School of Law

ALTERNATE DISPUTE FINANCING AND LEGAL ETHICS: FREE THE LAWYERS!

Michael I. Krauss,
George Mason University School of Law

***Mississippi College Law Review,* Forthcoming**

George Mason University Law and Economics Research Paper Series

13-54

ALTERNATE DISPUTE FINANCING AND LEGAL ETHICS: FREE THE LAWYERS!

*Michael I. Krauss**

ABSTRACT

As is the case for many of our entitlements, our rights of action are protected by a less-than-full property rule. As a result, financing of litigation has been limited. The recent rise of alternate dispute financing has raised serious ethical problems. In this Article, I discuss those problems, dismiss some (but not all) of them, and suggest that pushing the protection of our entitlement to sue closer to a property rule might alleviate those problems that remain.

I. INTRODUCTION

Every legal jurisdiction has some "inalienability rules"[1] scattered among its many property rule protections of entitlements. For example, I cannot sell myself into slavery. Relatedly, I can "lease" you my arm (i.e., I can chop wood for you for pay for a certain time), but I cannot sell it to you. I can neither sell nor buy my entitlement to vote, though I may legally "give it away" by declining to exercise it (unless I live in Australia, Belgium, Brazil or one of nineteen other countries).[2] I may give my blood (thus my entitlement to my blood is protected by a partial inalienability rule), but in many states I

* Professor of Law, George Mason University. Many thanks to Wesley Weeks for his always excellent research assistance. The title is a takeoff on *Free the Grapes*®: www.freethegrapes.org, an organization dedicated to the abolition of archaic wine distribution laws. This Article queries whether the anti-maintenance rule (ABA Rule 1.8(e)) is equally archaic.

[1] *See* Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972); Michael I. Krauss, *Property Rules vs. Liability Rules*, *in* 2 ENCYCLOPEDIA OF LAW & ECONOMICS 782, 786–87 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000), *available at* http://encyclo.findlaw.com/3800book.pdf.

[2] *Compulsory Voting,* WIKIPEDIA, http://en.wikipedia.org/wiki/Compulsory_voting#By_countries (last visited Aug. 23, 2013) (Countries that enforce their compulsory voting laws include Argentina, Australia, Brazil, Democratic Republic of the Congo, Luxembourg, Peru, Singapore, Uruguay, and one canton in Switzerland. Countries that have compulsory voting laws but do not regularly enforce them include Belgium, Bolivia, Costa Rica, Dominican Republic, Egypt, Greece, Honduras, Lebanon, Libya, Mexico, Panama, Paraguay, and Thailand.).

may not sell it.[3] More momentously, I can create a baby, may give away custody rights (by delivering the baby for adoption, for example) and may ask to be given custody rights (by adopting), but I may not buy custody rights.[4] As can be imagined, moral principles typically explain why full or partial inalienability rules are chosen to protect certain entitlements.[5]

It turns out that our litigation rights are protected by a modified inalienability rule. I can give away my right to sue you—indeed a (weakening) social norm discourages my taking you to court.[6] Alternatively, I can use my right by suing you. And I can "sell" my right to you, by settling on mutually agreeable terms. But this is only partial inalienability, since I cannot sell my right to sue you to anyone else, except that I may exchange part of my claim to a lawyer in return for his obligation to represent me in my suit.[7] Nor can I buy anyone else's claim, unless of course I am an attorney and then only in exchange for my legal services as stated immediately above. So, to be sure, the law protects my litigation rights with a partial inalienability rule.

---

[3] For a list of state laws on organ sales, including exceptions for the sale of blood, see U.S. Dept. of State, *Sale of Organs and Related Statutes*, http://www.state.gov/documents/organization/135994.pdf.

[4] For an article advocating a more market-based approach to this issue, see Elisabeth Landes & Richard Posner, *The Economics of the Baby Shortage*, 7 J. LEGAL STUD. 323 (1978). For a critique of this argument, see Tamar Frankel & Francis H. Miller, *Inapplicability of Market Theory to Adoptions*, 67 B.U. L. REV. 99 (1987).

[5] *See* Krauss, *supra* note 1, at 789–90.

[6] *See* Shawn J. Bayern, *Explaining the American Norm Against Litigation*, 93 CALIF. L. REV. 1697 (2005). Some have claimed that we shirk our moral duty to litigate, given the public good that precedent provides. *See* Richard L. Abel, *The Real Tort Crisis—Too Few Claims*, 48 OHIO ST. L.J. 443, 467 (1987) ("To assert a legal claim is to perform a vital civic obligation."). For criticisms of this proposal, see Steven P. Croley & Jon D. Hanson, *The Nonpecuniary Costs of Accidents: Pain-and-Suffering Damages in Tort Law*, 108 HARV. L. REV. 1785, 1810 (1995); Charles J. Goetz, *Commentary on 'Towards a Market in Unmatured Tort Claims': Collateral Implications*, 75 VA. L. REV. 413 (1989); Alan Schwartz, *Commentary on 'Towards a Market in Unmatured Tort Claims': A Long Way Yet To Go*, 75 VA. L. REV. 423 (1989).

[7] *See* MODEL RULES OF PROF'L CONDUCT R. 1.4(c) (2004).

A highly interesting question is whether that partial inalienability rule should be eliminated and replaced by a pure property rule. One can imagine a world where people and firms can buy the right to sue in tort, for instance, even before a cause of action arises[8] or, less radically, after an accident happens.[9] Should third parties be allowed to set up markets in tort suits, the rights to which could then be carved up and marketed in diversified tranches, as is done with mortgage-backed securities?[10] Or to the contrary, is the *status quo* of partial inalienability, with certain very restrictive exceptions for attorneys only, optimal? Or finally, should we proceed with caution and move ever so slightly more towards a property rule, while keeping crucial inalienability limitations?

In this paper, I begin by briefly sketching the two-dimensional view of litigation learned by 1L Law students. The real world is not two-dimensional, of course, and the dimension of time creates risks for plaintiffs (and, to a lesser extent, for defendants) that are not incorporated into the 1L model. Legal institutions classically evolved to enable both defendants and plaintiffs to cope with those risks, but many claim that the classical setup unduly disfavors plaintiffs.[11]

---

[8] The most radical proposals would allow plaintiffs to sell unmatured tort claims for wrongs that have not yet occurred. *See, e.g.*, Robert Cooter, *Towards a Market in Unmatured Tort Claims*, 75 VA. L. REV. 383 (1989).

[9] *See, e.g.*, Michael Abramowicz, *On the Alienability of Legal Claims*, 114 YALE L.J. 697 (2005); Susan Lorde Martin, *Syndicated Lawsuits: Illegal Champerty or New Business Opportunity?*, 30 AM. BUS. L.J. 485 (1992); Marc Shukaitis, *A Market in Personal Injury Tort Claims*, 16 J. LEGAL STUD. 329 (1987).

[10] *See, e.g.*, FRANK J. FABOZZI & FRANCO MODIGLIANI, MORTGAGE AND MORTGAGE-BACKED SECURITIES MARKETS (1992).

[11] I am indebted to the American Bar Association's *Commission on Ethics 20/20*, which reported on Alternate Litigation Financing to the ABA House of Delegates in February 2012. The Commission report may be found at http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/2011 1212_ethics_20_20_alf_white_paper_final_hod_informational_report.authcheckdam.pdf (last visited Aug. 23, 2013). The Report remained agnostic on many of the issues with which I will be dealing in this paper, but provided excellent food for thought.

II. The 1L Paradigm of "Instantaneous Tort" and Its Flaws

In my 1L Torts class we begin the semester by examining the famous Wisconsin case, *Vosburg v. Putney*.[12] The case is indecipherable enough for my rookie students, what with its (to say the least) unintuitive approach to intentional torts and its opaque (to them) distinction between contract and tort damages. Students' heads are often spinning after our Socratic encounter with the two young Waukesha boys whose seemingly casual interaction led to such tragedy.

And yet 1L students typically don't see the full tragedy of *Vosburg*. To my students, one young boy sues another after the first is injured. Each hires, and presumably pays for (though the students don't consider that), a lawyer. Litigation is instantaneous and cost-free. A decision is rendered and immediately appealed. A final decision is rendered, and the liable party repairs the tort. Corrective justice is satisfied,[13] the Rule of Law is elucidated and advanced, and that is the end of the story. The defendant pays the plaintiff if liable; the defendant pays nothing if not liable.

Alas, losses incurred in the typical tort suit are not instantaneous "one-off" losses as a two-dimensional 1L examination might imply. Steal my empty briefcase and you've caused an instantaneous, one-off loss that has no real effect on my ability to meet any ongoing obligations. Break my leg and you've possibly caused me a lifetime of lost income and decreased potential that I desperately need to get back before the bills become due.

---

[12] Vosburg v. Putney, 50 N.W. 403 (Wis. 1891).

[13] Michael I. Krauss, *Tort Law and Private Ordering*, 35 ST. LOUIS U. L.J. 623, 634-36 (1991); ERNEST J. WEINRIB, THE IDEA of PRIVATE LAW 196–203 (1995).

1L can be so overwhelming that it may take time for students to realize how much they missed when they first looked at *Vosburg*:[14]

- The case took *years* to resolve. Twice the trial court's judgment on the verdict was appealed; four times the Wisconsin Supreme Court dealt with the case in one form or another.[15]
- Andrew Vosburg's medical bills were staggering, and approached 100% of his parents' annual income, this in a day when there was no health insurance.[16] The exactions on his family, preceding the final settlement, must have been tremendous.
- The direct court costs of litigating were enormous, with plaintiffs' costs approaching 200% of the Vosburgs' annual income and defendants' costs approaching 50% of the average Waukesha worker's annual income.[17]
- The Vosburgs' attorneys' normal charges—not payable by the Putneys regardless of the ultimate outcome of the case because of the "American Rule"[18] —were apparently more than one year's family income.[19]
- After many years and two plaintiff's verdicts, the ultimate payment of $1200 may have left both parties *and* plaintiff's attorneys in the red.[20]

III. Common Law Adaptations to the "Instantaneous Tort" Paradigm

The Common Law reflects the long-term risks of torts that the 1L student so easily misses, through the development of institutions that allow the parties to purchase "options"[21] on these risks.

[14] Here I only deal with the financial and related risks that students tend to miss. *See* Zigurds Zile, *Vosburg v. Putney A Centennial Story*, 1992 Wis. L. Rev. 877 (1992) for a rich factual history of the case, of the kind that is always left out of sterile casebook summaries.

[15] *Id.* at 971.

[16] *Id.* at 892.

[17] *Id.* at 973. The Putneys were a relatively wealthy family; the Vosburgs were not.

[18] *See* John Leubsdorf, *Toward A History of the American Rule on Attorney Fee Recovery*, 47 L. & Cont. Prob. 9 (Winter 1984).

[19] Zile, *supra* note 14, at 974.

[20] *Id.* at 977. Wisconsin had just recently authorized contingent fees, and it is not clear whether plaintiffs' lawyers had selected such an arrangement.

[21] Option contracts give one the right to elect to buy (or sometimes sell) the underlying asset or security at a set price if exercised by a set expiration date. James Bradfield, Introduction to the Economics of Financial Markets 377–79 (2007). Options markets, such as futures markets, allow risks to be spread and communicate information to the market resulting in greater efficiency. *See id.* at 415–430.

A. On the Defendant's Side

Institutions have sprung up to shoulder much of the ongoing risk of complex litigation. The most frequent tool employed by defendants is liability insurance. While first-party insurance (wherein the purchaser pays someone to assume risks of damage to the purchaser's own property) arguably dates from almost two thousand years before the Common Era,[22] third-party or liability insurance (wherein the purchaser pays someone to assume risks of damage to the property of others, for which the purchaser would otherwise be liable) is of more recent vintage. Until the early 20th Century, almost all liability policies covered Workers' Compensation liability and nothing else. But starting in the 1920's (prompted no doubt by the advent and massive spread of the automobile, a machine allowing an impecunious person to cause considerable damage in a short time), general liability insurance (with caps of $5000, typically) began to be marketed.[23]

Today, liability insurance is highly developed and generally provides dual protection to insureds: it covers both any eventual liability resulting from judgment or settlement as well as legal fees to defend against any liability claim, founded or not.[24] Of

[22] The Babylonians developed a first party insurance system which was recorded in the Code of Hammurabi, c. 1750 B.C., and practiced by early Mediterranean sailing merchants. If a merchant received a loan to fund his shipment, he would pay the lender an additional sum in exchange for the lender's guarantee to cancel the loan should the shipment be stolen.

[23] James A. Robinson, *How Umbrella Policies Started Part 1: Early Liability Coverage, Risk & Insurance*, IMRI (Mar. 2000), http://www.irmi.com/expert/articles/2000/robertson03.aspx.

[24] This second aspect of liability insurance is necessitated by the "American Rule," which provides that lawyers' fees are not considered to be proximately caused by wrongdoing. Thus, each party bears his fees, regardless of the outcome of any litigation, unless the tort of malicious prosecution can be proved. Leubsdorf, *supra* note 18, at 9; Biggans v. Hajoca Corp., 94 F. Supp. 593, 599 (E.D. Pa. 1950) *aff'd*, 185 F.2d 982 (3d Cir. 1950) (footnotes omitted) ("There are a number of circumstances and conditions for the existence of which the jury may award compensatory damages to a plaintiff in an action for malicious prosecution. Some of these, a number of which overlap, may be listed as follows: Loss of liberty, loss of time, physical suffering or discomfort, mental suffering from humiliation and injury to feelings, injury to reputation and station in the community in which he resides, or does business, the risk of conviction, and the reasonable and necessary expenses in securing his release from arrest and defending the criminal prosecution."). Even a non-negligent defendant can therefore be called on to pay many tens of

course this creates a moral hazard, as negligence is more likely if its cost is borne by a third party. Liability insurance limits this moral hazard through co-pays (self-insurance by the liable party), liability limits, and underwriting evaluation (setting a premium based on correlates to moral hazard such as credit history).[25]

Attorneys have devised other protections against the ongoing risks of tort litigation. Uninsured tort defendants typically pay their attorneys by the hour, and as the *Vosburg* case illustrated, total hourly rates are as unpredictable as tort cases are long and complex. Though rare, *reverse contingent fees* are one way to protect against this risk. Under a reverse contingent fee, the parties agree on an objective worst-case liability scenario (the amount may well be much less than the exaggerated amount claimed by the plaintiff).[26] The parties agree that the attorney is entitled to a percentage of any amounts ultimately saved from this sum. If the worst-case scenario unfolds, the defense attorney

---

thousands of dollars in legal fees to defend himself against unfounded lawsuits – so liability insurance has stepped in to protect against this risk. In other countries, these risks are borne only by wrongdoers and false claimants.

[25] Many state politicians have introduced efforts to prevent liability insurance companies from using credit history to set premiums. *See* Heather Morton, *Use of Credit Information in Insurance 2011 Legislation*, NATIONAL CONFERENCE OF STATE LEGISLATURES (Dec. 20, 2011), http://www.ncsl.org/issues-research/banking/use-of-credit-information-in-insurance-2011-legisl.aspx. For example, Maryland legislators in 2011 declined to adopt a bill which would have banned the use of credit history to set motor vehicle insurance premiums. H.B. 1083, Reg. Sess. (Md. 2011), *available at* http://mgaleg.maryland.gov/webmga/frmMain.aspx?tab=subject3&ys=2011rs/billfile/hb1083.htm. For an in-depth look at the correlation between liability and credit scores, see Patrick Butler, *Why Low Credit Scores Predict More Auto Liability Claims: Two Theories*, Working Paper (July 3, 2007), http://www.centspermilenow.org/774-7703.pdf.

[26] In *Wunschel Law Firm, P.C. v. Clabaugh*, the plaintiff sued for $17,500 and the jury awarded $1,750. 291 N.W. 2d 331, 332 (Iowa 1980). Under the terms of the reverse contingent fee agreement, the lawyer representing the defendant would have been entitled to $5,250, or one-third of the $15,750 "saved" the client. *Id.* Relying in part on and quoting at length from an amicus brief filed by the Committee on Professional Ethics and Conduct of the Iowa State Bar Association, the Iowa Supreme Court found the fee agreement to be unreasonable (today under Model Rule 1.5) and void as against public policy, stating that the amount demanded in a tort claim was too speculative an amount upon which to base a reverse contingent fee. *Id.* at 336.

earns no fee.[27] Alternatively, firms such as Clearspire[28] have based their business model on defendant *fixed-fee billing*, wherein the law firm shares with the client the risk of unduly complex and costly representation.[29]

B. On the Plaintiff's Side

There also exist legal institutions designed to ease the risk of complex tort damage for victims. Most obvious is first party insurance. However, this insurance is very incomplete. Roughly half of all tort damages are "general" or non-pecuniary damages, called "pain and suffering" in many jurisdictions.[30] Plaintiffs typically cannot purchase pain-and-suffering insurance for several reasons.[31] Other institutions include:

1. The Collateral Source Rule[32]

If Dave Defendant negligently sets fire to Peter Plaintiff's barn, destroying the barn and livestock and making it impossible for Peter to earn a living, Peter's neighbors might spontaneously organize a barn-raising bee to replace the barn and livestock immediately, thereby eliminating the risk of interminable litigation and tempting low-ball offers from Dave. Peter's neighbors, who pooled the risk, might decide to obtain subrogation from Peter if and when Dave is called upon to compensate. In any case

---

[27] Reverse contingent fees were approved by the American Bar Association Standing Committee on Ethics and Professional Responsibility in Formal Opinion 93-373 (1993) (Contingent Fees in Civil Cases Based on the Amount of Money Saved for the Client).

[28] *See* www.clearspire.com.

[29] *See, e.g., Alternative Law Firms*, THE ECONOMIST, Aug. 13, 2011, for a description of the Clearspire model. This author was of counsel to Clearspire during its formative period, 2010-2012.

[30] *See* Neil Vidmar et al., *Jury Awards for Medical Malpractice and Post-Verdict Adjustments of Those Awards*, 48 DEPAUL L. REV. 265, 296 (1998); W. Kip Viscusi, *Pain and Suffering in Product Liability Cases: Systematic Compensation or Capricious Awards?*, 8 INT'L REV. L. & ECON. 203 (1988).

[31] Moral hazard precludes the development of a pain-and-suffering insurance market in most cases—it is too easy to "fake" a claim not verifiable by a first-party insurer. In those rare instances where moral hazard has not precluded it, pain-and-suffering insurance is indeed demanded by prospective tort victims. *See* Steven P. Croley & Jon D. Hanson, *Nonpecuniary Costs of Accidents: Pain-and-Suffering Damages in Tort Law*, 108 HARV. L. REV 1785 (June 1995).

[32] *See generally* Michael I. Krauss & Jeremy Kidd, *Collateral Source and Tort's Soul*, 48 U. LOUISVILLE L. REV. 1 (Fall 2009).

Peter's suit against David can go forward, without the intense time pressures typically felt by plaintiffs in a tort suit. The payment by Peter's neighbors does not extinguish David's debt, whether or not the neighbors have subrogated, pursuant to the collateral source rule. Of course most subrogated parties are first-party insurers as per the preceding paragraph, but the general availability of the collateral source rule goes beyond first party insurance.[33] If there is subrogation, the ensuing moral hazard[34] is minimized by a contractual clause whereby the insured party agrees to provide all necessary assistance to the insurance company in pursuing any subrogated claims

2. Contingent Fees

A contingent fee is essentially a non-recourse "advance" of the cost of litigation by the plaintiff's attorney, in return for a share of the proceeds if there is settlement or judgment. The "advance" is not (except for official court costs, which must be reimbursed to the lawyer by all but indigent clients) a loan, because of the non-recourse nature of the arrangement.[35] Contingent fees were once banned in the United States as illegal champerty,[36] but lawyers became exempt from champerty as the contingent fee became accepted.[37] Contingent fees allow an impoverished plaintiff (perhaps

[33] *Id.* at 33–50.

[34] A plaintiff who has already been compensated may less ardently pursue the party that is liable to him.

[35] *See* MODEL RULES OF PROF'L CONDUCT R. 1.8(e) (2004) ("A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that: (1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter.").

[36] Champerty is the furtherance of litigation: "We must regard an agreement by any attorney to undertake the conduct of a litigation on his own account, to pay the costs and expenses thereof, and to receive as his compensation a portion of the proceeds of the recovery, or of the thing in dispute, as obnoxious to the law against champerty." Peck v. Heurich, 167 U.S. 624, 632 (1897) (citing the District Court at 6 Ap. D.C. 283, 284).

[37] Even British courts impliedly recognize this: "Champerty is an aggravated form of maintenance. The distinguishing feature of champerty is the support of litigation **by a stranger** in return for a share of the proceeds." Giles v. Thompson, [1993] 3 All ER 321 at 329 (emphasis added), *available at*

impoverished by the tort itself) to secure legal services that, because of the American rule that prohibits fee shifting to losing defendants, she could likely not purchase by the hour. The lawyer thus shares part (the part represented by the value of her legal services) of the risk of tort litigation. Lawyers have a monopsonic right to purchase shares in cases in this way, leading to monopoly "rents" and to calls by some to outlaw contingent fees.[38] And of course only some litigation costs are borne by the contingent-fee attorney—housing costs and medical costs must still be paid by the injured plaintiff during litigation.[39]

Though markets and private law have provided both parties to a tort suit with means to mitigate the risks of long-term litigation, a crucial question is whether one party gets more protection than the other. The claim that the impecunious (perhaps because of the tort inflicted on him) plaintiff does not currently receive the equivalent of what liability insurance provides to defendant relies on the argument that plaintiffs cannot spread certain important risks in advance. Kindly neighbors may rescue a tort victim who ultimately avails himself of the collateral source rule, to be sure. But the only guaranteed protectiton a prospective victim can purchase in advance is insurance, and that insurance does not cover non-pecuniary costs. Similarly, after the accrual of a right of action (that is, after the accident), the lawyer can advance court costs, expert witness fees and the costs of the lawyer's own time and disbursements, but may not advance the myriad costs of living that may so pressure the plaintiff that he may be tempted to accept

---

http://www.bailii.org/uk/cases/UKHL/1993/2.html. Subrogated parties, and attorneys, are not strangers to the lawsuit.

[38] *See, e.g.*, R. Painter, *Litigating on a Contingency: A Monopoly of Champions or a Market for Champerty?*, 71 CHI.-KENT L. REV. 625 (1995).

[39] *See* MODEL RULES OF PROF'L CONDUCT R. 1.8(e) (2004), which prohibits the lawyer from advancing such costs, even with recourse (as a loan).

a low-ball offer from a clearly culpable defendant. Plaintiff's lawyer would arguably be an efficient provider of such costs of living (he has an informational advantage over banks or other lending institutions in determining the likelihood of victory, as he is privy to confidential client information and also has expert access to the legal rules that affect the outcome of the case) if such provision were allowed. But it is not. Despite the fact that lawyers are bound by ethics rules not to launch frivolous suits,[40] their full financing would constitute barratry, a serious felony in some states, everywhere prohibited on the grounds that lawyers able to fully finance lawsuits would "chase ambulances," stir up litigation, damage social cohesion and inflame enmities.[41]

Because of this alleged asymmetry in institutional risk management, it is claimed[42] that prospective tort victims should be allowed to sell a security (an investment in the right of action that has accrued in their favor) just as defendants purchase a security (the assumption by others of future tort liability debts) through liability insurance. Both types of securities allow risk-averse parties to purchase protection from the risks of uncertain, expensive and long-winded litigation—the defendant by paying a premium to share his load and the plaintiff by receiving a premium in return for sharing his booty.

---

[40] *See* MODEL RULES OF PROF'L CONDUCT R. 3.1 (2004).

[41] *See, e.g.,* TEX. PENAL CODE ANN. § 38.12 (West 2009). Barratry And Solicitation Of Professional Employment:

> (a) A person commits an offense if, with intent to obtain an economic benefit the person: . . . . (3) pays, gives, or advances or offers to pay, give, or advance to a prospective client money or anything of value to obtain employment as a professional from the prospective client; . . . .
> (c) It is an exception to prosecution under Subsection (a) or (b) that the person's conduct is authorized by the Texas Disciplinary Rules of Professional Conduct or any rule of court. . . .
> (f) An offense under Subsection (a) or (b) is a felony of the third degree.. . .
> (i) Final conviction of felony barratry is a serious crime for all purposes and acts, specifically including the State Bar Rules and the Texas Rules of Disciplinary Procedure.

[42] *See, e.g.,* J. Burton LeBlanc & S. Ann Saucer, *All About Alternative Litigation Financing*, 49(1) TRIAL (Jan. 2013).

The fact is that the plaintiff in a tort suit has suffered a possibly disabling loss right away, while the defendant is only out of pocket after a settlement or final judgment. Thus, if tort litigation lasts a long time, plaintiffs who can neither obtain bank financing nor sell a security as described will be vulnerable to low-ball offers from defendants, who might therefore systematically pay less than the damage they have wrongfully caused. Whether one sees Tort law as grounded in corrective justice[43] (which requires that the wrongdoer fully compensate the victim for the wrong that has been proximately caused) or deterrence[44] (which requires that the "price" seen by defendants be high enough to deter their future misfeasance), systematic underpayment fails to achieve Tort law's purposes.

If full securitization of lawsuits were allowed, this would pose ethical problems for attorneys of securitized suits. It's worthwhile to enumerate some of these problems right away—other issues will be dealt with in detail below:

1. *Who controls the litigation*? Lawyers must consult with clients on the means of pursuing litigation, and must defer to clients on its ends (responses to settlement offers, etc.).[45] When the client and those who have purchased securities in her litigation disagree on such issues, whose judgment should prevail? Should the prospectus, relied on by investors, be allowed to become the "constitution" of the case, prevailing over the lawyer's own ethical duties?
2. *To whom is owed the lawyer's duties of confidentiality and loyalty*? Should the lawyer be allowed to breach confidentiality to investors if the client reveals

[43] KRAUSS & WEINRIB, *supra* note 13.

[44] *See, e.g.*, WILLIAM MARTIN LANDES & RICHARD ALLEN POSNER, THE ECONOMIC STRUCTURE OF TORT LAW (1987).

[45] MODEL RULES OF PROF'L CONDUCT R. 1.7 (2004).

information detrimental to their investment or perhaps contrary to the prospectus that preceded it? Or should the lawyer's ethical duties[46] cede to the prospectus?

3. *What if some investors sue others, or the client*?[47] Can the lawyer remain in the case or must he withdraw from all representation, possibly to the extreme detriment of his client?

Questions such as these make it clear that full securitization of lawsuits, wherein causes of action would be transformed into "widgets" (fungible things, like barrels of oil or the output of factories) protected by pure property rules, might arguably entail a sea-change[48] in the notion of lawyering. It is far from clear that anyone advocates such a transformation. A tort suit seems very different from a human heart (which is covered by an inalienability rule) but a tort suit is not a widget either. A tort suit has some characteristics intrinsically personal to the client, which arguably rule out pure property rule protection.

In the context of this reflection, it is interesting to note that quasi-securitization has reared its head in the form of Alternate Litigation Financing (ALF), a new plaintiff's option that may rectify the asymmetry in risk sharing between plaintiffs and defendants, all the while respecting the personal nature of a lawsuit.

---

[46] *See id.*

[47] *See, e.g.,* MODEL RULES OF PROF'L CONDUCT R. 1.7 (2004).

[48] Full fathom five thy father lies,
Of his bones are coral made,
Those are pearls that were his eyes,
Nothing of him that doth fade,
But doth suffer a sea-change,
into something rich and strange,
Sea-nymphs hourly ring his knell,
Ding-dong.
Hark! now I hear them, ding-dong, bell.
Shakespeare, The Tempest, Act 1, Scene 2.

IV. The Rise of a New Plaintiff's Option: Alternate Litigation Financing (ALF)

A. Basic Features of ALF Currently

ALF involves only *matured* tort claims. Selling of non-matured tort claims (wherein a future plaintiff assigns any tort claim she might have in the future to the purchaser, likely an insurance company, in return for the purchaser paying the future plaintiff a certain sum, either in one lump sum or more likely in periodic payments)[49] is to liability insurance what a reverse mortgage is to a mortgage. Essentially the annuity payments to the sellers of non-matured claims amounts to *ex ante* compensation for recovery, but of course there is no tort compensation at all, for there has been no tort. Sales of non-mature tort claims eviscerate tort's corrective justice *raison d'être*, and perhaps for that reason no serious proposal to permit them has ever been made.[50]

In current ALF, only part of the claim is sold, in return for money given to plaintiff to pay for litigation and/or living expenses and to replace lost income until receipt of funds. The plaintiff remains in control of the litigation and remains the only client from the attorney's perspective. Presumably, the partial transfer of the tort claim mitigates moral hazard (reduction in the incentive the plaintiff has to vigorously prosecute her own case caused by its sale);

[49] For a promotion of this full property rule transformation by an economist, *see* Cooter, *supra* note 8. *See also* Stephen Marks, *The Market in Unmatured Tort Claims: Twenty Years Later*, Boston Univ. Sch. of Law Working Paper No. 11-14 (2011), http://www.bu.edu/law/faculty/scholarship/workingpapers/2011.html. Insurance companies would have comparative advantages in purchasing non-matured tort claims—they are in a good position to evaluate risks, and by selling liability insurance they are in a position to cancel out (through a clearing house mechanism with other insurers) purchased claims and thereby reduce transaction costs.

[50] Criticisms of Cooter's proposal include Goetz, *supra* note 6 and Schwartz, *supra* note 6.

In addition, current ALF financing is *non*-recourse; that is, if the plaintiff never obtains recovery, nothing need be paid to the ALF provider.[51] Because there is no absolute debt on the part of the plaintiff, the "advance" is considered not a "loan," but an "investment," and is therefore (just like contingent fees) not subject to state usury rules. ALF firms typically attempt to maximize the likelihood that they will not be considered lenders by terming the plaintiff a ''transferor'' of part of his interest in his litigation, not a ''borrower." The funding company, for its part, is termed a ''transferee,'' not a ''lender.'' Obviously, if tort recovery were virtually certain *ex ante*, this contract language might not prevail and the transaction might well be termed a loan.[52]

Finally, ALF is currently offered by finance companies, not by lawyers, who are forbidden to enter this market under Model Rule 1.8(e). Thus, the Model Rule requirement that all charges be objectively reasonable[53] does not apply to ALF.

Just as defendants who purchase liability insurance are protected (up to the coverage limits purchased) from the risks of an anti-defendant outcome, so are plaintiffs who are ALF transferors protected from the risks of an anti-plaintiff outcome to the extent of the payments "purchased" by transferring litigation rights. Of course, a liability insurance policy does not give the insurer an interest in any litigation, for such policies are written before any tort is mature. There IS NO case at the moment when liability insurance is subscribed, and in fact some of the value that liability insurers add consists

[51] This is only the case for individual financing—see the list of various kinds of financing below.

[52] *See, e.g.*, Lawsuit Fin. v. Curry, 683 N.W.2d 233 (Mich. Ct. App. 2004). However, In 2010, two ALF providers sued the Colorado Attorney General to obtain a declaratory judgment that their activities are not loans and are therefore by definition not subject to state usury rules. The trial judge hearing this suit held that under Colorado's Uniform Consumer Credit Code, debt need not be recourse and therefore consumer ALF transactions made with an "expectation of repayment" may not charge more than the interest rate set by that state's usury law. *See generally* Sheri P. Adler, *Alternative Litigation Finance and the Usury Challenge: A Multi-Factor Approach*, 34 Cardozo L. Rev. 329 (2012).

[53] MODEL RULES OF PROF'L CONDUCT R. 1.5 (2004).

of their help in preventing cases from arising in the first place (malpractice insurers encouraging competent professional practice; boiler insurers are experts in boilers and inspect for non-negligent maintenance; etc.).[54]

B. Possible Complaints About ALF?

1. Is ALF–to-Plaintiffs Champerty or Maintenance?

As will be seen in greater detail below, ALF provides funding to individual clients in some cases, to corporate clients in others, and to law firms in yet other cases, in exchange for a lucrative amount of any eventual recovery. But corporations, clients, and lawyers have always been able to borrow money after legal proceedings have begun.[55] When one borrows money, collateral is often pledged; here the collateral is aleatory (the eventual recovery). Is ALF, so described, champerty?

Champerty is a form of maintenance, and is defined by Black's Law Dictionary as ""[a] bargain between a stranger and a party to a lawsuit by which the stranger pursues the party's claim in consideration of receiving part of any judgment proceeds."
In my opinion, ALF is clearly *not* champerty, because the "stranger" (the ALF finance company) doesn't pursue the party's claim or direct the litigation, contemplation of which took place before the intervention of the ALF firm. [Nor, by the way, is subrogation champerty, for the same reason.]

---

[54] Harris Schlesinger and Emilio Venezian, *Insurance Markets with Loss-Prevention Activity: Profits, Market Structure, and Consumer Welfare*, 17 RAND J. ECON. 227 (1986).

[55] If *third party offers money* to sustain someone who has not had the idea to sue someone else, that would be "maintenance," which was illegal under common law. Black's Law Dictionary defines maintenance as "[a]n officious intermeddling in a lawsuit by a non party by maintaining, supporting or assisting either party, with money or otherwise, to prosecute or defend the litigation."

2. Is ALF Substantively Unfair?

As will be seen below, plaintiffs who obtain ALF often pay 60-80% interest. Law firms who obtain ALF to finance ongoing litigation typically pay over 20% interest. These rates might seem, respectively, so steep as to be unconscionable. Should the law tolerate such high interest rates if the alternative is that viable litigation will not be launched, or will be squelched by a low settlement that makes the high interest rate appear attractive by comparison?

3. Is ALF-to-Law-Firms Fee-Sharing?

Law firms have always been able to borrow money to smooth out their cash flow between cases, to finance salaries and to pay for other expenditures in long-running contingent fee cases where no income will be received for a long period. But under Model Rule 5.4(a), law firms cannot share fees with non-lawyers.[56] ALF seems to come suspiciously close to fee sharing *if* lawyers may not pledge their accounts receivable to receive financing. At least one court has rejected the claim that fee sharing is involved in ALF.[57]

---

[56] MODEL RULES OF PROF'L CONDUCT R. 5.4(A) (2004). *But see* DC RULE 5.4(B) ("A lawyer may practice law in a partnership or other form of organization in which a financial interest is held or managerial authority is exercised by an individual nonlawyer who performs professional services which assist the organization in providing legal services to clients, but only if: (1) The partnership or organization has as its sole purpose providing legal services to clients; (2) All persons having such managerial authority or holding a financial interest undertake to abide by these Rules of Professional Conduct; (3) The lawyers who have a financial interest or managerial authority in the partnership or organization undertake to be responsible for the nonlawyer participants to the same extent as if nonlawyer participants were lawyers under Rule 5.1; (4) The foregoing conditions are set forth in writing.").

[57] In *Core Funding Group v. McDonald*, it was held that it is not inappropriate for a lender to take a security interest in an attorney's accounts receivable, to the extent permitted by commercial law. No. L-05-1291, 2006 WL 832833 (Ohio Ct. App. Mar. 31, 2006). This is an ordinary secured transaction and does not violate the prohibition on sharing fees with a nonlawyer, the court concluded. Following these principles, no prohibited fee splitting would be involved if the lawyer repays interest on a loan taken out by the lawyer to fund the litigation.

4. Is ALF-to-Corporations Illicit Gambling?

Companies issue prospecti and solicit funds on the basis of individual opportunities all the time. A corporation exploring for oil can secure funding on the risky possibility of the find being a "gusher." Analogously, ALF investors being publicly or privately solicited could gauge the likelihood of success in the litigation in their decision to invest in the new issuance. Is there any reason to allow such "venture capital" funding except when the risky possibility is that of a lawsuit prevailing? Is "gambling" on an outcome tolerable for gold mines and new car designs but intolerable for litigation? Should it matter that the law is said to exist independent of the case at hand, which merely "discovers" it?[58] Isn't that also the case for the gold mine?

C. Analysis and Critique

1. ALF-To-Consumers

Those who watch cable television are familiar with advertisements by some of the three dozen firms that provide ALF to individual plaintiffs in forty-five states.[59] These funders perform almost no due diligence before disbursing loan amounts: typically, they require little more than an affidavit from a plaintiff's attorney certifying that he or she has accepted the client's case and finds it viable is enough to trigger a non-recourse "investment" by the funder. The perfunctory due diligence is understandable, given the very low amount of the "investment" (on average $4000, and almost never more than

[58] Michael I Krauss, *Rule of Law*, *in* INTERNATIONAL ENCYCLOPEDIA OF THE SOCIAL SCIENCES (William A. Darity, Jr., ed.., Ed., 2d edEd. 2006).

[59] For a representative ad by one of the larger firms in this area, Oasis Legal Finance, see the following youtube: http://bit.ly/YVvBzhhttp://bit.ly/YVvBzh.

$20,000).[60] The very high interest rates (60-80% per year) must be understood in the context of this lack of substantive analysis: if only one of every two funded suits resulted in recovery, the ALF firm would lose money even at those lofty rates.[61] In reality, funding firms must hope that every funded case will result in at least a "nuisance" settlement, from which the funding company would therefore take an enormous share. Nuisance settlements are not atypical in automobile accident cases, which constitute the bulk of ALF-To-Consumers.

Critics[62] have decried the exorbitant interest that must be paid by plaintiffs, who are often unsophisticated clients.[63] It is certainly true that those with little bargaining power often receive unfavorable terms. But it is not clear that an acceptable alternative is to deny them this option, for otherwise they might accept a low-ball settlement offer that is much worse for them. Nor is it clear that "payday loans" (rarely available for those injured in an accident) or loans from an American Indian reservation[64] are more attractive: these loans are recourse loans that must be repaid in every case, while ALF requires no payment from the plaintiff who, for whatever reason, is unable to recover.

The real problem here is that the loan purveyor knows relatively little about the real chances of success of the plaintiff's suit. The purveyor allays this risk in two ways:

---

[60] George S. Swan, *Economics and the Litigation Funding Industry*, 35 NEW ENG. L.Rev. 805, 824 (2001); Steven Garber, *Alternative Litigation Financing in the United States: Issues, Knowns and Unknowns*, RAND CORPORATION at 12 (2010).

[61] Assume a $1000 advance. If case 1 resulted in no payment to the funder, and case 2 resulted in a payment of $1800, the funder is still losing money.

[62] *See, e.g.*, Comments of the U.S. Chamber Inst. for Legal Reform to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. (Feb. 15, 2011).

[63] The more sophisticated clients are, typically, more credit-worthy, and therefore more likely to be able to self-fund or to obtain conventional and lower-cost financing.

[64] *See, e.g.,* Western Sky Loan Company terms of use, http://www.westernsky.com/TermsOfUse.aspx*available at* http://www.westernsky.com/ TermsOfUse.aspx (last visited Aug. 23, 2013).

by requiring a huge dollop of self-insurance (the average loan amount is very low, and the typical plaintiff must therefore bear much of the financial burden of surviving until judgment or settlement) and by charging an imposing interest rate. If purveyors had more competition, these rates might go down and the amount loaned might go up.

And there *is* potential competition available: the plaintiff's lawyer, who already has "skin in the game" (his contingent fee) and who may know more about the chances of success of the lawsuit than anyone, including perhaps the plaintiff. But the anti-maintenance Rule 1.8(e) prohibits the plaintiff's attorney from competing with ALF purveyors. The perverse result is that those lending money are ill suited to do so. High "premiums" and very incomplete "insurance" are predictable results.

Another frequently voiced critique of ALF-to-consumers, especially by the United States Chamber of Commerce, is that it increases litigation costs. This is allegedly so because, once they have received ALF, plaintiffs are less likely to accept initial offers from defendants in "worthless" or low-amount cases. Since the great majority of that initial offer will go to the ALF purveyor, the plaintiff can, it is said, externalize the risk of litigation by "rolling the dice" and going to trial, which is socially costly.[65] There is quite possibly truth to this assertion. On the other hand, the main brake on the survival of low-value suits is the plaintiff's lawyer's decision that the chances of earning substantial contingent fees are slim to none. In other words, defendants *and plaintiff's lawyers* have

[65] *See, e.g.,* Nate Raymond, *U.S. Chamber Calls For Regulation Of Litigation Funders*, REUTERS, (Oct. 24, 2012), http://www.reuters.com/article/2012/10/25/chamber-funders-idUSL1E8LP0BQ20121025. IBM General Counsel reported that his company had faced numerous ALF lawsuits. He claimed that the funders' involvement of litigation funders prolongs cases that otherwise would be on their "death bed." "It adds to the court burden," he said. "We've seen it time and time again."

a common interest in not prolonging the agony of a worthless suit, even if the plaintiff himself is indifferent to the situation because of ALF.

Perhaps the Chamber of Commerce feels that a suit with a 90% of no recovery and a 10% chance of, say, a $500,000 recovery is a "worthless" suit.[66] A contingent fee lawyer, who diversifies his risk by taking on several such suits, might pursue this one. And a plaintiff who has received $10,000 in ALF, and who therefore owes $18,000 from any settlement to the purveyor, might refuse a $25,000 settlement offer. Whether this refusal is socially wasteful or costly is a complex and difficult question, for the case is "worth" $50,000 given the figures used above. In any case any social cost incurred by the litigation of such cases would presumably have to be balanced against the social gain involved in cases where ALF enables a righteous plaintiff (that is, a plaintiff with a sure win case for, say, $50,000) to turn down a $10,000 offer because he has the wherewithal to survive for a few more months.

Clearly, making litigation less risky for plaintiffs will result, *ceteris* paribus, in more litigation. Whether this is a socially bad or good thing depends crucially on which litigation is pursued. For it is not *a priori* certain that only worthless litigation will be pursued. Thus, for example, the recent $1.1 *Billion* settlement of Toyota's "unintended acceleration" lawsuit took place despite NHTSA determinations that no Toyotas or Lexuses accelerated "all by themselves." In every case NHTSA determined that user misuse (either in depressing the wrong pedal or in failing to attach carpets correctly) was

---

[66] The chance of recovery might be slim because of the credibility of witnesses, or because of statistical issues related to cause-in-fact

involved.[67] Was this mammoth settlement caused by ALF (assuming *arguendo* that some plaintiffs availed themselves of it)? Or did bad publicity and the American Rule, which condemns Toyota to pay enormous lawyers' fees even if it prevails at most trials, prompt the settlement? If the Chamber wishes to attack an institution as giving rise to frivolous suits, a more suitable target might be the American Rule.[68]

Finally, criticism of ALF-to-consumers rightly invokes Model Rule 1.7. A conflict of interest can arise if plaintiff's lawyer recommends the ALF purveyor, advises client on the contract with the purveyor and advises the purveyor during settlement negotiations. This is not an intrinsic criticism of ALF-to-consumers, but a kind of "as applied" criticism.[69] A lawyer who prepares an ALF agreement for the purveyor is like a lawyer who prepares a bank loan document that will enable his client to pay the lawyer's fees; he must advise the client to get independent counsel, must obtain informed consent if such counsel is declined, etc.[70]

2. ALF-to-Plaintiffs'-Law-Firms

The current issue of the plaintiffs' bar's *Trial* magazine contains no fewer than five advertisements for ALF-to-Plaintiffs'-Law-Firms, from among the dozen or so firms that engage in this type of financing.[71] This is typically recourse funding (a true loan that must be repaid regardless of the outcome of the case). It is sought by undercapitalized

[67] NHTSA, *Technical Assessment of Toyota Electronic Throttle Control (ETC) Systems* (2011), *available at* http://www.nhtsa.gov/staticfiles/nvs/pdf/NHTSA-UA_report.pdf.

[68] For a criticism of the American Rule, *see* Comment, *Court Awarded Attorney's Fees and Equal Access to the Courts*, 122 U. PA. L. REV. 636, 638 (1974).

[69] Like an as-applied constitutional challenges to statutes, the success of this challenge to ALF does not call the basic practice of ALF into question.

[70] American Bar Association Commission on Ethics 20/20 Informational Report to the House of Delegates*on Alternate Litigation Financing to the ABA House of Delegates*, *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.

[71] See Appendix 1 for an example of these ads.

law firms that do not have sufficient collateral for a bank loan secured by all the assets of the firm. The range of interest rates in ALF-to-Plaintiffs'-Law-Firms is unknown, as these are private contracts, but one investigator has concluded that rates are in the vicinity of 20 per cent per year for loans made post-suit and pre-settlement, though much less for suits post-settlement but pre-receipt of funds. In any case rates are well above those available to corporate law firms from commercial banks.[72] Typically much more due diligence by the funding firm takes place, since the funding per case greatly exceeds that of ALF-to-consumers. This due diligence frequently requires the communication of confidential client information to the borrower (after informed consent given by clients, of course). The clients' consent is likely to be forthcoming because the granting of financing by a well capitalized funder serves as a signal to the (typically corporate) defendant-opponent that the plaintiff firm has the wherewithal to endure a long suit, and that third party attorneys have vetted the claim in detail and found it valid. The funding itself may contribute to a substantial settlement if the defense believes the plaintiff has the ability to fully prosecute a case.[73]

ALF-to-plaintiffs'-firms arguably gives the borrower an even greater incentive to win a suit than does its contingent fee. Is this incentive too strong? Is the financed lawyer more likely to succumb to pressure to bias the process to repay his financiers and obtain future financing at lower rates? An Ecuadorian ex-judge, who presided over the infamous Chevron case, recently revealed that plaintiffs' lawyers had offered him a $500,000 bribe to secure an $18.2 billion judgment, and actually had actually drafted the

[72] GARBER, *supra* note 60, at 13.

[73] *See* JONATHAN HARR, A CIVIL ACTION (1996), for an example where no large settlement was forthcoming, in part because the plaintiff firm was undercapitalized and could not prosecute the case competently.

government's decision against the company. Were these lawyers financed through ALF? If they were, that might be a reason for bar associations to monitor law firm capitalization closely to ensure that such Faustian bargains are not reached.

So a risk of corruption there is, and Bar vigilance is needed. But it is not clear that this risk of corruption is worse than, say, the risk that afflicts defense lawyers' financed by insurance companies they are desirous of pleasing in order to retain repeat business.[74] Whenever a non-client with multiple repeat business promises money, whether that non-client be an ALF purveyor or a liability insurer, lawyers' ethical mettle will be tested. In every case the client must retain authority over decision-making[75] and the third party payers may not compromise the attorney's professional competence.[76] If ALF is to be banned for this reason, should we ban insurer funding?

3. ALF-to-Corporate-Plaintiffs (High-Value Cases)

A half-dozen funding firms[77] provide capital directly to businesses or to their outside counsel, to finance plaintiff-side high value (business-vs. -business) claims. Here, unlike the other forms of ALF, it appears that financing is provided in exchange for a percentage of eventual recovery.[78] Investments appear to vary from a few million dollars up to $20 Million, with (as would be expected) very considerable due diligence by funding firms. This funding is sought in part because of corporate regulations: often

[74] Rule 1.8(f) prohibits lawyers from accepting compensation from a third party unless the client gives informed consent. But the client clearly consents to ALF as he consents to insurer funding. For an article demonstrating the difficult position of the lawyer in insurance-funded litigation, *see* Charles Silver & Kent Syverud, *The Professional Responsibilities of Insurance Defense Lawyers*, 45 DUKE L.J. 255, 313 (1995).

[75] MODEL RULES OF PROF'L CONDUCT R. 1.2(A) (2004).

[76] MODEL RULES OF PROF'L CONDUCT R. 5.4(C) (2004).

[77] As of 2010, ARCA Capital, Burford Capital, Calunius Capital, IMF Australia, Juridica Investments and Juris Capital invested in commercial claims. GARBER, *supra* note 60, at 15.

[78] *Id.* at 13.

inside counsel does not want to commit corporate capital to a case if such capital had not been identified for this purpose in the corporation's past budgeting process. In addition, and importantly, inside counsel is typically very anxious to obtain the strong outside vetting that this type of ALF provides, and that is additional to the evaluation of outside counsel, since the latter (paid on an hourly basis perhaps) may be suspect. The very substantial investment by this type of ALF purveyor is a clear build-up in an "arms race" with defendant, and is a sign of serious intent to litigate that is likely designed to maximize the defendant's ultimate settlement offer.

One might wonder why, since there are no living expenses or "pain and suffering" here, Corporate plaintiffs are not content to "finance" all such cases *via* contingent fees? The answer, it seems, is that this type of corporation typically does not want to hire contingent fee law firms, which are typically the firms that sue them. They would prefer using their usual firms, which use either fixed fee (Clearspire) or hourly billing. ALF is the alternate financing in such cases, as contingent fees may not be available.[79]

---

[79] GARBER, *supra* note 60, at 38.

There have been very few critiques leveled at this type of ALF. Interest rates are low, there is no unequal bargaining power, and conflicts of interest are exceedingly rare. It is important that corporate counsel understands that the information communicated to obtain financing may result in loss of privilege and work-product protection (in house counsel usually provides informed consent to this effect), since the purveyors are not lawyers. Case law is very skeletal on this count.[80]

V. Conclusion: Is Reform Needed?

It is time to return to the questions raised earlier in this paper:

A. Why Does a Partial Inalienability Rule, Instead of a Property Rule, Protect our Entitlement to Causes of Action?

Some have argued for full purchase and sale of all dispute rights?[81] For them, clearly, commodifying causes of action and securitizing them as desired present no problem.[82] Many, however, will resist commodification on the grounds that tort suits, at least consumer suits resulting from personal injuries causing non-economic harm, are too personal to be treated as widgets. True, purely personal things can in a sense be borrowed against (I can borrow money to be repaid from the revenue obtained through the use of my arm if, say, I'm a baseball pitcher) but they may not be sold (the ballplayer may not sell his arm). Should the ballplayer be able to sell the lawsuit that results from the wrongful amputation of his arm?

---

[80] However, at least one state bar has opined on this issue: *See* N.Y. State Bar Ass'n, Comm. on Prof'l Ethics, Op. 769 (Nov. 4, 2003) ("The lawyer should advise the client that disclosures of confidential information to the financing institution might compromise the attorney-client privilege and might therefore cause the information to be available to an adverse party in discovery) (citing *see generally* PAUL R. RICE, ATTORNEY-CLIENT PRIVILEGE IN THE UNITED STATES § 9 (2d ed. 1999)).

[81] *See, e.g.,* Michael Abramowicz, *On the Alienability of Legal Claims*, 114 Yale L. J. 697 (2005).

[82] For Professor Abramowicz's views on this issue, presented at the panel on Third Party Financing of Litigation at the Fourth Annual Judicial Symposium on Civil Justice Issues, at Northwestern Law School in December 2009, see http://www.youtube.com/watch?v=Rrb6RoixbSU (last visited Aug. 23, 2013).

Whatever the answer to this question, they are less apposite as regards corporate litigation, and it is therefore not surprising to see securitization of suits take place there.

B. Why *Do We Give* a *Monopoly* to *Lawyers* as *Concerns Partial Purchase* of *Tort Suit?*

The malignant explanation for lawyers' monopoly on contingent fee financing is that it is an economic rent acquired through Public Choice abuse of the legal process.[83] The benign explanation is that lawyers are professionals and officers of the court, governed by a strict code of ethics to which they swear a solemn oath, and who can therefore be trusted to preserve their client's interests throughout the litigation. Though of course many lawyers fall short of this ideal, I prefer the benign explanation. My career as a legal ethics professor makes little sense otherwise.

C. Given the Benign Explanation, Then, Why Not Just Expand the Role of Lawyers to Allow Them to Provide ALF?

This, I think, is a reform whose time has quite possibly come. Lawyers may already front court costs, other litigation costs (expert witnesses, etc.) and their own time through the contingent fee. They have done due diligence about a client's case in a way not feasible (in small cases) for funding firms. They could therefore front much more than a $4000 non-recourse advance for a case they truly believed in. Why not, then, relax 1.8(e) and allow lawyer to front living expenses and the like, or part thereof, as part of their extra legal services[84]?

[83] *See, e.g.*, Lester Brickman, *Introduction to Lawyer Barons: What Their Contingency Fees Really Cost America*, Cardozo Legal Studies Research Paper No. 322 (Feb. 15, 2011), http://ssrn.com/abstract=1773796.

[84] MODEL RULES OF PROF'L CONDUCT R. 5.7 (2004).

Lawyers currently charge no interest to their clients for fronting court costs and expert witness fees.[85] Why would they charge more for fronting living expenses? Presumably, though, lawyers might themselves have to borrow to provide ALF to their clients. Ethics rules would allow them to charge back any interest they pay for this (but not to mark up the interest, in my opinion). They could borrow at rates (currently 20%) much below the exorbitant rates charged by ALF firms to consumers. This would result in a much lower effective interest rate for clients than they currently pay for ALF, while procuring them much more in sustenance.

Market supply and demand might result in the loan becoming a recourse conditional loan (with an increase in contingent percentage if there is recovery, and the pass-through interest rate if there is no recovery) for solvent plaintiffs, and a non-recourse advance (very high contingent fee if there is recovery, nothing due otherwise) for indigent plaintiffs, much as contingent fee lawyers are currently permitted to make court and expert costs non-recourse loans. Might lawyers' contingent fees, under such arrangements, appropriate the majority of a client's claim? That seems unlikely, and if it happened, lawyers (unlike ALF purveyors) are sanctionable for unreasonable fees under the Model Rules.

One beneficial side effect of allowing attorneys to provide ALF is that a ploy of unethical plaintiffs' attorneys (alleging "newly discovered information" to reduce the previously stated value of plaintiffs' case, to induce plaintiffs to settle for a low amount,

---

[85] Some states allow the charging of interest on the advancements, but it seems only to the extent that the lawyer incurred those interest charge him or herself. *See, e.g.*, D.C. Bar Ethics Op. 345, *available at* http://www.dcbar.org/for_lawyers/ethics/legal_ethics/opinions/opinion345.cfm; Kentucky Bar Association Ethics Op. KBA E-216 (1979), *available at* http://www.kybar.org/documents/ethics_opinions/kba_e-216.pdf.

giving attorneys a contingent windfall for almost no work and freeing them up to take the next windfall case) would be foiled. Plaintiffs are much less likely to accept an unethical low-ball offer communicated to their possibly conniving attorney if their essential life needs have been provided for through ALF. At the margin, unethical plaintiffs' lawyers will therefore be less likely to make such offers.

Might this change the structure of plaintiffs' law firms? It might. Better-capitalized firms could obtain lower interest loans, which might begin to resemble low-interest ALF-to-corporate-plaintiff loans more than than the high-interest ALF-to-plaintiffs'-firms loans given to undercapitalized plaintiffs' firms today. Better-capitalized plaintiffs' firms would therefore offer more favorable ALF financing to their clients. Plaintiffs' firms might start to resemble defense firms in their size, structure and capitalization. It's not clear that this is a problem: indeed, 1.8(e) may have led to inefficient undercapitalization in plaintiffs' firms.

Might attorney-provided ALF be deemed maintenance or champerty? It would be, if lawyers trolled for clients and offered to maintain them pending judgment. But that is and would remain unethical and prohibited. If lawyers did not troll for clients, they would no more be guilty of maintenance and champerty than are current ALF firms. On the other hand, if there is a real fear of champerty and maintenance, the state Bar might establish a clearing house to which plaintiffs' lawyers must refer cases (preserving confidences and privilege) before obtaining permission to offer ALF financing.

ALF has risks, but its time has come. The complex multidimensional nature of tort litigation demands it. Attorneys can provide it ethically and efficiently, I think. Maybe it's time to free the lawyers.

APPENDIX 1: TRIAL MAGAZINE ADS APRIL 2013

What's wrong with this picture?

1.877.894.9724 • www.AdvocateCapital.com