but not something freely offered to an outside third-party. As a practice point, it makes sense to include questions about litigation financing in initial discovery.

From these observations, it is clear that litigation financing has a practical effect on the day-to-day practice of law. Practitioners should tread carefully when a client expresses interest in funding a suit with a litigation financing agreement. Even if the jurisdiction allows for such agreements, attorneys should be conservative with regard to divulging information, careful in preserving their independent judgment, and transparent about their own role in setting up the financing. In the area of discovery, a practitioner should take an aggressive approach toward financing agreements and disclosures. A financing agreement will have a significant impact on the strategies of both parties, and discovery of its existence could be important to securing a good and fair result.

## **CONCLUSION**

The growth of litigation financing in recent years has been extraordinary. What began as a small-scale entrepreneurial movement has now developed into transnational entities financing corporate lawsuits and managing hedge funds. From Las Vegas to London, the movement has burgeoned largely unchecked. That cannot continue. The long-established doctrines of maintenance, champerty, and barratry share a deeply-rooted societal concern that third-party involvement in legal actions could lead to a host of problems, and the manner in which some litigation financing companies conduct their business demonstrates that the

concern is not just with effects on the judicial system, but harm to those who fall prey because of financial conditions, exorbitant rates, and unfair terms.

Lamenting the swiftness with which some courts have dismissed the vitality of champerty laws in the face of modern developments provides only a complaint without a solution. The legal system must craft a more complete and consistent response to this rapidly changing industry, and given the less than adequate common law doctrines, the best hope may lie with the legislatures. Through provisions requiring clear disclosure of terms, fair rates, licensing of financiers, and the presence and advice of counsel before execution of agreements, statutes can curb some of the worst potential effects of litigation financing and also provide modern courts with a clear set of principles to apply, all the while allowing the market to operate freely. Such statutory schemes could also provide guidance to rank and file attorneys as they seek to counsel their clients about financing options and develop strategies for trial.

Failure to advocate such a position at this time will enable litigation financiers to dictate the contours of the industry. With potentially billions of dollars at stake, it would be naïve to think that industry players will wait for further legal developments before continuing to take advantage of the status quo and relative silence of the law (and, in some cases, endorsements). Litigation financing might be here to stay, but it does not have to stay in a form that undesirably affects the American legal system. Waiting longer will only mean the prospect of taming an ever-growing dilemma with increasingly inadequate and ostensibly outdated tools.