

WAITING FOR GOOD DOUGH: LITIGATION FUNDING COMES TO LAW

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Over the years, I have kept a mental list of the worst court decisions in the area of lawyer regulation. Admission to this list is limited to ten. Being wrong is not enough; the opinion must be very wrong. Even that is not enough. Is the opinion thoughtful nonetheless? Does it purport to be a serious treatment of the issue? Is the court influential? How much harm will the opinion likely cause? Has it since been limited? Each question must be asked and no single answer is determinative. Membership on the list shifts as new opinions appear and displace old ones or as cases are overruled. Someday, I may write an article called *The Ten Worst Opinions in Professional Responsibility*. Or maybe that should be the topic of a future panel discussion with each panelist taking an opinion or two.

My current list includes: *Balla v. Gambro, Inc.*,¹ *Birbrower, Montalbano, Condon & Frank v. Superior Court*,² *In re Cooperman*,³

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1. 584 N.E.2d 104 (Ill. 1991) (lawyer fired after he complied with state ethics requirement by revealing that employer had put a dangerous product on the market; *held*, employed lawyers do not have the same state retaliatory discharge claims available to other employees).

2. 949 P.2d 1, 13 (Cal. 1998) (denying fees to New York lawyers for work physically or “virtually” in California). *See also* Stephen Gillers, *Lessons from the Multijurisdictional Practice Commission: The Art of Making Change*, 44 ARIZ. L. REV. 685 (2002) (attempting a microscopic analysis of the opinion in article on the work of the ABA commission that responded to the issues the case raised).

3. 633 N.E.2d 1069, 1071 (N.Y. 1994) (forbidding “special nonrefundable retainer fee agreements”). I agree with the result in *Cooperman* and much of the analysis but believe the court wrote much too broadly and failed to define its terms.

Evans v. Jeff D.,⁴ *Leis v. Flynt*,⁵ *Mickens v. Taylor*,⁶ *Professional Adjusters, Inc. v. Tandon*,⁷ and *Rancman v. Interim Settlement Funding Corp.*⁸ *Ranta v. McCarney*⁹ had been on the list but *Birbrower* displaced it. *Birbrower* is from a more influential court and addresses a lawyer's virtual as well as physical presence in a state in its analysis of unauthorized practice of law by out of state lawyers.¹⁰ Its implications, if unrestrained, were breathtaking.¹¹

In this Article, I want to examine *Rancman*. The court's treatment of one issue it raised—the question of champerty¹²—is myopic, hostile, and superficial. The resolution of this issue on the facts before the court promotes injustice. The court introduced the issue into the case without the benefit of briefing.¹³ The Ohio legislature has since overruled *Rancman*.¹⁴ There is reason to believe that the Ohio Supreme Court will defer to the legislation, although we cannot know for certain until it addresses the question, as discussed below.¹⁵ But whatever the validity of the statute,¹⁶ the court's broad view of champerty, a concept that

4. 475 U.S. 717, 728-30 (1986) (noting that a settlement offer in a class action may be conditioned on waiver of statutory counsel fee; plaintiff's lawyer is ethically obligated to accept waiver).

5. 439 U.S. 438 (1979) (per curiam opinion issued without oral argument and holding that Ohio could deny *pro hac vice* admission to New York lawyer, who had been retained to represent an accused in Ohio state court, without giving any reason and without a hearing).

6. 535 U.S. 162, 174-76 (2002) (explaining that a trial judge has no obligation to investigate assigned defense lawyer's possible conflict of interest, even when she knows or should know of the conflict, unless lawyer personally raises the issue) (limiting *Holloway v. Arkansas*, 435 U.S. 475 (1978)).

7. 433 N.E.2d 779, 783 (Ind. 1982) (declaring unconstitutional on separation of powers grounds a detailed legislative scheme that regulated and licensed insurance adjusters to negotiate on behalf of consumers with their insurers following a property loss).

8. 789 N.E.2d 217 (Ohio 2003).

9. 391 N.W.2d 161, 166 (N.D. 1986) (denying Minnesota lawyer compensation for federal tax work performed for North Dakota client while lawyer was physically in North Dakota).

10. *Birbrower, Montalbano, Condon & Frank v. Superior Court*, 949 P.2d 1 (Cal. 1998).

11. *Birbrower* was eventually limited by rules 9.45-9.49 of the California Supreme Court, rules that do not go as far as Rule 5.5 of the Model Rules of Professional Conduct. But I have kept it on the list because it will remain influential, lacks a larger vision, and is from a prominent court.

12. *Rancman*, 789 N.E.2d at 219.

13. See *infra* note 54 and accompanying text.

14. See *infra* notes 92-95 and accompanying text.

15. See *infra* note 101 and accompanying text. The court may also see the legislation as an intrusion on its inherent power to regulate the bar.

16. OHIO REV. CODE ANN. § 1349.55 (West 2008)

emerged in dramatically different historical circumstances and has been rejected outright or much limited by other courts, deserves attention.¹⁷

Rancman and *Tandon* have something in common: the specter of a stranger in our midst.¹⁸ A non-lawyer has presumed to be part of our enterprise even if only at the periphery. *Birbrower* is a cousin to this alarm: The Court believed lawyers from elsewhere (New York) had invaded its turf and must suffer loss of fees for work they did on the matter while physically or virtually “in” California (but not for work they did when physically in New York, so long as they were not doing that work while “virtually” in California, via phone or e-mail, for example).¹⁹ We saw a similar anxiety over the appearance of *the other* in the debate over multidisciplinary practice (MDP).²⁰ While MDP certainly poses legitimate concerns that were thoughtfully raised during the American Bar Association (ABA) debate, some comments went over the top by projecting the end of the legal profession as we know it.²¹

Indeed, when we debate new rules, like those in the MDP proposal, we have a habit of predicting how they will affect behavior of lawyers and clients. However, we rarely bother with empiricism. This is not limited to threats posed by non-lawyers. That’s understandable. Prediction is easy. Anyone can do it. Empiricism is hard. No matter that the predictions may not come true. We continue to predict with only our imagination and ideas about human nature to guide us. This is of course inevitable. Often, the prediction of untoward consequences is intuitively so strong that we ought not chance a proposal. Sometimes empirical testing is not possible, at least not without great expense and demands of time. Sometimes none of this is so, and the prediction is not worth much.

17. See *Bluebird Partners, L.P. v. First Fid. Bank, N.A.*, 731 N.E.2d 581, 585 (N.Y. 2000) (tracing the history of the concept to “a type of French feudal tenure in land”). See also *Saladini v. Righellis*, 687 N.E.2d 1224, 1226 (Mass. 1997), as an example of one state high court that has abandoned the concept.

18. See *Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217 (Ohio 2003); *Professional Adjusters, Inc. v. Tandon*, 433 N.E.2d 779, 780 (Ind. 1982). *Tandon* gets a worse ranking than *Rancman*. It barely tries to justify its result beyond telling the legislature to stay off the court’s turf. *Id.*

19. See *generally*, *Birbrower, Montalbano, Condon & Frank v. Superior Court*, 949 P.2d 1 (Cal. 1998).

20. See American Bar Association’s Center for Professional Responsibility, House of Delegates Annual Meeting 7/11/00 Transcript (2000), http://www.abanet.org/cpr/mdp/mdp_hod_transc.html.

21. *Id.*

When the ABA debated Rule 5.7, which allows ancillary legal services under certain conditions,²² Larry Fox wrote that if lawyers and non-lawyers were permitted to co-own businesses that sell ancillary legal services, it “could expose the profession to levels of liability that have been unheard of until now” and also “undermin[e] our entitlement to self-regulation.”²³ Didn’t happen.²⁴ When the ABA debated new exceptions to Rule 1.6,²⁵ we heard predictions about the end of client candor and trust notwithstanding that many jurisdictions had long since adopted those very exceptions and a few even made them mandatory, seemingly without harm to the client-lawyer relationship.²⁶

Even when we do predict a risk of bad consequences based on our understanding of human nature and intuition, often we overlook similar situations where we tolerate the same risk without a second thought. I will focus on presumed threats when non-lawyers hover around the work of lawyers—the context for *Rancman*. We accept the presence of non-lawyers in so many ways. We even encourage it.

We permit the non-lawyer agents of organizational clients—including those who have vital control over the terms and conditions of a lawyer’s professional life—to instruct its lawyers on the client’s behalf.²⁷ But until the recent amendment to Rule 1.13,²⁸ we have not allowed the lawyers to protect the client if those non-lawyers were harming it through illegal conduct.²⁹ The unamended rule gave lawyers the option of withdrawing and remains the sole option under the amended version unless the misconduct is very serious indeed.

We allow non-lawyers to pay lawyers to represent clients.³⁰ While this may not be much of a problem where a friend or relative is paying the client’s bill, the stakes differ when the fees come from insurance companies. A law firm may be highly dependent on the good will of the

22. MODEL RULES OF PROF’L CONDUCT R. 5.7 (2007).

23. Lawrence Fox, *Restraint is Good in Trade*, NAT’L L.J., Apr. 29, 1991, at 17.

24. *See id.* Larry Fox might now say that he wrote “could”, not “would”, and surely his prediction *could* have come to pass. True, but he was adamantly against Rule 5.7. He was not making idle chatter.

25. MODEL RULES OF PROF’L CONDUCT R. 1.6.

26. *See* STEPHEN GILLERS, ROY D. SIMON, AND ANDREW M. PERLMAN, *REGULATION OF LAWYERS: STATUTES AND STANDARDS* (2010) (providing examples of jurisdictions that mandate disclosure of client confidences in some circumstances).

27. MODEL RULES OF PROF’L CONDUCT R. 1.13(a).

28. MODEL RULES OF PROF’L CONDUCT R. 1.13(c) (2007).

29. Further, the amendment (or some form of it) has been adopted only in a few states, including Arizona, Maryland, Michigan, Minnesota and New Jersey.

30. MODEL RULES OF PROF’L CONDUCT R. 1.8(f).

insurer, a frequent source of work. Meanwhile, the client makes a single appearance in the lawyer's life. Of course, we tell the lawyer to remember who the real client is,³¹ but we accept the risk. To reduce any danger of misplaced obedience, we could, but do not, tell law firms that they may not let any insurance company account for more than 10 percent of their income. We just trust the lawyers.

Malpractice insurance companies can tell law firms what they must do to reduce the risk of getting sued and thereby enjoy lower premiums. The influence may be entirely salutary; however, that's not the point. We allow it from a lay entity that has monetary leverage. Banks can monitor how law firms are run as businesses. This encourages banks to extend needed lines of credit to law firms. We let law firms include non-legal personnel in a "compensation or retirement plan . . . based in whole . . . on a profit-sharing arrangement."³² We choose not to see that as fee splitting on the somewhat artificial view that the non-lawyer's participation is in the gross profit, not the recovery in any single case. In Washington, D.C., we let non-lawyers have equity and managerial positions in law firms with no untoward consequences so far reported.³³

There's more. With informed client consent, we let law firms accept multiple representations that create concurrent client conflicts. However, either client (perhaps the greater source of present and future business) may subtly impose on the firm to act for its benefit if interests collide or strategies differ.³⁴ The firm may even tilt that way reflexively, without a client's imposition. Non-lawyers serve on the boards of and manage not-for-profit organizations whose legal staffs represent clients and where the organization may have a social or political agenda that varies from, and is potentially inconsistent with, the best interests of any particular client.³⁵ We let law firms share court-awarded legal fees with lay-controlled not-for-profit entities that either co-counsel with the firms or merely recommend them.³⁶ We let organizations run by lay individuals, like union legal service plans, represent their members.³⁷

31. *Id.*

32. MODEL RULES OF PROF'L CONDUCT R. 5.4(a)(3) (2007).

33. D.C. RULES OF PROF'L CONDUCT R. 5.4 (2008).

34. MODEL RULES OF PROF'L CONDUCT R. 1.7(a).

35. MODEL RULES OF PROF'L CONDUCT R. 5.4(d). A lawyer may not work for an organization authorized to practice law if the organization has lay management, but only if the organization practices law for a profit.

36. MODEL R. 5.4 (a) (4).

37. *United Transp. Union v. State Bar of Mich.*, 401 U.S. 576, 584-86 (1971).

I do not oppose these arrangements. Some may be constitutionally protected.³⁸ Each is beneficial, a symbiosis that works to the advantage of all. Some, as when officers of an organizational client instruct its lawyers, are unavoidable because (biological) non-clients must do that. I list various ways in which lay persons may participate along with lawyers in the rendition of legal services or may be positioned to exert influence on how lawyers render those services only to make the point that the risk of improper lay interference is embedded in many client-lawyer relationships. Yet we either accept or overlook the risk. Only sometimes do we quiver at the prospect of improper lay influence to which lawyers will succumb. It can be hard to explain the differences in our tolerance for risk.

Here, I want to discuss one particular way in which a representation may encounter lay influence. This is through companies offering to buy a share in a litigant's claim. Let's look at this economically and use an example. In late 2003, Janie Millicent Deall, a 56-year-old Akron, Ohio resident is hurt when a display case at Carl's Shoe and Sneaker Emporium falls on her while she is in the store buying sandals. She loses consciousness. An ambulance takes her to the hospital. As it turns out, Janie's injuries are not life threatening, but they are serious. She spends four days in the hospital and will need home health care for several months. Her medical insurance will cover less than half of her expenses. She will be unable to return to her job as an assistant at an architectural firm for eight or nine months, perhaps a year. Her sick leave will cover only two weeks' pay. Her employer's disability insurance provides a pittance. She has only modest savings. None of her usual expenses are going away and, indeed, her cost of living is going up because of medical and other bills related to the accident.

As it happens, the most valuable asset Janie has to sell at the moment is her claim against Carl's Shoe and Sneaker Emporium, a substantial business owned by a company with twelve other shoe and sneaker emporiums in the Midwest. Can Janie sell an interest in this asset to keep her afloat while she sues Carl's? She has been told it can take two or more years before she gets a reasonable settlement offer or a trial.

38. *Id.* at 585-86 (holding that union plans are constitutionally protected).

Yes and no. She can sell her lawyer an interest in her claim for about one-third of her recovery.³⁹ Her lawyer will even pay the thousands of dollars needed to prosecute the action and Janie will not have to reimburse these unless she prevails.⁴⁰ In exchange, Janie gets excellent legal representation. But the lawyer cannot help Janie with her rent and utility bills, medical costs, or other expenses of daily living.⁴¹ Janie knows that she will not be able to hold out until she can return to work.

Who else will buy her claim? There is one buyer authorized to pay her cash for her claim—cash she can immediately use to pay the rent and doctors and buy food until she can start working again. It is Carl's Shoe and Sneaker Emporium, or more likely its insurance company. Carl's (or its insurer) is in a rather luxurious position. It is under no time pressure. It is, furthermore, the only authorized purchaser of Janie's claim, the only one allowed to bid on it. Now it requires no MBA to recognize that if one person is under duress and needs to sell something and another person is the only one legally allowed to buy it, the buyer has an enormous advantage.

Assume tort lawyers in Akron agree that Janie has a very good case. She has a 90 percent chance of getting \$300,000, a conservative number, and a 50 percent chance of getting more than \$400,000. Discounting the risk of loss (10 percent), the value of her claim is at least \$270,000. If a third goes to her lawyer, it means the claim is worth \$180,000 to Janie, ignoring for our purposes the time-value of money. If the cost of litigating the case is \$10,000, which Janie must pay from her proceeds, she can expect \$170,000 in two years or so.

Carl's insurer is willing to buy Janie's claim today for \$75,000, which will net Janie \$50,000 after she pays her lawyer (assuming no disbursements). Janie does not see this as a good deal and neither does anyone else, but Janie needs cash and her situation is growing more dire monthly. Is there no one else out there willing to invest in her claim? After all, it has a 90 percent chance of success and the \$300,000 target is conservative. Surely, she asks her lawyer, someone will partner with her even if the lawyer cannot. Right?

39. *Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217, 220 (Ohio, 2003) (court assumes a 30 percent contingent fee).

40. OHIO. RULES OF PROF'L CONDUCT R. 1.8(e) (1) (2009). When *Rancman* entered her contract, Ohio had the Code of Professional Responsibility. *Rancman*, 789 N.E.2d at 221. But I think it more useful now to use the current professional conduct rules. Nothing turns on it.

41. OHIO. RULES OF PROF'L CONDUCT R. 1.8, cmt. 10.

And this is where Janie's lawyer tells her about *Rancman*. Ms. Rancman was injured in a one-car collision.⁴² She sued State Farm for uninsured motorist benefits.⁴³ She then contacted a litigation funding company.⁴⁴ Eventually, that company and another company to which it referred her, advanced Rancman a total of \$7,000.⁴⁵ In exchange, Rancman promised to pay the companies the first \$19,600 she recovered if the case were resolved within twelve months, the first \$25,000 she received if resolution took twelve to eighteen months, and the first \$30,400 she received if the dispute was resolved within twenty-four months.⁴⁶ Rancman would pay nothing if she recovered nothing.⁴⁷

Rancman settled for \$100,000 within twelve months and sued the two companies to avoid payment.⁴⁸ She alleged that the defendants were guilty of "unfair, deceptive and unconscionable sales practices. . . ." ⁴⁹ The magistrate found in her favor on a different theory.⁵⁰ The magistrate ruled that the money was a loan and the rate usurious.⁵¹ On appeal, the defendants argued that the money was an investment, not a loan, so the usury law did not apply.⁵² The Supreme Court did not address that argument.⁵³ Although neither party raised the issue and there was no briefing on it,⁵⁴ the Supreme Court offered a third reason to refuse to enforce the agreement. It held that the defendants were guilty of maintenance and champerty, and the contract therefore void.⁵⁵ The court wrote:

The advances sub judice constitute champerty because [the defendants] sought to profit from Rancman's case. They also constitute maintenance because FSF and Interim each purchased a

42. *Rancman*, 789 N.E.2d at 218.

43. *Id.*

44. *Id.*

45. *Id.* at 218-19.

46. *Id.* The court does not say what Rancman's liability would be if the case had been resolved after twenty-four months. *Id.*

47. *Id.*

48. *Id.* at 219.

49. *Id.*

50. *Id.*

51. *Id.*

52. *Id.*

53. *Id.*

54. *Id.* at 221 (Christley, J., concurring). Deciding this important issue without the benefit of argument is one reason this case goes on my ten worst list.

55. *Id.* at 219.

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

Equally troubling is a champertor's earning a handsome profit by speculating in a lawsuit and by potentially manipulating a party to the suit

Except as otherwise permitted by legislative enactment or the Code of Professional Responsibility, a contract making the repayment of funds advanced to a party to a pending case contingent upon the outcome of that case is void as champerty and maintenance. Such an advance constitutes champerty and maintenance because it gives a nonparty an impermissible interest in a suit, impedes the settlement of the underlying case, and promotes speculation in lawsuits. The advances made to Rancman constituted champerty and maintenance. Consequently, the contracts requiring their repayment are void and shall not be enforced.⁵⁶

The court illustrated the disincentive to settle arithmetically.⁵⁷ For Rancman to recover any additional money, State Farm would have to offer more than \$28,000, assuming Rancman's lawyer's fee was 30 percent of the recovery and that settlement occurred within twelve months.⁵⁸ In other words, Rancman had no incentive to settle for less than \$28,000 because she would get nothing from the settlement.⁵⁹

To further illustrate the effect on incentives, the court went on to assume that Rancman wanted to walk away with \$80,000 less counsel fees (\$24,000), or \$56,000 net.⁶⁰ If that were her goal, she would have had to hold out for \$98,000 in order to recoup the additional \$12,600 (net of counsel fees) she would need to pay the defendants their profit (on top of their original payment).⁶¹

Now, there are two ways to read the court's analysis. They are not mutually exclusive. The simplest reading to which the opinion explicitly lends itself is syllogistic. Major premise: Because maintenance and champerty violate public policy, a contract that falls within either

56. *Id.* at 220-21.

57. *Id.*

58. *Id.* at 220.

59. *Id.*

60. *Id.* at 221.

61. *Id.* The court's assumption, in order to prove its point, of a plaintiff whose bottom line for settlement is \$80,000 is a little too convenient. *See infra* note 115.

category is “void” under Ohio law.⁶² Minor premise: The defendants engaged in maintenance and champerty.⁶³ Conclusion: The contract is void.⁶⁴ End of story.

Even assuming the accuracy of *Rancman*'s syllogism,⁶⁵ the fact is that the major premise is a product of common law, the court's own law.⁶⁶ The court could have narrowed the definitions of champerty and maintenance. Elsewhere, courts have declined to follow *Rancman* because the doctrine of champerty in their states is narrower.⁶⁷ It requires that the funding company have instigated the litigation.⁶⁸ But here, *Rancman* had already sued and she then went to the defendants.⁶⁹ They did not inspire her to sue.⁷⁰

Separately, in defense of its major premise, the court identified three harms that the current Ohio law prevented.⁷¹ This is the other way in which the court justified its holding. The first harm the court identified, as illustrated with its arithmetic models, is that litigation-funding investments give a party like *Rancman* “a disincentive to settle her case.”⁷² Second, the defendants would earn “a handsome profit by speculating in a lawsuit.”⁷³ Third, the investment created a risk of “potentially manipulating a party to the suit.”⁷⁴ Only the first harm, the disincentive to settle, is explained in any depth.⁷⁵ The other harms are just declared.⁷⁶

Recognition that the investment gave *Rancman* a “disincentive to settle her case” (or to settle for less than a certain sum) is of course arithmetically true, as the court nicely illustrated, and I'll say more about that below.⁷⁷ The court did not spell out what it meant by

62. *Rancman*, 789 N.E.2d at 221.

63. *Id.*

64. *Id.*

65. *Id.*

66. See *Bluebird Partners, L.P. v. First Fid. Bank, N.A.*, 731 N.E.2d 581, 585 (N.Y. 2000).

67. See, e.g., *Odell v. Legal Bucks, Inc.*, 665 S.E.2d 767, 775 (N.C. App. 2008).

68. *Oliver v. Bynum*, 592 S.E.2d 707, 711 (N.C. Ct. App. 2004).

69. *Rancman*, 789 N.E.2d at 218.

70. *Id.*

71. *Id.* at 220.

72. *Id.*

73. *Id.* at 221.

74. *Id.*

75. *Id.* at 220.

76. *Id.* at 221.

77. *Id.* at 220-21. See *infra* notes 104-16 and accompanying text.

manipulation.⁷⁸ If the fear is that the investors will interfere with litigation strategy, the fear is misguided. The solution is to insure that Rancman's counsel recognizes only her as the client. We say the same when *A* pays counsel to represent *B*, including when *A* is an insurance company that is a good source of the lawyer's business.⁷⁹ Instead, the court could have used its rulemaking power to forbid lawyers to share non-public information with investors, like the defendants, or to take instructions from them about the matter.

As for the reference to a "handsome profit by speculating in a lawsuit,"⁸⁰ what can the court mean? The profit was meant to recognize the risk of non-recovery. Rancman's lawyer took the same risk when he "bought" an interest in her claim in exchange for work.⁸¹ Contingent fees can also be handsome—higher than the market for hourly fees—precisely because of this risk.⁸² Why can't the defendants' profits also be handsome? It is no answer to say it is because they are not lawyers. That simply restates the conclusion. It is no answer to say that lawyers who work on contingency perform a valuable service for the justice system. We must ask whether the defendants here do as well.

The word "speculating"⁸³ is rhetorical and emotive and was obviously meant to be. Were the defendants speculating? They saw a valuable property, a claim, and wished to invest in it, recognizing the risks. We can assume they investigated the merits of Rancman's claim and adjusted their offer accordingly. "Speculating" is not a word that promises to advance serious analysis of the issues before the court. And of course we can use the same word about contingency fee lawyers, but we don't.

Perhaps, what the court means, although it did not say so, was that the business of investing in lawsuits was unregulated. Investors can charge whatever they like, not merely handsome but exorbitant profits.

78. *Id.* at 221.

79. OHIO RULES OF PROF'L CONDUCT R. 1.8(f) (2009). Ohio modifies the ABA version of this rule by adding a requirement that lawyers who are retained by an insurer to represent an insured must give the insured a "Statement of Insured Client's Rights," which describes the lawyer's obligations to the client and the insurer. *Id.* R. 1.8(f)(4). See also MODEL RULES OF PROF'L CONDUCT R. 1.8(f) (2007).

80. *Rancman*, 789 N.E.2d at 221.

81. See *id.* at 220-21. See also *McKenzie Constr. v. Maryland*, 823 F.2d 43, 44-45 (3rd Cir. 1987) (contingent fee that yields \$1,430 hourly in 2008 dollars is not unreasonable even though it is thirteen times the lawyer's hourly fee).

82. *McKenzie*, 823 F.2d at 47-48.

83. *Rancman*, 789 N.E.2d at 221.

Plaintiffs are often desperate. (Of course that is also true when there is only one “buyer,” the defendant in the underlying action, which we manage to overlook.) At least, the contingent fee that lawyers may charge is (or can be) limited by court rule.⁸⁴ There is no rule capping the profits of a litigation funding companies, and the court was not about to write one.

Perhaps this is why the opinion mentions legislation.⁸⁵ The court wrote: “Except as otherwise permitted by legislative enactment or the Code of Professional Responsibility, a contract making the repayment of funds advanced to a party to a pending case contingent upon the outcome of that case is void as champerty and maintenance.”⁸⁶ It appears that the court may have been inviting the legislature to regulate the field.⁸⁷

But if the court meant to extend that invitation, it had an awfully strange way of doing so. Its language is stridently hostile to the whole business.⁸⁸ The court wrote that champerty and maintenance “have been vilified in Ohio since the early years of our statehood.”⁸⁹ It quotes precedent for the proposition that maintenance is “an offense against public justice [that] . . . *perverts* the remedial process of the law into an engine of *oppression*.”⁹⁰ It writes that “[a]n intermeddler is not permitted to *gorge* upon the fruits of litigation.”⁹¹ What lawmaker will read those sentences as encouragement to attempt to legalize such harmful practices?

Some lawmakers did, though. Five years later, Ohio enacted a law that permits a “non-recourse civil litigation advance” and purports to regulate these.⁹² The regulation is light. Essentially, it requires certain notices to the plaintiff (called a “consumer”) in twelve-point type, including both the “total dollar amount to be repaid” and the “annual percentage rate of return” for varying six-month periods.⁹³ The law, which apparently applies only in contingent fee cases, gives the

84. See, e.g., *McKenzie*, 823 F.2d at 43-48.

85. *Rancman*, 789 N.E. 2d at 221.

86. *Id.*

87. See *id.*

88. See *id.* at 220.

89. *Id.* (emphasis added).

90. *Id.* (emphasis added) (internal quotes omitted).

91. *Id.* at 221 (emphasis added).

92. OHIO REV. CODE ANN. § 1349.55 (West 2008).

93. *Id.*

consumer a five-day cooling off period.⁹⁴ The consumer must be “a person or entity residing or domiciled in Ohio.”⁹⁵

What the law certainly does not do is prevent “a handsome profit”⁹⁶ to the company making the “advance.”⁹⁷ The profit can be drop-dead gorgeous and still legal. The rate of return is not addressed. The statute also does not reflect *Rancman*’s alarm over disincentives to settle.⁹⁸ As for the danger of the company “manipulating” the consumer,⁹⁹ the statute says only that the contract must provide (again in twelve-point type) that “the company will not make any decisions with regard to the underlying civil action or claim or any settlement or resolution thereof and that the right to do so remains solely” with the consumer and his or her attorney.¹⁰⁰ No language forbids the attorney to share confidential or any other information with the company, perhaps because that authority, such as it is, is left to the professional conduct rules and substantive law.

Whether the Ohio Supreme Court will defer to this light regulation or see it as an infringement on the court’s inherent power to regulate the practice of law, we have yet to learn.¹⁰¹ For my purpose here, the question is whether allowing companies to make non-recourse advances is a good thing, and surely it is. No one has to take an advance. The only question is whether one should be available for those who choose to take it. Let us enumerate their value and some of the contrary arguments:

94. *Id.*

95. *Id.* The constitutionality of this last limitation is dubious. The law would not benefit a resident of Indiana harmed by an Ohioan in Ohio, even if Ohio was the sole place of personal jurisdiction. But the Ohioan who sues the Indianan in Ohio could make use of the law. But that’s a debate for another day.

96. *Rancman*, 789 N.E.2d at 221.

97. OHIO REV. CODE ANN. § 1349.55.

98. *Rancman*, 789 N.E.2d at 220.

99. *Id.* at 221.

100. OHIO REV. CODE ANN. § 1349.55.

101. Like other state high courts, the Ohio Supreme Court has held that it has inherent power over the conduct of lawyers and admission to the bar.

“[I]t has been methodically and firmly established that the power and responsibility to admit and discipline persons admitted to the practice of law, to promulgate and enforce professional standards and rules of conduct, and to otherwise broadly regulate, control, and define the procedure and practice of law in Ohio rests inherently, originally, and exclusively in the Supreme Court of Ohio.”

Shimko v. Lobe, 813 N.E. 2d 669, 673 (2004). The extent to which a state high court is willing to share this power varies from place to place. See STEPHEN GILLERS, *REGULATION OF LAWYERS: PROBLEMS OF LAW AND ETHICS* 7-9 (8th ed. 2009).

a. *Litigation funding encourages frivolous litigation.* Highly dubious. These are non-recourse advances in which the company gets paid only if the consumer does. It may get nothing or less than its advance. Companies that pay plaintiffs to bring frivolous cases will soon go bankrupt. The incentive to investigate closely and pick the best cases based on historical settlement patterns and verdicts is strong. That's what good contingent fee lawyers do, too.

b. *Litigation funding exploits the vulnerable plaintiff.* The plaintiff may be in financial straits or merely wish to spread the risk. But let us assume the former because the latter plaintiff is by definition not financially vulnerable. Without the advance, as illustrated with my example of Janie Millicent Deall, the plaintiff can still be exploited, but solely by the defendant who can "buy" the entire claim for far less than market value. The advance gives the plaintiff the chance to sell part of her claim and retain an interest in part of it. The plaintiff may be pressed by her financial predicament to take the advance, but without it she is pressed to sell her entire claim for less than her due, possibly far less. Her choice is an economic one, and the cash from the litigation funding company may be the more attractive option. In any event, the availability of litigation funding means she will be able to make a choice. She can have multiple buyers.

c. *The consumer lacks information to make an informed choice.* That need not be. Despite the Ohio law's odd provision¹⁰² that purports to eliminate the plaintiff's lawyer as a source of advice on the transaction, the lawyer is in a perfect position to give the plaintiff critical information. For starters, an experienced lawyer can help the plaintiff shop and compare offers available from other companies. (Even without the lawyer, the client can shop around.) Beyond that, the lawyer can help evaluate the deal by making informed judgments about the several variables that should influence the client (as they likely influenced the lawyer in taking the matter): What are the chances of success? What is the range of the expected recovery? And how long will resolution take? The lawyer can offer several "endgame" examples. "If you recover X

102. The law says that the contract must say in twelve-point type: "YOU ACKNOWLEDGE THAT YOUR ATTORNEY IN THE CIVIL ACTION OR CLAIMS HAS PROVIDED NO . . . FINANCIAL ADVICE REGARDING THIS TRANSACTION." OHIO REV. CODE ANN. § 1349.55 (West 2008). Whose idea was this? The plaintiff's lawyer is best positioned to advise on the wisdom of the proposal. Why must this language be in the contract? Perhaps the trial bar wanted to exempt itself from any responsibility for a plaintiff's decision to accept money from a litigation funding company.

dollars in Y months, I get so much of it, the company gets so much, and you get the rest.” And so on, with different values for X and Y.

d. *The potential rewards to the company are too “handsome.”*¹⁰³ We don’t know what lobbying went into the Ohio bill. It would be interesting to learn but that is beyond the focus of this article. Perhaps the funding companies blocked a cap on their potential recovery. A law could be written limiting recovery just as laws or court rules limit a lawyer’s contingent fee in personal injury matters. On the other hand, that may not be feasible because a fair return on an investment will depend on variables affecting the risk that cannot easily be captured in a legislative formula. These include the potential scope of recovery, likelihood of recovery (how risky is this claim?), and predictions about trial calendars.

But even without a limit on the investor’s return, the market can impose a limit if several companies compete for the business. Furthermore, the presence of funding companies tells the defendant that it is not the sole buyer in the market for the plaintiff’s claim. In other words, the mere existence of litigation funding can inspire a defendant to increase its settlement offer to enable the plaintiff to avoid having to pay the handsome profit. The defendant can no longer confidently take advantage of a plaintiff’s possibly desperate situation. It has competition.

e. *Lawyers will succumb to the entreaties of the funding companies to press their clients to accept offers that may be inadequate.* This is what I call the “stop me before I kill again” reason. Lawyers are weak. Funding companies are strong. Lawyers want them to fund future plaintiffs. Funding companies will not do that if the lawyers fail to follow their coded instructions to do what is best for the funding companies. A funding company’s interests conflict with the plaintiff’s interest. The company will be happy with any settlement that yields the contract profit regardless of what remains for the plaintiff. But that may not be good for the plaintiff.

This argument proves too much. A similar argument can be made when a lawyer gets an even modest amount of work from insurance companies to represent their insureds. Anyway, even assuming there is any intuitive appeal to the prediction of how lawyers will behave, there is something truly perverse in arguing that commercial arrangements otherwise good for clients must be forbidden because they may

103. *Rancman*, 789 N.E.2d at 221.

sometimes cause lawyers to violate their ethical obligations and succumb to the wishes of third parties to the disadvantage of the very same clients.

f. *Litigation funding reduces the likelihood of settlement.* This can be true for two reasons. First, settlement may not occur, or occur as quickly, because the funds ease the plaintiff's financial distress and enable her to avoid an economically unfair resolution. That's a good thing. No legitimate policy can support denial of funding as a way to squeeze plaintiffs without financial reserves and thereby force an early unjust settlement, especially when defendants can use procedural strategies to buy delay.

The second way in which litigation funding impedes settlement is where a borrower who did not need money—or did but because of the funding agreement no longer does—rejects reasonable settlement offers because they will net him too little or nothing once he pays the funding company. In *Rancman's* example, the court wrote that the offer would have to be \$98,000 if Rancman wished to net \$80,000 less counsel fees.¹⁰⁴ Rancman would want the extra \$18,000 to pay the funding company after deducting her counsel's fee on the increment.¹⁰⁵ Otherwise, Rancman would, in this hypothetical, have accepted the \$80,000.¹⁰⁶

We can assume that litigation funding will influence settlement positions. Not only will the funded plaintiff *be able* to stay in the game longer because of the funders' money, but because she has to share any settlement or judgment, she may now hold out for even more money than she would otherwise have been prepared to accept, further delaying or entirely preventing settlement and forcing a trial.¹⁰⁷ Even if the plaintiff does appreciate that she can no longer keep *as much of the money* now that she has a partner, she may still want more than she would previously have accepted in settlement in order to recoup at least part of the difference. In other words, the plaintiff will wish to shift to the defendant at least some responsibility for the cost of her transaction with the funders. So while the cash from the litigation funding company may save a plaintiff from having to succumb to an improvident

104. *Id.*

105. *Id.* She would also have to repay the \$7,000 she received, but that repayment does not affect her net recovery.

106. *Id.*

107. *See id.*

settlement, the flip side is that the obligation to the company may now cause her to hold out for unrealistic offers or go to trial.

This is a legitimate concern, but there are several reasons to dismiss it. First, even if the prediction that the plaintiff's changed circumstances will increase the likelihood of trial is true, we must ask whether that prospect as a matter of public policy justifies denying the needy plaintiff the financial means that will enable her to reject a settlement offer that is too low. Which harm is worse?

Let's consider the various harms. The harm to the plaintiff is that she may do no better or worse at trial than the last settlement offer before trial, perhaps much worse. We can dismiss that concern because it is a product of her strategic (presumably counseled) choice. The litigation funders will have to wait longer for their money and may not get paid at all or as much, depending on the verdict. But this is a danger of which they will have been aware when they set their "price" and against which they can partly protect themselves, as discussed below.

The defendant will have the added expense of trying the case and the plaintiff's lawyer will have to spend the extra time required to try the case and perhaps extra disbursements. The defendant of course can avoid a trial with a more generous settlement offer and the plaintiff's lawyer will be aware of any increased likelihood of trial when he accepts a client who may turn to a litigation funding company. In fact, the plaintiff's lawyer may see the existence of these companies as a good thing on the whole, because even though funding may make trial more likely or make cases take longer to settle, absence of funding can avoid early, low settlements.

Last is the harm to the court system, which may now be forced to try a case that would otherwise have settled. Let's accept that this is something we should try to avoid. I first question whether we can even say that the prospect of trial is appreciably more likely. There are ways to hedge that risk. The funding company can dim the plaintiff's enthusiasm to press for trial ("what do I have to lose?") by, as in *Rancman* and as recognized in the ensuing legislation, calibrating the return on its investment to the length of time before the matter is resolved.¹⁰⁸ The longer it takes to resolve, the greater the company's return.¹⁰⁹ In *Rancman* itself, the funding companies would have been entitled to \$19,600 if the case ended within twelve months, but their

108. *Id.* at 218-19.

109. *Id.*

entitlement would increase by \$5,400 in each ensuing six-month period.¹¹⁰ To net each increment, the borrower would have had to recover as much as \$8,000 in order first to pay her lawyer's contingent fee.¹¹¹ That reality should encourage a plaintiff in Rancman's position to treat settlement offers seriously. In other words, Rancman did have something to lose by delay, namely keeping more of the eventual payment.¹¹² And of course Rancman herself did settle within twelve months, before she could know whether the court would uphold her agreement with the funding companies, which raises the possibility that the agreement actually encouraged settlement.¹¹³

Furthermore, if the defendant is entitled to learn of the litigation funding agreement or does learn of it informally, as is likely, it will understand that the chances to settle are greatest before any current six-month period ends. The plaintiff will keep more of the money. Indeed, the plaintiff may choose to present this fact in negotiations. "I'll take so much now but I'll want more next month." And as stated above, the very fact that a plaintiff in need can get litigation funding at all—the fact that there are other buyers for at least part of her claim—should alert the defendant that it cannot count on plaintiff's financial exigency to get a lower price. It is no longer a monopolistic buyer. It may even make an attractive settlement offer *before* the plaintiff enters the market for, or commits to, litigation funding. The plaintiff may use that prospect in early negotiation. Indeed, for all we know, State Farm made the \$100,000 offer it did when it did¹¹⁴ because Rancman had secured litigation funding.

Nor should we assume that the funded plaintiff will act irrationally. While the fact that the funding company has become her partner may cause her to desire a greater settlement, that fact does not change the value of her claim. If she had a 90 percent chance of recovering \$300,000 before she accepted the funding, that remains her chance. She must still weigh any offer against the time it will otherwise take to get to judgment (and the increment in the funding company's profit if it does

110. *Id.*

111. *See id.*

112. *See id.*

113. *Id.* at 219.

114. *Id.*

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take longer) and the risk of loss or of recovering less than what the lawyer has said the case is worth.¹¹⁵

For these reasons, we should not assume that litigation funding will increase the number of trials. We certainly should not make policy based on such a possibility without proof when the consequence is to force financially pressed plaintiffs to lose the reasonable value of their claim. Besides, even if there are more trials, so what? That puts a burden on the court system, but it's a burden to try cases, which is why the court system exists in the first place. It's what judges get paid to do. Are we really prepared to say that a state's justice system will not allow a plaintiff to get the funds she needs to persist in an effort to secure just compensation because then judges will have to try some number of cases that would otherwise have settled, a number we can't even quantify? I hope not.

Maybe, given Ohio's corrective legislation,¹¹⁶ I'll remove *Rancman* from my list of ten worst cases, or will once the Ohio courts uphold the statute. I won't have any trouble finding a new case to take its spot. The pool of really bad decisions, while thankfully shallow, never seems to run dry.

115. This is why *Rancman's* hypothetical of a plaintiff who wants to settle for \$80,000 is not useful. *Id.* at 221. It allows the court to posit an intransigent plaintiff ("\$80,000 and not a penny less!"), and therefore an inevitable set of consequences that must follow, while ignoring other factors, including counsel's advice and predictions, which may influence any plaintiff's initial settlement position.

116. OHIO REV. CODE ANN. § 1349.55 (West 2008).