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STATE OF MINNESOTA COUNTY OF HENNEPIN	DISTRICT COURT FOURTH JUDICIAL DISTRICT
Prospect Funding Partners LLC and Prospect Funding Holdings LLC, Plaintiffs, vs. Deanna Williams, Defendant.	Case Type: Personal Injury Court File No. 27-CV-13-8745 Hon. Kristin A. Siegesmund **ORDER**

On March 19, 2014 the parties appeared before this Court on three motions: 1) Defendant Williams' Motion for Summary Judgment on the grounds that the contract at issue is void because it violates public policy against champertous contracts; 2) Plaintiffs' Motion to Strike certain affirmative defenses; and 3) Plaintiffs' Motion for Summary Judgment based on Defendant's breach of the contract at issue. Plaintiffs Prospect Funding Partners LLC ("Partners") and Prospect Funding Holdings LLC ("Holdings") were represented by Robert Hopper and Eric Magnuson. Defendant was represented by Jonathon Heller, Richard McGee and Diane Bratvold.

Based upon the arguments of the parties and all the files, records and proceedings herein,

OVERVIEW

This case arises out of a pre-settlement funding contract entered into between Defendant Williams and Plaintiffs. Williams had begun a personal injury suit for sexual assault which had the possibility of a substantial recovery. Although Williams' attorney was funding her litigation through a contingency fee arrangement, she needed living expenses. She had previously entered into another pre-settlement funding contract with a different company, but that company would no longer fund her. She was referred to Plaintiffs for possible additional funding.

Plaintiffs are in the business of buying interests in lawsuits from claimants they believe will likely receive large sums of money from settlements. They provide cash payments to pay claimants' living expenses during the pendency of the lawsuit. In exchange, they get an interest in the proceeds of the lawsuit. The contract is structured as a sale rather than a loan. If there are no proceeds there is no obligation to repay the debt. The contract also has a liquidated damages provision that can lead to an absolute obligation to pay a large amount of money well in excess of the scheduled amount due if the contract is violated.

In October 2011, with the parties believing that trial was scheduled for February 2012, Williams entered into a contract with Plaintiffs in which the former pre-settlement contract was paid off for $107,283, and she initially received four months of living expenses starting in November 2011. These monthly payments were extended to a total of nine months when the trial

was delayed. In exchange Williams promised to pay Plaintiffs back from any proceeds she received. If she was unsuccessful she had no obligation to repay Plaintiffs. The money that she received had additional processing fees over 16.5%, and the principal and fees accrued interest at a rate of 4.5% per month compounded monthly, which is equivalent to an annual interest rate in excess of 54%. The amount that Plaintiffs would be entitled to receive was not limited to a percentage of the funds received by Williams in her lawsuit.

The case did not settle as quickly as had been contemplated and the trial date was set back. Plaintiffs refused to extend more payments to Williams beyond June of 2012. Williams' counsel withdrew in July 2012 and she retained her current counsel who would not agree to sign papers from Plaintiffs acknowledging their contract with Williams.

After Plaintiffs stopped funding Williams, her personal injury case was resolved with a confidential settlement in the fall of 2012. Plaintiffs claim that they have expended $140,808 on Defendant's behalf and are entitled to receive payment from the settlement proceeds of either a scheduled amount, which as of March 31, 2014 is $590,878, or liquidated damages of $987,221 for breaching the contract, plus all their costs of collection. Defendant has refused to pay either amount claiming that such pre-settlement funding contracts are not recognized in Minnesota because they are champertous and violate public policy.

PROCEDURAL POSTURE

Plaintiffs filed this action on May 2, 2013 to enforce their contract and filed a second amended complaint in August 2013 that stated four causes of action: Count I: Breach of Contract; Count II: Anticipatory Breach; Count III: Breach of Covenant of Good Faith and Fair Dealing; and Count IV: Unjust Enrichment. Defendant's Second Answer raised fourteen affirmative defenses. The parties have filed cross motions for Summary Judgment and Plaintiff has also filed a motion to strike. In regard to the motion to strike, Plaintiffs originally challenged all 14 of the affirmative defenses raised by Defendant in her Amended Answer. Prior to this hearing the parties agreed that only two affirmative defenses remained at issue and should be considered by the Court in the current motion to strike; specifically Defense 9 (Unclean Hands) and Defense 11 (Contract of Adhesion).[1]

[1] The challenges to the other 14 defenses have been resolved. The parties agreed that Defense 3 (Standing), Defense 4 (Failure to state a claim of Good Faith and Fair Dealing) and Defense 10 (Privity) have been resolved by Judge Alton's Order of February 14, 2014 which allowed both Plaintiffs to remain in the case and continue with their cause of action regarding Williams' alleged breach of a covenant of good faith and fair dealing. Defendant has voluntarily withdrawn Defenses 7 and 8 regarding Fraudulent Inducement, Defense 12 regarding the application of a certain federal court ruling on confidentiality and Defense 13 regarding Defendant's offer to restore Plaintiff to the status quo. With regard to the champerty style defenses in Defenses 1, 2 and 6 the parties agreed that if champerty is recognized in Minnesota then these are defenses. The issue of applicability is the subject of Defendant's summary judgment motion. In regard to Defense 5 (failure to state a claim for Unjust Enrichment), the parties agreed that the unjust enrichment claim was an alternative claim to a contract claim. If the contract was valid, there could not be an additional unjust enrichment claim. And the parties agreed that Williams could challenge the validity of the liquidated damages clause, but disagreed whether it needed to be stated as a separate affirmative defense.

UNDISPUTED FACTS

1. Defendant Melaine Williams claimed that she had been sexually assaulted by a wealthy sports star and started a lawsuit in Florida for personal injury in November 2010.

2. Plaintiff Prospect Funding Partners LLC ("Partners") is a pre-settlement funding company that advances money to clients against future claims resolution.[2]

3. Plaintiff Prospect Funding Holdings LLC ("Holdings") is the financial arm for Partners.[3] Partners is authorized by Holdings to make purchases, sign contracts and obligate Holdings to binding agreements.[4] Partners originates, services, administers and monitors claims on behalf of Holdings.[5]

4. A purpose stated in Plaintiffs' advertising is to provide funds to "help clients cover living expenses giving them and their attorney more time to negotiate a better settlement."[6] Holdings provides funding to plaintiffs in contingency cases. While attorneys fund the litigation, Holdings provides funding to cover living expenses of a litigant.[7] Holdings provides advances to parties who have insufficient resources.[8] The funding provided by Holdings is time-limited. Holdings does not intend to provide funding through trial.[9]

5. Holdings provides non-recourse funding. It is anticipated that if the client is unsuccessful no monies will be paid to Holdings.[10]

6. The arrangement is structured as a sale of an interest in the proceeds from the client's lawsuit, rather than as a loan.[11]

7. Williams had entered into two prior pre-settlement funding agreements that purported to sell an interest in the proceeds of any settlement or award from her litigation.

8. The first prior agreement was with Oasis Legal Finance ("Oasis") which she found through her attorney.[12] Oasis funded Williams for a number of months. When Oasis reached its limit, Boston Finance Group ("Boston") bought Oasis' interest in Williams' lawsuit for $53,880.[13] Boston also agreed to pay Williams ten monthly installments of $3,725 for living necessities. Boston charged her 2% monthly interest. The Boston payments ended in October 2011.[14]

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[2] Dep of Melanie Greening p 10.
[3] Dep of M. Greening p 36.
[4] Plaintiffs' Response to Defendant's Motion to Dismiss dated Oct. 20,103 at 10.
[5] Amended Complaint para 9.
[6] Dep of M.Greening p 51.
[7] Memorandum of Law in Support of Plaintiffs' Motion for Summary Judgment at 5, Aff. of M. Greening.
[8] Memorandum of Law in Support of Plaintiffs' Motion for Summary Judgment at 5.
[9] Dep of M. Greening at 121, 170.
[10] Dep of M. Greening p 40-41.
[11] *See* Williams Purchase Agreement; Dep of M. Greening p. 40.
[12] Dep of Williams p 94.
[13] Memorandum of Law in Support of Plaintiffs' Motion for Summary Judgment at 10.
[14] Dep of Williams p 43, 84, 98.

9. Williams entered into a pre-settlement funding contract with Plaintiff Holdings on or about October 31, 2011.

10. At the time Holdings entered into the contract with Williams, Holdings had been told that Williams had psychological injuries that prevented her from working. Holdings understood that Williams needed the monthly $3,725 for her monthly maintenance in order to live.[15]

11. As part of the funding for Williams, Holdings paid Boston $107,283 to buy out their pre-settlement funding contract with Williams.[16] Holdings charged Williams an additional purchase fee of $17,761 for paying off the Boston contract and for her initial $3,725 monthly payment.[17]

12. Plaintiffs learned of Williams' situation through Boston Finance Group.[18] Boston Finance Group are investors in Prospect Funding.[19] (Although the record is not clear whether Boston is an investor in Partners or Holdings or both, it is undisputed that Boston invests in Plaintiffs' business).

13. At the time Holdings entered into the agreement it believed there was a February 2012 trial date.[20] Holdings valued the possible settlement in Williams' litigation at $5 million and never changed that assessment.[21] At the time Holdings entered into the contract with Williams, Holdings had discussed the details of settlement negotiation with Ms. Williams' attorney and believed that $1.3 million was the floor of any settlement.[22]

14. In October 2011, Holdings was considering funding Williams for three or five months, essentially until the February trial date.[23] The original agreement was for four months of payments of $3,725 with an expectation of additional payments unless either party opted out by giving three days' written notice.[24] When the case did not resolve by February 2012, Holdings agreed to extend the payments for a few more months. Holdings gave notice and made its last payment in June 2012.[25] Although the trial was still some months off and Williams requested more payments, Holdings made no more payments after June 2012.

15. For each of the nine monthly payments received between November 1, 2011 and June 26, 2012 Williams was charged an 18% processing fee of $671.

16. Including the $107,283 that Holdings paid to Boston and the $33,505 for the nine monthly payments that Williams received, Holdings advanced a total of $140,808 on behalf of

[15] Dep of M. Greening at 110-12.
[16] Aff of M. Greening in Support of Plaintiffs Motion for Summary Judgment para 6, Dep of M. Greening p 42.
[17] Aff of M. Greening in Support of Plaintiffs Motion for Summary Judgment at para 21. Dep of M. Greening at 88.
[18] Dep of M. Greening p 120.
[19] Dep of M. Greening p 31.
[20] Dep of M. Greening at 108.
[21] Dep of M. Greening at 176.
[22] Dep of M. Greening at 200. 216.
[23] Dep of M. Greening at 76-77, 107.
[24] Williams Purchase Agreement p 1 and Sched A.
[25] Dep of M. Greening at 116.

Williams. In addition, Williams was charged a total of $23,800 in fees for the $140,808 that Holdings advanced.[26] This represents fees equivalent to 16.9% of the monies advanced.

17. Although Boston had charged 2% a month interest on the amounts it advanced, Williams' new contract with Holdings was accruing interest at 4.5% each month, [27] over double the rate charged by Boston. Because this was compounded rather than simple interest the actual annualized interest rate was over 54%.[28]

18. Because of the high compounding interest rate, the amount owing on the contract escalates rapidly. Under the contract, the payoff balance as of December 31, 2012 would have been $305,319.[29] Currently, as of March 31, 2014, Williams would owe $590,878 for the $140,808 advanced by Holdings.[30] The amounts due under the contract increase indefinitely.

19. The contract also ensured that Plaintiffs would make a significant profit even if the case settled as quickly as Holdings anticipated. The contract required that Williams pay interest for a minimum of 6 months.[31] So the minimum payoff for Williams even if the case had settled in one month would have been 30% on the fees and money advanced, which would be equivalent to a 360% annual rate of return.[32]

20. The contract did not ensure that Williams would necessarily receive a portion of her settlement. The contract had no limit to how much Holdings could be paid. The amount Holdings is entitled to is not limited to a percentage of the settlement. If settlement funds were insufficient to pay the full amount owed to Holdings, then Williams would get nothing.[33]

21. The contract also had a liquidated damages clause. If valid, the liquidated damages clause for any breach of the contract would require that Williams pay $987,221 even if she received no proceeds from her lawsuit.[34]

22. This liquidated damages clause is stated in two places in the contract. Paragraph 7.2 states:

> "Specific Default. IF SELLER MAKES ANY FALSE STATEMENTS IN THIS PURCHASE AGREEEMENT (SEE SECTION 2.3), FAILS TO DISCLOSE A PRIOR SALE (SEE SECTION 3.4), RECEIVES ADDITIONAL ADVANCES WITHOUT PURCHASER CONSENT (SEE SECTION 5.3), REPLACES SELLER'S ATTORNEY WITHOUT OBTAINING A NEW ACKNOWLEDGMENT FROM THE REPLACEMENT ATTORNEY (SEE SECTION 5.8), DOES NOT COMPLY WITH THIS PURCHASE AGREEMENT OR AVOIDS OR ATTEMEPTS TO AVOID PAYMENT TO PURCHASER, SELLER SHALL IMMEDIATELY PAY TO THE

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[26] Aff of M. Greening in Support of Plaintiffs for Motion for Summary Judgment para 19, 22.
[27] Aff of M. Greening in Support of Plaintiffs for Motion for Summary Judgment para 24.
[28] Dep of M. Greening at 88-89.
[29] Melanie Greening dep Ex 8.
[30] Aff of M. Greening in Support of Plaintiffs for Summary Judgment para 25.
[31] Dep of M. Greening at 88.
[32] *See* payment schedule attached to Williams' contract.
[33] *See* Williams' Purchase Agreement p4, para 6.1.
[34] Aff of M. Greening in Support of Plaintiffs for Summary Judgment para 27 (the amount is calculated at the 40 month rate of the payment schedule). *See* Williams' Purchase Agreement p 1 and para 7.2.

PURCHASER LIQUIDATED DAMAGES IN THE AMOUNT THAT WOULD BE DUE AT 40 MONTHS IMMEDIATELY REGARDLESS OF THE OUTCOME OF THE LEGAL CLAOK OR THE AMOUNT OF THE PROCEEDS, IN ADDITION, SELLER SHALL PAY FOR ALL COLLECTION COSTS, INCLUDING ATTORNEY'S FEES AND EXPENSES OF PURCHASER."

The same terms are substantially reiterated on page 1.

23. Under the contract, an event of default that could trigger the liquidated damages clause includes terminating Seller's attorney and failing to retain a replacement within 30 days.[35]

24. Williams' contract with Holdings prohibited her from entering into any other pre-settlement funding agreements to receive advances without prior written permission of Plaintiffs.[36] Getting additional funding without Plaintiffs consent would have triggered the liquidated damages clause.

25. The contract required that "If Seller determines to hire new or additional attorneys to represent Seller in the Legal Claim, Seller agrees that, prior to hiring, Seller shall (a) provide Purchaser with written notice of such determination." The contract also required that the Seller require her new attorney to execute an acknowledgement of the contract between Seller and Purchaser.[37] Failure to do these things under the contract would trigger the liquidated damages clause.

26. Williams' attorney Dolce withdrew in July 2012. Williams hired her current counsel Jonathon Heller after Dolce withdrew. She did not provide Holdings with written notice of her intention to hire Mr. Heller prior to hiring him.

27. The civil lawsuit reached a confidential settlement in the fall of 2012.

28. Under the contract, attorney's fees are paid prior to Holdings getting paid. The lawyers representing Williams prior to her current lawyer Mr. Heller have filed liens claiming a right to part of the settlement proceeds.

29. Williams has not paid back any of the money she received from Holdings. Williams tendered to Plaintiffs the amount that was advanced on her behalf, but Plaintiffs have refused to accept that tender because it is less than the contract amount.

30. The contract provides that contract shall be construed and enforced according to the laws of Minnesota.[38]

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[35] Williams' Purchase Agreement p 5 para 7.1.

[36] Williams' Purchase Agreement p 1 and Para 5.3 ("Seller shall not sell, assign, pledge, or transfer (whether voluntarily or by operation of law or otherwise) any interest in the Legal Claim or Proceeds without the prior written consent of Purchaser, except for transfers by intestate due to Seller's death. . . .").

[37] Williams' Purchase Agreement p 4, para 5.8.

[38] Williams' Purchase Agreement p 6, para 8.10.

CONCLUSIONS OF LAW

Summary Judgment Standard

Rule 56 of the Minnesota Rules of Civil Procedure is designed to implement the stated purpose of the rules – securing a just, speedy, and inexpensive determination of an action – by allowing a court to dispose of an action on the merits if there is no genuine dispute regarding the material facts, and a party is entitled to judgment under the law applicable to such facts.[39] Accordingly, summary judgment is appropriate if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that either party is entitled to a judgment as a matter of law.[40] Summary judgment is not intended as a substitute for trial when there are factual issues to be determined.[41] Summary judgment is a "blunt instrument" and "should be employed only where it is perfectly clear that no issue of fact is involved, and it is neither desirable, nor necessary to inquire into facts which clarify the application of the law."[42]

In considering a summary judgment motion, the Court must determine whether there are genuine issues of fact.[43] The substantive law identifies which facts are material.[44] A material fact is one that will affect the outcome or result of a case.[45] There is no genuine issue of material fact "when the nonmoving party presents evidence which merely creates a metaphysical doubt as to a factual issue and which is not sufficiently probative with respect to an essential element of the nonmoving party's case to permit reasonable persons to draw different conclusions."[46]

The burden is on the moving party to show the absence of any genuine issue of material fact.[47] Once the moving party has made a prima facie case that entitles it to summary judgment, the burden shifts to the nonmoving party to produce specific facts that raise a genuine issue for trial.[48] The party resisting summary judgment must do more than rest on mere averments or unsupported allegations, but must come forward with specific facts to satisfy its burden of production.[49] In analyzing a motion for summary judgment, the Court views the evidence in the light most favorable to the party opposing the motion.[50] "[I]f any doubt exists as to the existence

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[39] *DLH, Inc. v. Russ*, 566 N.W.2d 60, 69 (Minn. 1997).
[40] Minn. R. Civ. P. 56.03.
[41] *Naegele Outdoor Advertising Co. of Minneapolis v. City of Lakeville*, 532 N.W.2d 249, 252 (Minn. Ct. App. 1995).
[42] *Donnay v. Boulware*, 144 N.W.2d 711, 716 (Minn. 1966).
[43] *Pine Island Farmers Co-op v. Erstad & Reimer*, 649 N.W.2d 444, 447 (Minn. 2002); *DLH, Inc.*, 566 N.W.2d at 70.
[44] *Bond v. Comm'r of Revenue*, 691 N.W.2d 831, 836 (Minn. 2005).
[45] *Laska v. Anoka County*, 696 N.W.2d 133, 140 (Minn. Ct. App. 2005).
[46] *DLH, Inc.*, 566 N.W.2d at 71.
[47] *Bixler v. J.C. Penney Co.*, 376 N.W.2d 209, 215 (Minn. 1985).
[48] *Bebo v. Delander*, 632 N.W.2d 732, 737 (Minn. Ct. App. 2001).
[49] *Hunt v. IBM Mid-Am. Employees Fed. Credit Union*, 384 N.W.2d 853, 855 (Minn. 1986) ("In order to successfully oppose a motion for summary judgment, a party cannot rely upon mere general statements of fact but rather must demonstrate at the time the motion is made that specific facts are in existence which create a genuine issue for trial.").
[50] *Fabio v. Bellomo*, 504 N.W.2d 758, 761 (Minn. 1993).

of a genuine issue as to a material fact, the doubt must be resolved in favor of finding that the fact issue exists."[51]

Williams' Motion for Summary Judgment

Although the parties disagree about their respective motivations regarding the pre-settlement funding contract at issue here, they agree that Plaintiffs provided money to Williams for living expenses so that she could pursue her lawsuit and that she only had to pay the advances, fees and interest back if she was successful in her suit. The basis of Williams' Motion for Summary Judgment is that such an agreement is void under Minnesota law because it is champertous and in violation of public policy.

The question for this court is whether a non-recourse advance of funds secured by an interest in a pending lawsuit with a contracted interest rate in excess of 54% per year is permissible under Minnesota law. [52]

The common law prohibitions against maintenance and champerty have long been recognized in Minnesota. Although most of the case law in Minnesota dates back to the 19th and early 20th century, in 2004 the Minnesota Court of Appeals revisited the issue in *Johnson v Wright*, 682 N.W.2d 671 (Minn. App. 2004) and reaffirmed that these prohibitions are valid in the 21st century. "Champerty is defined as "[a]n agreement between a stranger to a lawsuit and a litigant by which the stranger pursues the litigant's claims as consideration for receiving part of any judgment proceeds." *Blacks Law Dictionary* 224 (7th ed.1999). Similarly, maintenance is defined as "[a]ssistance in prosecuting or defending a lawsuit given to a litigant by someone who has no bona fide interest in the case; meddling in someone else's litigation." *Blacks Law Dictionary* 965 (7th ed.1999)."[53]

The Court of Appeals in *Johnson* reviewed the case law on champerty and maintenance in Minnesota including *Huber v Johnson*, 68 Minn 74, 70 N.W.2d 806 (1897) and *Hackett v Hummel,* 185 Minn. 387, 241 N.W. 68 (1932). Citing *Huber*, the Court of Appeals noted that the purpose of these doctrines was to avoid intermeddling with lawsuits because when outsiders have a stake in the lawsuit that stake has a tendency to disrupt the remedial processes of the law.

> "The general purpose of the law against champerty and maintenance was to prevent officious intermeddlers from stirring up strife and contention by vexatious or speculative litigation which would disturb the peace of society, lead to corrupt practices, and pervert the remedial process of the law. The principle upon which it proceeded was the contracts conducive of such results were against public policy."[54]

In *Johnson*, Wright wanted to sue Mystic Lake Casino but could not afford her attorney's retainer. She entered into an agreement with Johnson to fund litigation expenses, living expenses and some personal expenses. In exchange, Johnson would receive 27.67% of her proceeds from her lawsuit. Johnson also secured the advances with a promissory note for $140,000. After

[51] *Rathbun v. W.T. Grant Co.*, 219 N.W.2d 641, 646 (Minn. 1974).
[52] The actual interest rate would be well in excess of 54%. Because the interest rate of 4.5% a month is compounded monthly the effective annual rate is 69.59%.
[53] *Johnson v. Wright*, 682 N.W.2d 671, 675 (Minn. Ct. App. 2004).
[54] *Id.* at 676

examining cases on champerty and maintenance in Minnesota and in other jurisdictions, and the underlying public policy considerations, the court concluded that the law prohibiting champerty is still valid in Minnesota. Although the court upheld the promissory note because it was not contingent on the outcome of the lawsuit and required repayment, the court held that the nonrecourse agreement to pay 27.67% of her recovery was champertous because recovery is tied to the outcome of the case. If Wright recovered nothing she was obligated to pay nothing. The court found that the agreement "effectively intermeddled and speculated in appellant's litigation and its outcome."[55]

The *Johnson* court set forth a simple standard. If a stranger to the lawsuit provides non-recourse advances that are secured with an interest in the outcome of the lawsuit, the contract is champertous and void. The Minnesota Court of Appeals was unpersuaded by the argument that unlike earlier cases, Johnson had not exercised direct control over the litigation by hiring the lawyer or requiring written consent for a settlement. The court rejected the suggestion that direct control of litigation is a necessary factor. Under *Johnson*, when a stranger advances money secured solely by the results of a lawsuit, the contract is champertous and illegal. There is no dispute that the agreement here is exactly that type of contract.

Here Plaintiffs ask the Court to reconsider Minnesota's longstanding policy against strangers taking a stake in a lawsuit, arguing that the contract in this case does not present the evils that champerty was meant to avoid. Plaintiffs argue that the prohibition against champerty, and its cousins barratry and maintenance, was primarily aimed at situations in which a stranger stirs up litigation by encouraging people to sue. There is no dispute that in the present case Williams had already decided to sue and had commenced her litigation long before she had any contact with Plaintiffs to provide additional pre-settlement funding. However, the ill effects of a contract that gives a stranger a contingent interest in the outcome of litigation go well beyond encouraging people to sue or direct control of the litigation. Such contracts should continue to be suspect because they create a disincentive to settle and because public policy does not encourage strangers profiting from the litigation of others.

The disincentive to settlement created by such agreements was explained by the Ohio Supreme Court in 2008 when it struck down a similar agreement as champertous.[56] The *Rancman* court gave an example of how such a disincentive occurs.

> "The $6000 advance, for example, gave FSF the right to the first $16,800 . . . . If there had not been any superior liens on Rancman's settlement and her attorney had charged a

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[55] *Johnson* 682 N.W.2d at 678; *See also Rancman v. Interim Settlement Funding Corp.,* 2003-Ohio-2721, 99 Ohio St. 3d 121, 125, 789 N.E.2d 217, 221 (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).

[56] *Rancman* 99 Ohio St. 3d at 124, 789 N.E.2d at 220 ("The advances sub judice constitute champerty because FSF and Interim sought to profit from Rancman's case. They also constitute maintenance because FSF and Interim each purchased a share of a suit to which they did not have an independent interest; and because the agreements provided Rancman with a disincentive to settle her case.")

> 30 percent contingency fee, Rancman would not have received any funds from a settlement of $24,000 or less. This calculation gives Rancman an absolute disincentive to settle for $24,000 or less because she would keep the $6,000 advance regardless of whether she settles with State Farm and would not receive any additional money from a $24,000 settlement."[57]

Similarly in this case, since Williams has no obligation to pay advances back unless she receives proceeds, she would have no incentive to settle the case unless it would produce more than her attorney's fees plus the amount she would owe to Holdings. As the amount owed to Holdings rapidly escalates, so too her base line settlement demands would quickly increase, very likely deterring settlement. For example, as of December 2012 Williams would have owed Holdings over $300,000. Assuming that she owed her lawyers at least 30% of any settlement, Williams would have had no reason to accept a $450,000 settlement offer. Currently when Holdings claim is $600,000, Williams would have no incentive to take a $900,000 settlement. This type of disincentive to settlement can prolong litigation and is the type of adverse influence to the remedial processes of the law that the prohibitions against champerty and maintenance were designed to avoid.[58]

Conversely, the escalating repayment schedule in this case could propel Williams to settle early for far less than she believed she was entitled because taking the time to bring a case to trial or waiting for a more favorable settlement may result in her owing Holdings such a great amount that she is left with nothing. In either scenario, a new factor has entered into the settlement process disrupting the calculation that should be based on the merits of the case rather than whether the funding contract can be repaid. Because of the potential disincentive or over-incentive to settlement that the contract in this case creates, there is a significant public policy basis to strike it down as disruptive to litigation and therefore void as against public policy.

The potential manipulation of the litigation is not confined to the dangers of an escalating repayment schedule. Other clauses in this contract could indirectly manipulate a litigant. First, the contract allows Plaintiffs to withhold payments, payments they know are necessary living expenses, rather than commit to funding through the trial. This could be used to pressure a quick resolution. Second, the contract forbids Williams from seeking another pre-settlement funder unless Holdings agrees. Thus in the instance that Holdings stops funding, as it did here, Williams would not be able to go to another source without permission. This also could force settlement or compel Williams to agree to a profitable buy out of Holdings interest at Williams' expense.[59] Third, the provision requiring Williams to hire only attorneys who would agree to

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[57] *Id.* 99 Ohio St. 3d at 124, 789 N.E.2d at 220.

[58] Even North Carolina courts, cited by Plaintiffs, recognize that pre-settlement agreements can create disincentives. *Odell v. Legal Bucks, LLC*, 192 N.C. App. 298, 309, 665 S.E.2d 767, 774 (2008) ("We share Plaintiff's concerns regarding the potential negative effects of litigation funding on a borrower's ability or willingness to settle her underlying claim, especially given our State's strong public policy in favor of encouraging settlements"). Despite its concern about the adverse effect on settlement, the court in *Odell* felt compelled to enforce the agreement because of longstanding North Carolina law which narrowly defines champerty. Minnesota has an opposite history of being broadly suspicious and consistently striking down agreements between strangers and litigants that involve a non-recourse stake in the proceeds.

[59] Although the exact reasons for the buyout of the Boston contract was not presented as part of this motion, the Court wonders if the Boston contract contained a similar prohibition thereby necessitating a buyout even though that

the provisions of this contract could limit her ability to hire counsel of her choice. Because this contract has the potential to indirectly affect Williams' decisions in the litigation, it raises the type of intermeddling concerns that the prohibitions against champerty are intended to avoid.

The question before this court is not whether these adverse effects did occur, but whether there is a sufficient risk of adverse effects to continue to uphold the prohibitions against champertous contracts that Minnesota has consistently recognized. As the Alabama Court of Appeals explained, the general tendency of these contracts to adversely interfere with litigation is what that makes them void on the ground of public policy.

> "The question whether an agreement is void on the ground that it is contrary to public policy is to be determined by its general tendency. If that is opposed to the interests of the public, the agreement is void, even though in the particular case the intent of the parties may have been good and no injury to the public may have resulted. It matters not that any particular contract is free from any taint of fraud, oppression, or corruption.... The law looks to the general tendency of such agreements, and it closes the door to temptation, by refusing them recognition in any of the courts of the country. It is enough that the contract belongs to a class which has a tendency contrary to the public good, although in the particular instance, no injury results."[60]

Public policy also does not favor speculating in a lawsuit for profit, particularly at the expense of a litigant. As the Ohio Supreme Court in *Rancman* held: "Equally troubling is a champertor's earning a handsome profit by speculating in a lawsuit and by potentially manipulating a party to the suit. However, a lawsuit is not an investment vehicle. Speculating in lawsuits is prohibited by Ohio law. An intermeddler is not permitted to gorge upon the fruits of litigation."[61] In the current case Plaintiffs charge fees of over 16% on the money they advanced, and then expected to get over 54% interest on top of that. To put this in perspective, Minnesota has set a reasonable rate of return in its usury statute of 8%.[62] On the $141,000 advanced by Plaintiffs in this case, 8% would amount to $11,280 interest in one year. Instead, at the end of one year Plaintiffs here expected to reap a profit of over $150,000. The profit as of March 31, 2014, approximately two years after the loan, would be $450,000. There is good reason to question profiteering at this level.

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contract was finished. The buyout gave Williams no additional benefit and simply increased the fees and interest rate on the amounts Boston had extended.

[60] *Wilson v. Harris*, 688 So. 2d 265, 270 (Ala. Civ. App. 1996) citing *Samplíner v. Motion Picture Patents Co.,* 255 F. 242, 251-52 (2d Cir.1918), rev'd on other grounds, 254 U.S. 233, 41 S.Ct. 79, 65 L.Ed. 240 (1920).

[61] *Rancman,* 99 Ohio St. 3d at 125, 789 N.E.2d at 221

[62] Minn. Stat 334.01. The Court notes that the 8% cap does not apply to loans over $100,000. Although the initial advance was for $107,000, most of that advance went to pay off Boston. The additional funding that Williams received from Plaintiffs was less than $35,000. The Court has been troubled by why there was a need for Plaintiffs to pay off the Boston contract which was ending on its own terms. Buying out Boston simply increased the rate of interest for Williams on the entire amount dramatically increasing the amount of profit to Plaintiffs. It is also troubling that Boston invests in Plaintiffs so that this was not an arm's length transaction.

The unbridled profit in this contract potentially strips the victim of compensation for her injury. In a very short time Holdings can make an immense profit and leave Ms. Williams with nothing. The Court fails to understand how public policy should condone a contract that essentially sweeps the entire proceeds of a damage award away from the injured party into the hands of investors preying on the desperation of people who do not even have the means to meet their daily living necessities. Plaintiffs have offered no rationale for why a contract that would pay them fully and leave Williams with nothing is in her or the public interest other than suggest that it leaves her no worse off than if her suit had never been brought. Even that contention is doubtful given the toll both emotionally and in time expended that any lawsuit, especially one based on a sexual assault, entails.

Although funding a needy litigant with living expenses could have a benefit, the risks of abuse for such a person in need are high. Although Plaintiffs could have taken the safe harbor offered under Minnesota law and loaned money to Ms. Williams secured by a lien on the litigation proceeds, such a loan would have been covered by many regulations and laws to protect unsophisticated consumers. Instead Plaintiffs chose a different unregulated route with a profit potential of over 54% annual interest. The undisputed facts do not support Plaintiffs' assertion that their risk of total loss supported such a high premium. Despite their repeated claims that the investment was very risky, their own statements belie that characterization. At the time Ms. Greening made the decision to advance $140,000 she believed settlement of no less than $1.3 million dollars was expected in just a few months. This level of profit is at best suspect. Without legislative guidance, the risk of abusive profit-taking in these situations justifies striking such high-interest repayment schemes as violating public policy.

Plaintiffs argue that champerty is an old fashioned concept that no longer has relevance. Although some states have greatly loosened or eliminated prohibitions on people taking interests in lawsuits, Minnesota has not. For over 100 years it has consistently stuck down agreements like the one in this case, for strong public policy reasons which are still valid. This contract violates the very simple test reaffirmed in *Johnson* that strangers cannot advance money with repayment based solely on the resolution of a lawsuit. In addition, other aspects of this contract such as the high interest rate, the alternative funding prohibition, and lack of a repayment ceiling, heighten the concern over influencing settlement and possibly inequitably stripping a victim of her damage compensation, making Williams' contract even more suspect on public policy grounds.

Whether any such pre-funding contract should ever be seen as a benefit to allow access to the legal system, as Plaintiffs argue, is not before this court. Minnesota does recognize some situations, like attorney contingency fees, that allow for an interest in the outcome of litigation. But these are tightly proscribed by the Rules of Professional Responsibility and judicial oversight as to reasonableness. No oversight exists here. Since by its very nature the persons seeking pre-settlement funding for necessary living expenses are vulnerable and are not in a position to bargain or seek more reasonable choices, a decision to allow such funding in Minnesota should be made by the legislature which could put reasonable parameters in place and require disclosures to address the real public policy concerns raised by these contracts.

Plaintiffs have failed to provide a compelling reason to abandon Minnesota's long standing public policy against strangers speculating on lawsuits. The agreement between

Plaintiffs and Williams will be declared void as contrary to the public policy of the state of Minnesota.

Other Collateral Matters: Unjust Enrichment and Defendant's Attorney's Fees

Based on the Court's finding that the contract is void as contrary to public policy, Plaintffs' Unjust Enrichment claim will also be dismissed. Plaintiffs cannot bring a claim in equity to be compensated for an agreement that has been found to violate public policy. In an early champerty case the Minnesota Supreme Court specifically held that parties could not indirectly enforce the champertous contract through an equity claim for quantum meruit. [63] Similarly in contracts struck down as usurious the courts have held that the lender can receive no compensation.[64] The court finds that since the contract in its essence violates public policy, Plaintiffs can recover nothing in law or equity. Also because the contract is void, Williams' claim for attorney's fees which derives from the contract is also unenforceable.

Motion to Strike

Although the Court is dismissing Plaintiffs' claims, making the Motion to Strike moot, in anticipation of a possible appeal the Court is issuing a decision on Plaintiffs' Motion to Strike in the event that the matter is remanded to this court for further proceedings.

1. Unclean Hands. Plaintiffs' argue that Unclean Hands is only a defense to an equitable claim. However, Plaintiffs have raised an equitable claim of Unjust Enrichment. The Court finds that Defendant has stated sufficient facts in her Second Amended Answer and in these proceedings to support its defense and allow this defense to proceed if Plaintiffs are ever allowed to proceed with their equitable claim.

2. Contract of Adhesion. Plaintiffs argue that this cannot be a contract of adhesion because Defendant Williams bargained hard for the terms. But this is a disputed question of fact. The Court finds that the Defendant has stated sufficient facts in her Second Amended Answer and in these proceeding to support this defense and to allow this defense to proceed if Plaintiffs are ever allowed to proceed on their contract claims.

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[63] See *Gammons v. Johnson,* 76 Minn. 76, 82, 78 N.W. 1035, 1037-38 (1899) ("To hold that a party can thus illegally stir up and instigate litigation, and yet obtain the benefits of it by ignoring the special contracts, and bringing suit upon a quantum meruit for services performed in prosecuting the litigation which he has unlawfully instigated, would be a travesty on justice, and to permit a party to do indirectly what he cannot do directly")
See also Rancman 789 NE 2d at 221. Although not asked directly to consider alternative equitable relief, the court strongly stated that there should be no recovery. (The advances made to Rancman constituted champerty and maintenance. Consequently, the contracts requiring their repayment are void and shall not be enforced).

[64] See numerous Minnesota cases holding when a contract is held void because it is usurious, the lender cannot recover either the principle or interest. *Fogie v. THORN Americas, Inc*., 190 F.3d 889, 900 (8th Cir. 1999) (" Minnesota courts have long stated that, when a victim of usury cancels a usurious contract, the victim does not need to compensate the usurer for the goods obtained under the usurious contract as a condition for receiving cancellation. In *Trauernicht v. Kingston,* 156 Minn. 442, 195 N.W. 278 (1923), the Minnesota Supreme Court stated 'The general rule over the country is that a borrower on usury when he comes to a court of equity asking affirmative relief by way of the cancellation of an obligation ... must restore the money actually received.... Our own rule, often announced, is that restoration need not be made.'")

Plaintiff's Motion for Summary Judgment on Breach of Contract

Because the Court has found that the contract is void for public policy, Plaintiff's motion based entirely on breach of contract has no basis, and must be denied.

ORDER

1. Defendant's Motion for Summary Judgment is **GRANTED.** The agreement between Plaintiffs and Williams is declared void as contrary to the public policy of the state of Minnesota.

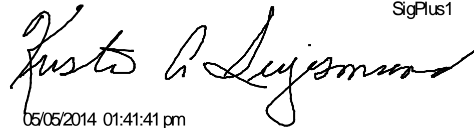
2. All of Plaintiffs' counts in the complaint are **DISMISSED WITH PREJUDICE.**

3. Plaintiffs' motion to strike is entirely **DENIED**.

4. Plaintiffs' Summary Judgment motion for breach of contract is **DENIED.**

LET JUDGEMENT BE ENTERED ACCORDINGLY

BY THE COURT:



Dated: May 5, 2014

The Honorable Kristin A. Siegesmund
Judge of District Court