IN FOR A PENNY AND OUT FOR PROFIT: A FEDERAL APPROACH TO CONSUMER THIRD-PARTY LITIGATION FUNDING

Abstract: The third-party litigation funding market in the United States is growing at a tremendous pace. The pace of regulation, however, is far from commensurate. Third-party litigation funding, or TPLF, is currently regulated by a patchwork of state regimes that draw on usury prohibitions, bespoke statutes, and the ancient common-law doctrines of champerty and maintenance. Although TPLF is not regulated at the federal level today, the *Howey* Test from the U.S. Supreme Court's 1946 decision in *SEC v. W.J. Howey Company* provides a flexible standard through which TPLF agreements can be brought under the regulatory purview of the Securities Act of 1933 and the Securities Exchange Act of 1934. This Note argues that consumer TPLF agreements should be regulated as investment contracts under existing federal securities law, rather than as loans at the individual state level.

INTRODUCTION

In the wake of *The New York Times*' 2017 exposé revealing Harvey Weinstein's sexually abusive conduct, perhaps the last source of criticism Weinstein expected was a Brooklyn-based litigation funding company.[1] Via X, formerly known as Twitter, LawCash informed "#HarveyWeinstein" that "sexual abuse is a crime" before proceeding to advertise its funding services for plaintiffs in civil cases involving sexual abuse.[2]

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[1] *See* LawCash (@LawCash1), X (Oct. 25, 2017, 5:00 PM), https://twitter.com/LawCash1/status/923293284998377472?ref_src=twsrc%5Etfw [https://perma.cc/LE62-SCAD] (advertising funding assistance for sexual abuse lawsuits); Jodi Kantor & Megan Twohey, *Harvey Weinstein Paid Off Sexual Harassment Accusers for Decades*, N.Y. TIMES (Oct. 5, 2017), https://www.nytimes.com/2017/10/05/us/harvey-weinstein-harassment-allegations.html [https://web.archive.org/web/20230920041321/https://www.nytimes.com/2017/10/05/us/harvey-weinstein-harassment-allegations.html] (detailing multiple victim accounts of Weinstein's sexual harassment and assault over a two-decade period and the producer's attempts to cover up his conduct). Weinstein, an acclaimed movie producer, was convicted of a first-degree criminal sexual act and third-degree rape in New York in February of 2020. *See Harvey Weinstein Timeline: How the Scandal Unfolded*, BBC NEWS, https://www.bbc.com/news/entertainment-arts-41594672 [https://perma.cc/F7CM-J544] (Feb. 24, 2023) (providing a timeline of the accusations and legal proceedings against Weinstein from October 2017 through February 2023). He is currently serving a twenty-three year sentence in connection with the charges. *Id.* In December 2022, Weinstein was separately convicted of three sex crimes in California. James Queally, Noah Goldberg & Richard Winton, *Harvey Weinstein Convicted of Rape in Los Angeles*, L.A. TIMES, https://www.latimes.com/california/story/2022-12-19/harvey-weinstein-verdict-in-los-angeles [https://perma.cc/2QBT-887D] (Dec. 19, 2022).

[2] *See* LawCash (@LawCash1), *supra* note 1 (drawing on the accusations against Weinstein to advertise LawCash's legal funding services). In November 2021, LawCash joined with two other

On the opposite coast, one of LawCash's competitors, Nova Legal Funding, had recently inked one such funding deal with Heather Rothermund.[3] Rothermund sued her employer for $250,000 after the employer failed to discipline a coworker who sexually assaulted her.[4] While the case wound through the court system, Rothermund faced repossession of her car and dwindling financial assets as she attempted to pay for therapy and medications related to post-assault treatment.[5] After coming across Nova in an online advertisement, Rothermund agreed to a $2,000 advance from Nova against her future settlement with her employer.[6] The catch: Rothermund would owe Nova $4,000 if the case settled within the year and even more if the settlement timeline extended further.[7]

Elsewhere in California, Underwood Ranches filed a complaint against sriracha-maker Huy Fong Foods for intentional misrepresentation and concealment claims in August 2017.[8] Although a California court awarded the

litigation funding companies to do business under the unified brand Cartiga, with offices in New York City, New York and Boca Raton, Florida. *See LawCash, Momentum Funding, and Ardec Funding Will Merge to Form Cartiga—Push the Legal Tech and Financial Industry Forward*, PR NEWSWIRE (Nov. 17, 2021), https://www.prnewswire.com/news-releases/lawcash-momentum-funding-and-ardec-funding-will-merge-to-form-cartiga—push-the-legal-tech-and-financial-industry-forward-301427220.html [https://perma.cc/T6EU-VG8A] (announcing the merger to the public); *Contact Us: How Can We Help?*, CARTIGA (2022), https://cartiga.com/contact-us/ [https://perma.cc/7W5X-PDRQ] (providing contact information and locations for the company).

[3] *See* Matthew Goldstein & Jessica Silver-Greenberg, *How the Finance Industry Is Trying to Cash In on #MeToo*, N.Y. TIMES (Jan. 28, 2018), https://www.nytimes.com/2018/01/28/business/metoo-finance-lawsuits-harassment.html [https://perma.cc/2YPU-P9RD] (discussing third-party litigation funding in the context of the #MeToo movement). The #MeToo movement, in broad terms, describes the ongoing global movement to increase awareness and activism around gender-based violence and sexual harassment. *See "MeToo" Global Movement*, GLOB. FUND FOR WOMEN (2023), https://www.globalfundforwomen.org/movements/me-too/ [https://perma.cc/2729-HYPH] (defining the movement as it coalesced in 2017). According to its corporate website, Nova Legal Funding is headquartered in Los Angeles, California and most frequently provides funding for suits involving auto accidents, wrongful deaths, premise liability, and traumatic brain injuries. *See About Nova Legal Funding*, NOVA LEGAL FUNDING (2023), https://fundmylawsuitnow.com/about/ [https://perma.cc/RER2-7687] (providing an overview of the company).

[4] Goldstein, *supra* note 3.

[5] *Id.*

[6] *Id.*

[7] *Id.* As of 2022, on its "Lawsuit Loan Calculator" webpage, Nova Legal Funding states that its lawsuit loan interest rates are between 1–3%. *See What Will the Interest Rate on My Lawsuit Loan Be? (Calculator)*, NOVA L. FUNDING, https://fundmylawsuitnow.com/how-much-do-lawsuit-loans-cost/#How_Does_Nova_Legal_Funding_Set_Interest_Rates [https://perma.cc/RJ7T-KVGZ] (Feb. 24, 2023) (explaining the process by which Nova Legal Funding sets interest rates).

[8] *See* Judgment at *1–2, Huy Fong Foods, Inc. v. Underwood Ranches LP, No. 56-2017-00505141-CU-BC-VTA (Cal. Super. Aug. 26, 2019), 2019 WL 4919921 (reporting the initial complaint filing date and causes of action); Maeve Allsop, *Sriracha Maker Must Pay $23 Million to Pepper Farm in Fraud Suit*, BLOOMBERG L. (July 27, 2021), https://news.bloomberglaw.com/litigation/sriracha-maker-must-pay-23-million-to-pepper-farm-in-fraud-suit [https://perma.cc/LQ9J-Q2KG] (discussing the factual background of the case).

family-owned and operated farm $23 million in economic and punitive damages in 2019, the payout was halted pending the outcome of Huy Fong Foods' appeal.[9] When the state appellate court affirmed the verdict in 2021, Underwood Ranches collected the $23 million and promptly turned $8 million of the award over to litigation funding company Burford Capital.[10] The $8 million represented full repayment of a $4 million settlement advance provided to Underwood Ranches by Burford Capital in the years between the jury trial and the appellate decision, plus 100% interest.[11]

In 2021, third-party litigation funding (hereinafter "TPLF") investments grew 16% year-over-year and totaled roughly $17 billion globally.[12] The United States accounts for 52% of the global TPLF market.[13] About two-thirds of TPLF funds in the United States are invested in commercial lawsuits like that of Underwood Ranches, with the remaining one-third invested in so-called "consumer" lawsuits brought by individuals like Heather Rothermund.[14] The consumer TPLF market, in particular, is at least nominally intended to mitigate economic barriers to bringing forward meritorious lawsuits.[15] And yet, despite the size, scope, and purported social function of the industry, state statutory regulations for TPLF are disjointed, state-level common law is in flux, and federal regulation is effectively non-existent.[16]

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[9] *See* Judgment, *Huy Fong Foods, Inc.*, No. 56-2017-00505141-CU-BC-VTA, at *3 (providing the verdict and damages award); *60 Minutes: Convoy of Life, Litigation Funding, Lourdes* (CBS television broadcast, Dec. 18, 2022) (discussing Underwood Farms' lawsuit in the broader context of the litigation funding industry).

[10] *See* Huy Fong Foods, Inc. v. Underwood Ranches, LP, 281 Cal. Rptr. 3d 757, 761 (Ct. App. 2021) (affirming the verdict for Underwood Ranches and $23 million award amount, of which $13 million represented economic damages and $10 million represented punitive damages); *60 Minutes: Convoy of Life, Litigation Funding, Lourdes*, *supra* note 9 (interviewing the owner of Underwood Farms about his funding agreement with Burford Capital).

[11] *See 60 Minutes: Convoy of Life, Litigation Funding, Lourdes*, *supra* note 9 (querying the owner of Underwood Farms about the ultimate amount paid to Burford Capital). Burford Capital, which went public on the London Stock Exchange in 2009 in the Alternative Investment Market and on the New York Stock Exchange in 2020, was founded in 2009 by Christopher Bogart, a former general counsel for Time Warner, and Jonathan Molot, a professor at the Georgetown University Law Center. *About Burford*, BURFORD CAP., https://www.burfordcapital.com/about-burford/ [https://perma.cc/63SJ-GGDK].

[12] *See* IRINA FAN ET AL., SWISS RE INST., U.S. LITIGATION FUNDING AND SOCIAL INFLATION 8 (2021) (exploring the quantitative and qualitative dimensions of the TPLF market in both the United States and globally).

[13] *Id.*

[14] *Id.*; *see supra* notes 3–7 and accompanying text (describing Rothermund's litigation funding agreement in connection with her employer negligence lawsuit); notes 8–11 and accompanying text (describing Underwood Ranches' litigation funding agreement in connection with the company's commercial contract-related lawsuit).

[15] *See infra* notes 178–181, 195, and accompanying text (discussing the professed social benefits of consumer TPLF Agreements).

[16] *See* Latif Zaman, *ABA Outlines Best Practices for Third-Party Litigation Funding*, ABA (Dec. 10, 2020), https://www.americanbar.org/groups/business_law/publications/committee_newsletters/

Part I of this Note describes the rise of litigation funding in the United States, the assortment of state approaches under which the consumer TPLF industry is currently regulated, and the legal tests that determine the contractual arrangements to which the Securities Act of 1933 and the Securities Exchange Act of 1934 attach.[17] Part II contrasts the application of state-level usury prohibitions to consumer TPLF Agreements with the application of federal securities laws to such Agreements.[18] Part III argues for unified federal regulation of consumer TPLF Agreements under the provisions of the Securities Act of 1933 and Securities Exchange Act of 1934.[19]

I. UNDERSTANDING CONSUMER TPLF AND ATTEMPTS TO REGULATE IT

The American TPLF industry is broadly divided into commercial and consumer sectors, although both commercial and consumer TPLF Agreements serve the same core function.[20] In commercial TPLF Agreements, a TPLF provider supplies large sums of money to parties typically engaged in commercial lawsuits.[21] In exchange, the providers receive an agreed-upon percentage of the client companies' ultimate recovery.[22] Parties seeking commercial TPLF Agreements are generally large and sophisticated entities seeking amounts in at

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consumer/2020/202011/third-party/ [https://web.archive.org/web/20210119124759/https://www.americanbar.org/groups/business_law/publications/committee_newsletters/consumer/2020/202011/third-party/] (introducing the American Bar Association's recommendations for attorneys working within the structures of clients' TPLF Agreements); *infra* notes 20–101 and accompanying text (describing the current state of TPLF regulation at the state and federal levels).

[17] *See infra notes* 20–101 and accompanying text.

[18] *See infra notes* 102–181 and accompanying text. Note that, although a basic understanding of commercial TPLF is essential to understanding the TPLF industry, this Note focuses specifically on the consumer TPLF sector.

[19] *See infra notes* 182–204 and accompanying text.

[20] *See* Ronen Avraham & Anthony Sebok, *An Empirical Investigation of Third Party Consumer Litigant Funding*, 104 CORNELL L. REV. 1133, 1135 (2019) (providing an overview of the American TPLF industry structure); Wendy Gerwick Couture, *Securities Regulation of Alternative Litigation Finance*, 42 SEC. REG. L.J. 5, 6 (2014) (same). In the United States, Perry Walton is often credited with jumpstarting the litigation funding industry. *See* Jenna Wims Hashway, *Litigation Loansharks: A History of Litigation Lending and a Proposal to Bring Litigation Advances Within the Protection of Usury Laws*, 17 ROGER WILLIAMS UNIV. L. REV. 750, 754 (2012) (tracing the history of the American litigation funding industry to Walton's business endeavors in the late 1990s). Walton, who previously served an eighteen-month probation sentence for extortion in connection with a separate lending business, opened Future Settlement Funding Corp. in 1998. *Id.* Through Future Settlement Funding Corp., Walton provided money advances to lawsuit plaintiffs with repayment dependent on the plaintiff's receipt of a monetary award from the suit. *Id.* Given that he could only collect on these arrangements if a plaintiff was successful, Perry marketed the advances as "contingent obligations" rather than loans. *Id.* As part of his business, Walton hosted for-pay seminars to educate others about establishing similar companies and trained four hundred attendees within the first two years of doing so. *Id.*

[21] *See* Avraham & Sebok, *supra* note 20, at 1135 (describing the typical structure of a commercial TPLF Agreement); Couture, *supra* note 20, at 6 (same).

[22] *See* Couture, *supra* note 20, at 6 (describing common fee structures in commercial TPLF Agreements).

least the hundreds of thousands.[23] Consumer TPLF Agreements, in contrast, provide funding directly to an individual litigant.[24] The individual, like the commercial client, promises a certain portion of their ultimate recovery to the TPLF provider in exchange for immediate access to funds, but he or she is also subject to regular interest charges based on a monthly or annual calculation arrangement.[25] Both commercial and consumer TPLF Agreements are typically structured as nonrecourse, where the TPLF provider is repaid only if the lawsuit results in a monetary award.[26]

Section A explores the common-law doctrines of champerty and maintenance as they apply to TPLF Agreements.[27] Section B discusses both successful and unsuccessful attempts to leverage common-law usury as a TPLF regulatory tool.[28] Section C examines three sample state statutes regulating consumer TPLF Agreements.[29] Section D introduces the Securities Act of 1933, the Securities Exchange Act of 1934, and governing federal case law as to the definition of an "investment contract" under these Acts.[30]

A. Champerty and Maintenance

The ancient common-law champerty and maintenance doctrines prohibit third parties from obtaining a stake in another party's lawsuit and inform foun-

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[23] *See* Avraham & Sebok, *supra* note 20, at 1135 (characterizing clients in commercial TPLF Agreements); Couture, *supra* note 20, at 6 (same). The scale of such investments, in addition to providing potentially significant returns to TPLF providers, has in recent years attracted outside private equity interest from institutions like D.E. Shaw & Co., Elliott Management Corp., and TowerBrook Capital Partners. *See* Katharine Gemmell, *Here's How Hedge Funds Are Speculating on Justice*, WASH. POST (Aug. 27, 2022), https://www.washingtonpost.com/business/heres-how-hedge-funds-are-speculating-on-justice/2022/08/27/a4f9dc68-2602-11ed-a72f-1e7149072fbc_story.html [https://perma.cc/787A-46G7] (summarizing the scale of and major players in, the TPLF market).

[24] *See* Avraham & Sebok, *supra* note 20, at 1135 (contrasting clients in commercial versus consumer TPLF Agreements); Couture, *supra* note 20, at 6 (noting that consumer TPLF Agreements are most commonly entered into by individual plaintiffs in personal injury cases).

[25] *See* Avraham & Sebok, *supra* note 20, at 1135 (describing the common structure of consumer TPLF Agreements); Couture, *supra* note 20, at 6 (same).

[26] *See* MARK POPOLIZIO, VERISK, FOLLOW THE NEW MONEY TRAIL: THE RISE OF THIRD-PARTY LITIGATION FUNDING 3 (2021) (describing the basic TPLF structure in the United States market); Couture, *supra* note 20, at 6 (same). In nonrecourse arrangements, a borrower cannot be held personally liable for the value of his or her debt, and the lender may only recover up to the previously agreed-upon collateral even when such collateral is insufficient to cover the full amount. *Nonrecourse*, LEGAL INFO. INST., https://www.law.cornell.edu/wex/nonrecourse [https://perma.cc/SKU4-PP32] (Sept. 2021). In recourse arrangements, a borrower is personally liable for the debt, and the lender may collect non-collateral assets in satisfaction of the debt. *Id.*

[27] *See infra* notes 31–44 and accompanying text.

[28] *See infra* notes 45–73 and accompanying text.

[29] *See infra* notes 74–86 and accompanying text.

[30] *See infra* notes 87–101 and accompanying text.

dational assessments of TPLF's basic legality.[31] The maintenance prohibition bans a third party with no legitimate interest in a lawsuit from promoting, supporting, or maintaining that lawsuit.[32] The prohibition on champerty, as a specific subtype of maintenance, disallows arrangements in which one party agrees to assist another in bringing a lawsuit in exchange for a portion of the monetary award from that lawsuit.[33]

Although the typical structure of TPLF Agreements seems to run afoul of the common-law bar on champertous agreements, many states either no longer recognize champerty or have limited its application.[34] Minnesota is one such recent example.[35] In 2020, in *Maslowski v. Prospect Funding Partners*, the

[31] *See* Julia H. McLaughlin, *Litigation Funding: Charting a Legal and Ethical Course*, 31 VT. L. REV. 615, 624–25 (2007) (describing the relationship between TPLF and champerty and maintenance); Susan Lorde Martin, *Syndicated Lawsuits: Illegal Champerty or New Business Opportunity*, 30 AM. BUS. L.J. 485, 498 (1992) (referring to the determination of whether TPLF Agreements are champertous as the "main issue" in cases in which TPLF is involved). In earlier editions, *Black's Law Dictionary* defined champerty as "a bargain by a stranger with a party to a suit, by which such third party undertakes to carry on the litigation at this own cost and risk, in consideration of receiving, if successful, a part of the proceeds or subject sought to be recovered." *Champerty*, BLACK'S LAW DICTIONARY 292 (4th ed. 1968). Maintenance was defined as "an unauthorized and officious intermeddling in a suit in which the offender has no interest, to assist one of the parties to it, against the other, with money or advice to prosecute or defend the action." *Maintenance*, BLACK'S LAW DICTIONARY 1106 (4th ed. 1968). More recent editions of *Black's Law Dictionary* fold the concept of maintenance into champerty. *See Champerty*, BLACK'S LAW DICTIONARY 262 (9th ed. 2009) (defining champerty as "an agreement between an officious intermeddler in a lawsuit and a litigant by which the intermeddler helps pursue the litigant's claim as consideration for receiving part of any judgment proceeds; specif., an agreement to divide litigation proceeds between the owner of the litigated claim and a party unrelated to the lawsuit who supports or helps enforce the claim"). Doctrinal predecessors of champerty and maintenance existed in ancient Greek and Roman law. *See* Max Radin, *Maintenance by Champerty*, 24 CAL. L. REV. 48, 49, 51–52 (1935) (discussing the role of such concepts as *sycophanteia*, *calumnia*, and *praevericatio* in Greek and Roman law).

[32] *See* McLaughlin, *supra* note 31, at 624–25 (providing a contextual definition of maintenance); RESTATEMENT (FIRST) OF CONTRACTS § 540 (AM. L. INST. 1932) (defining the doctrine of maintenance).

[33] *See* McLaughlin, *supra* note 31, at 624–25 (defining champerty); Susan Lorde Martin, *Financing Litigation On-Line: Usury and Other Obstacles*, 1 DEPAUL BUS. & COM. L.J. 85, 87 (2002) (same); RESTATEMENT (FIRST) OF CONTRACTS § 540 (same).

[34] *See Champerty and Maintenance*, ARC: ALL. FOR RESPONSIBLE CONSUMER LEGAL FUNDING, http://arclegalfunding.org/champerty-and-maintenance/ [https://perma.cc/2RXR-5Y9G] (discussing the current legal status of champerty in the United States) (2016). More than thirty states no longer recognize the common-law doctrines of champerty and maintenance. *See id.* (listing states that have ended their recognition of the doctrines). States that have eliminated champerty and maintenance have done so through both state court decisions and via statute. *See, e.g.*, OHIO REV. CODE § 1349.55 (2022) (abrogating the state's champerty prohibition); Osprey, Inc. v. Cabana Ltd., 532 S.E.2d 269, 277 (S.C. 2000) (ending champerty as a common-law defense in South Carolina); Saladini v. Righellis, 687 N.E.2d 1224, 1224 (Mass. 1997) (holding that Massachusetts no longer recognizes champerty).

[35] *See* Maslowski v. Prospect Funding Partners, LLC, 944 N.W.2d 235, 241 (Minn. 2020) (overturning the common-law bar on champerty in Minnesota). In *Maslowski*, a plaintiff in a personal injury lawsuit sought judgment declaring her consumer TPLF Agreement void as a matter of champerty. *Id.* at 236–37. In the agreement, which was nonrecourse, the plaintiff received $6,000 from the de-

Minnesota Supreme Court ended the state's long-standing champerty prohibition as a matter of public policy.[36] The *Maslowski* court determined that changes in society's attitude toward litigation, such as the widespread use of contingency fee arrangements previously barred by the common law and developments in the legal profession's self-regulation, rendered the champerty prohibition unnecessary.[37]

The state of New York, in contrast, continues to ban champertous arrangements via statute.[38] Even this statutory ban, however, is not airtight.[39] First, as written, New York's statutory ban includes a safe harbor provision excluding transactions involving $500,000 or more.[40] Second, the statute is subject to a "primary purpose" limitation that New York courts have expanded over time.[41] Under this limitation, a transaction can only be champertous, and therefore prohibited, if its principal objective is to bring a legal claim or suit.[42]

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fendant upfront in anticipation of her eventual monetary award from the lawsuit. *Id.* at 236. In exchange, the plaintiff, assuming she received a monetary award, owed back the $6,000 plus fees. *Id.* Every six months, the total amount owed increased 30%, up to a $25,245 maximum. *Id.*

[36] *See id.* at 237, 240–41 (asserting that Minnesota's modern rules of civil procedure, attorney conduct, and still-existing common-law defense of unconscionability were sufficient to address the abuses against which the champerty prohibition was intended to protect). In *Maslowski*, the court overturned state precedent on champerty dating as far back as 1897 and most recently reaffirmed in 1932. *See id.* at 241; *see, e.g.*, Hackett v. Hammel, 241 N.W. 68, 69 (Minn. 1932) (voiding a contract between a plaintiff involved in a property dispute over an iron mine and a defendant who provided a $705 advance in exchange for "ten times the amount so advanced" if the plaintiff won the suit); Holland v. Sheehan, 122 N.W. 1, 2–3 (Minn. 1909) (voiding an agreement between an attorney and an individual, in which the individual sought out plaintiffs for the attorney in exchange for a percentage of such plaintiffs' future settlements); Gammons v. Johnson, 78 N.W. 1035, 1037–38 (Minn. 1899) (barring an attorney from seeking plaintiffs who would agree to attorney-funded suits against a railroad, provided the attorney received a portion of the ultimate proceeds from the suits); Huber v. Johnson, 70 N.W. 806, 807 (Minn. 1897) (first setting out Minnesota's prohibition on champerty and declaring such a prohibition as intended 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").

[37] *See Maslowski*, 944 N.W.2d at 238–240 (providing the court's rationale in ending the state's champerty prohibition).

[38] N.Y. JUDICIARY LAW § 489(1) (2014).

[39] *See id.* § 489(2) (defining the scope of the champerty statute, including its safe harbor provision); JAMES J. BILSBORROW ET AL., N.Y.C. BAR ASS'N, REP. TO THE PRESIDENT BY THE N.Y.C. BAR ASS'N WORKING GROUP ON LITIG. FUNDING 7–8 (2020) (laying out both the statutory and common-law regulatory schemes of TPLF in New York).

[40] N.Y. JUDICIARY LAW § 489(2); *see* N.Y.C. BAR ASS'N, *supra* note 39, at 7 (describing the statutory safe harbor). Consumer TPLF Agreements typically involve claims between $500 and $100,000. *See* Paige Marta Skiba & Jean Xiao, *Consumer Litigation Funding: Just Another Form of Payday Lending?*, 80 LAW & CONTEMP. PROBS. 117, 122 (2017) (reporting the dollar value range of consumer TPLF Arrangements, with $100,000 at the high end of that range).

[41] *See* N.Y.C. BAR ASS'N, *supra* note 39, at 7–8 (noting the "primary purpose" requirement under New York law).

[42] N.Y. JUDICIARY LAW § 489(1); *See* Bluebird Partners, L.P. v. First Fidelity Bank, N.A., 731 N.E.2d 581, 587 (N.Y. 2000) (explaining that, for a claim to be champertous, "the foundational intent to sue on that claim must at least have been the primary purpose for, if not the sole motivation behind,

In the TPLF context, courts have come to conflicting conclusions about the champertous nature of TPLF Agreements based on this "primary purpose" limitation.[43] Statutes and common-law regimes banning champerty in other states similarly vary in construction and application.[44]

B. Usury as a TPLF Regulatory Tool

Usury laws, which can be found in the annals of nearly every ancient society, are largely the domain of individual states.[45] Usury typically consists of four core elements: (1) a monetary loan; (2) an absolute repayment obligation on the borrower as to the principal amount due on that loan; (3) a rate of interest charged by the lender that exceeds the rate allowed under the relevant jurisdiction's law; and (4) intentional violation of the law by the lender.[46] Usury laws have emerged as a potential counterweight to the rapid growth of the TPLF industry in the United States beginning in the 1990s, although outcomes are highly dependent on the jurisdiction and the specific funding arrangement.[47]

Subsection 1 of this Section examines state cases that exemplify the legal arguments that undermine the application of usury prohibitions to TPLF Agreements.[48] Subsection 2, in contrast, presents state cases in which usury prohibitions have been successfully applied to such agreements.[49]

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entering into the transaction"); Moses v. McDivitt, 88 N.Y. 62, 65 (N.Y. 1882) (interpreting the predecessor statute of § 489 to be subject to a similar "primary purpose" limitation).

[43] *Compare, e.g.*, Justinian Cap. SPC v. WestLB AG, 65 N.E.3d 1253, 1254–57 (N.Y. 2016) (finding the plaintiff's third-party-funded purchase of notes in an investment vehicle for the explicit purpose of suing the manager of the vehicle was an impermissible champertous agreement because the notes were purchased with the "primary purpose" of suing the defendant), *with* Echeverria v. Est. of Lindner, 2005 N.Y. Slip Op. 50675(u), at *5 (Sup. Ct. 2005), *judgment entered sub nom.* Echeverria v. Lindner (N.Y. Sup. Ct. 2005) (finding the plaintiff's litigation funding agreement did not constitute champerty because the agreement was made *after* the plaintiff had already brought the suit, such that the agreement failed the "primary purpose" test).

[44] *See generally* Martin, *Financing Litigation On-Line*, *supra* note 33, at 87–88 (giving examples of champerty prohibitions from various states).

[45] *See* Mitchell Edwards & Matthew McDonnell, *What Litigators Should Know About Usury Laws*, ABA (Apr. 19, 2022), https://www.americanbar.org/groups/litigation/committees/commercial-business/practice/2022/what-litigators-should-know-about-usury-laws/ [https://perma.cc/XNK9-46SL] (summarizing the general landscape of usury laws in the United States). *See generally* CHARLES R. GEISST, *Saints and Sinners*, *in* BEGGAR THY NEIGHBOR: A HISTORY OF USURY AND DEBT 13, 13–57 (2013) (describing the role of usury laws throughout Middle Eastern and Western history). Defined broadly, usury is the levying of an illegally high interest rate; the actual interest rate or range considered to be usurious is a state-by-state decision. 75 AM. JUR. PROOF OF FACTS 3D *Proof of Violation of State Usury Consumer Loan Law* § 103 (2003).

[46] 75 AM. JUR. PROOF OF FACTS 3D, *supra* note 45.

[47] *See infra* notes 50–73 and accompanying text.

[48] *See infra* notes 50–58 and accompanying text.

[49] *See infra* notes 59–73 and accompanying text.

1. Usury as an Unsuccessful State-Level Challenge to TPLF Agreements

In 1996, in *Kraft v. Mason*, the Florida Fourth District Court of Appeal rejected a usury challenge to a litigation funding agreement between two siblings.[50] As a threshold matter, the court in *Kraft* disposed of the notion that the defendant possessed the requisite intent to collect interest at an imputed rate higher than allowed by Florida law.[51] With broader implications, the court in *Kraft* also determined that usury could not exist in a lending agreement in which payment to the lender is uncertain.[52] That neither repayment itself nor the amount of repayment were known to the lender at the time of the transaction sufficiently persuaded the court that any amounts received by the lender in excess of the principal was more accurately interpreted as a "bonus" for engaging in a risky transaction, rather than improperly charged interest.[53]

In 2006, in *Anglo-Dutch Petroleum International, Inc. v. Haskell*, the Court of Appeals of Texas considered for the first time whether litigation funding agreements could be considered usurious.[54] Although the case involved a commercial, rather than consumer, TPLF Agreement, the court in *Anglo-Dutch* relied on legal reasoning similar to that of the court in *Kraft* in declining to find the agreement usurious.[55] The plaintiff, a large oil company, solicited investments from third parties to help fund its trade secret lawsuit against two of its competitors, in which it sought $650 million in damages.[56] Upon reaching a settlement with the defendants, the plaintiff, citing Texas public policy, informed the third-party funders that their agreements with the plaintiff were

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[50] *See* Kraft v. Mason, 668 So. 2d 679, 681–82, 684 (Fla. Dist. Ct. App. 1996) (laying out the facts of the case and the court's ultimate decision). After signing a TPLF Agreement with a third party to fund a federal antitrust lawsuit, Kraft required more funds and entered into an identical funding agreement with his sister, Mason. *Id.* at 681. Mason lent Kraft $100,000 in exchange for 20% of the first $1,000,000 awarded to Kraft in the lawsuit, 6% of the next $4,000,000 awarded, and 3% of any award thereafter. *Id.* Although Kraft's lawsuit ultimately settled for over $5,000,000, Mason received only $85,000 and initiated a suit against her brother to recover the remaining obligation. *Id.* at 681–82.

[51] *See id.* at 684 (citing Florida's precedential emphasis on the clear establishment of "corrupt intent" to find usurious conduct).

[52] *See id.* (referencing the comparatively definite nature of loan repayment). Note that the court's emphasis on the conditional nature of the loan's repayment reflects, albeit implicitly, the traditional doctrinal definition of a "loan," which requires an unqualified agreement from the borrower to repay the lender in the future. *See* 9 WILLISTON ON CONTRACTS § 20:18 (4th ed. 2001) (putting forth the traditional requirements for an instrument to be considered a loan).

[53] *See Kraft*, 668 So. 2d at 684 (noting, at the time the loan was made, any repayment was purely speculative).

[54] *See* Anglo-Dutch Petroleum Int'l, Inc. v. Haskell, 193 S.W.3d 87, 100 (Tex. App. 2006) (noting that, although usury cases were not new to the court, the specific application of the state's usury laws to litigation funding was a matter of first impression).

[55] *See id.* at 96–97 (concluding that the contingent nature of the TPLF agreement renders usury impossible on the part of lenders); *Kraft*, 668 So. 2d at 684 (same).

[56] *See Anglo-Dutch*, 193 S.W.3d at 90–91 (outlining the facts of the case).

unenforceable.[57] As in *Kraft*, the court in *Anglo-Dutch* also regarded as dispositive the contingent nature of the agreement, such that the known possibility that the third-party funders could receive no payment at all undercut any claims that the TPLF Agreement constituted a usurious loan.[58]

2. Usury as a Successful State-Level Challenge to TPLF Agreements

In 1991, in *Swindell v. Federal National Mortgage Association*, the Supreme Court of North Carolina defined usury consistent with the four contours noted above.[59] Per *Swindell's* definition, the state's usury laws applied only to loans or forborne collections of money owed.[60] In 2007, the North Carolina General Assembly broadened via statute the financial instruments to which the state's usury laws applied to include five categories of lending devices.[61] As amended in 2019, the statute restricts the interest charged on principal amounts less than $25,000 to the lesser of 16% or the U.S. Treasury's six-month rate on U.S. Treasury bills plus 6%.[62]

In 2008, in *Odell v. Legal Bucks, LLC*, the Court of Appeals of North Carolina confronted the question of how, if at all, the state's usury statute applied to a consumer TPLF Agreement.[63] The crux of the court's analysis focused on whether a consumer TPLF Agreement, although not a loan in the traditional sense, constituted an "advance" for the purposes of the statute.[64] Citing both to Black's Law Dictionary and a 1978 state case defining the term, the court in *Odell* concluded that, where an advance exists, the parties to the

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[57] *Id.* at 91.

[58] *See id.* at 96–98 (relying on the definition of "loan" used in the Texas Finance Code); TEX. FIN. CODE § 301.002(a)(10) (2021) (defining a loan as "an advance of money that is made to or on behalf of an obligor, the principal amount of which t*he obligor has an obligation to pay the creditor*") (emphasis added).

[59] *See* Swindell v. Fed. Nat'l Mortg. Ass'n, 409 S.E.2d 892, 895 (N.C. 1991) (defining usury as understood by North Carolina law); *see also supra* note 46 and accompanying text (setting out the four traditional elements of usury).

[60] *See Swindell*, 409 S.E.2d at 895 (defining the scope of the applicability of the state's usury laws).

[61] N.C. GEN. STAT. § 24-1.1 (2022). In addition to parties to loans, the statute broadened the application of North Carolina's usury laws to parties to a "purchase money loan, advance, commitment for a loan or forbearance other than a credit card, open-end, or similar loan." *Id.*

[62] *Id.* § 24-1.1(a)(1), (c).

[63] *See* Odell v. Legal Bucks, LLC, 665 S.E.2d 767, 776 (N.C. Ct. App. 2008) (considering the legality of a litigation funding agreement between Legal Bucks and a plaintiff in a personal injury lawsuit). Odell was injured in a motor-vehicle collision and expected to collect $30,000 from the defendant's personal injury lawsuit. *Id.* at 770. She received a $3,000 advance on this anticipated award from Legal Bucks. *Id.* The terms of the agreement required Odell to pay back at least $4,200 if she paid within three months of disbursement. *Id*. If she paid after the three-month period, she would be liable for the $4,200 amount plus 7.8% of the initial advance amount per month, up to a total charge of $9,750, or 325% of the advance amount. *Id*. at 770–71.

[64] *See id.* at 776 (determining the central question at issue in the case).

agreement possess an expectation of reimbursement rather than a right to repayment.[65] Therefore, although the TPLF provider was not contractually assured of repayment, its expectation of reimbursement from the plaintiff brought the consumer TPLF Agreement within the purview of North Carolina's usury statute.[66]

In 2015, in *Oasis Legal Finance Group, LLC v. Coffman*, the Colorado Supreme Court worked to define the appropriate intersection of consumer TPLF Agreements and the Uniform Commercial Code of Colorado (hereinafter "the UCCC").[67] In *Coffman*, two consumer TPLF providers, Oasis Legal Finance Group, LLC and Plaintiff Funding Holding, Inc. (d/b/a LawCash), sought judgment in an action against Colorado's Attorney General and UCCC Administrator declaring that their TPLF Agreements were not loans and thus not in violation of the state's usury statute.[68]

In 2010, an unrelated business entity requested an official opinion letter from the Administrator of the Colorado UCCC laying out any licensing requirements or regulations applicable to consumer TPLF providers operating in Colorado.[69] Drawing on a 2001 state court decision involving the legal status of a tax refund advance provider, the Administrator determined that a consumer TPLF provider would be engaging in transactions constituting consumer loans and would therefore be subject to the UCCC.[70] While researching the TPLF industry in Colorado and its legal status in response to the opinion letter request, the Administrator discovered the in-state operations of both Oasis and LawCash and opened an investigation into their practices.[71] When Oasis and LawCash were informed that their TPLF businesses were in violation of both the UCCC and the Colorado Consumer Protection Act, the TPLF providers declined the Administrator's offer of a non-judicial remedial process and filed

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[65] *Id.* at 777 (citing Louchheim, Eng & People v. Carson, 241 S.E.2d 401, 404 (N.C. Ct. App. 1978)).

[66] *See id.* (holding that the consumer TPLF Agreement was subject to regulation under North Carolina's usury statute).

[67] *See* Oasis Legal Fin. Grp., LLC v. Coffman, 361 P.3d 400, 401–02 (Colo. 2015) (laying out the scope of the legal question before the court). The Colorado Legislature adopted the Uniform Commercial Code on April 23, 1965, with effect taken on July 1, 1966. Dellas W. Lee, *Impact of the Uniform Commercial Code on Colorado Law*, 42 DENV. L. CTR. J. 67, 68 n.5 (1965). The Uniform Commercial Code was adopted by all fifty states, with some modifications on a state-by-state basis, between 1953 and 1973. See *Uniform Commercial Code*, UNIF. L. COMM'N (2022), https://www.uniformlaws.org/acts/ucc [https://perma.cc/E42Q-956J] (describing the history of the UCC).

[68] *See Coffman*, 361 P.3d at 401–02 (laying out the background of the case).

[69] *Id.* at 403–04.

[70] *Id.* In the case on which the Administrator drew, *State ex rel. Salazar v. The Cash Now Store*, the defendant provided individuals with an upfront lump-sum of money in exchange for an assignment of the federal or state tax refund amount owed to the individual but not yet received. *See* 31 P.3d 161, 163–64 (Colo. 2001) (providing the case's factual and procedural background).

[71] *Coffman*, 361 P.3d at 404–05.

suit.[72] In an opinion exploring the definition and requisite characteristics of "debt" for the purposes of the UCCC, the Colorado Supreme Court ultimately determined that Oasis and LawCash's TPLF Agreements were, in fact, loans and thus subject to the UCCC.[73]

C. Direct Regulation Via State Statute

Rather than apply common-law doctrines to TPLF Agreements, some states have adopted an assortment of regulatory statutes designed to combat abusive practices in the consumer sector.[74] Although the specific provisions vary widely, such statutes tend to incorporate elements of interest rate controls, mandatory disclosures, and entity registration requirements.[75] The consumer TPLF statutes of Arkansas, Maine, and West Virginia demonstrate the variety of terms these statutes may include.[76]

Under Arkansas' statute, consumer TPLF Agreements are subject to the same 17% interest rate cap applicable under the state's usury statute.[77] A TPLF provider must also treat any money paid by the consumer in excess of the TPLF amount he or she initially received as interest.[78] Additionally, the consumer must receive a written contract for the TPLF Agreement that "prominently disclose[s]" the applicable annual rate of interest.[79]

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[72] *Id.*

[73] *Id.* at 410; *see infra* notes 106–118 and accompanying text (examining the legal arguments underpinning the decision in *Coffman*).

[74] *See* U.S. GOV'T ACCOUNTABILITY OFF., GAO-23-105210, THIRD-PARTY LITIGATION FINANCING: MARKET CHARACTERISTICS, DATA, AND TRENDS 25–26 (2022) (describing the current landscape of state statutes targeted specifically at consumer TPLF Agreements).

[75] *See id.* at 45–46 (non-exhaustively listing existing state regulatory statutes and their key terms).

[76] ARK. CODE ANN. § 4-57-109 (2020); ME. STAT. tit. 9-A, § 12 (2022); W. VA. CODE § 46A-6N (2022). Several other states, including Indiana, Nebraska, Nevada, Ohio, Oklahoma, Tennessee, and Vermont, have statutes that specifically address consumer TPLF providers and the contracts by which their agreements are defined. *See, e.g.*, IND. CODE §§ 24-12-1 to -4.5 (2022) (laying out the state's statutory regulations for consumer TPLF Agreements); NEB. REV. STAT. §§ 25-3301 to -3309 (2022) (same); NEV. REV. STAT. § 604C (2021–2022) (same); OHIO REV. CODE ANN. § 1349.55 (2022) (same); OKLA. STAT. tit. 14A, §§ 3-80 to -817 (2022) (same); TENN. CODE ANN. § 47-16 (2021) (same); VT. STAT. ANN. tit. 8, §§ 2251–2260 (2021) (same).

[77] *See* ARK. CODE. ANN. § 4-57-109(b)(1) (incorporating Arkansas' usury statute by reference). Rather than laying out a specific maximum interest rate in the statutory language, Arkansas' usury statute incorporates the 17% maximum interest rate set out in Amendment 89 to the Arkansas Constitution. *See id.* § 4-57-104 (setting the maximum permissible interest rate at that which is required under the constitutional amendment); ARK. CONST. amend. 89, Sections 1–3 (setting the maximum permissible rate on loans at 17%, other than for loans issued by the government or depository institutions that are federally insured).

[78] ARK. CODE. ANN. § 4-57-109(b)(2).

[79] *Id.* § 4-57-109(c). More specifically, the statute requires the TPLF provider to include the annual percentage interest rate in "bold, 20-point type and Arial font surrounded by a black rectangle border of line weight one point five . . . ." *Id.*

Maine's TPLF statute requires consumer TPLF providers to formally register with the state, provide specific disclosures, and comply with fee structure requirements.[80] As to disclosures, consumer TPLF providers must attach a standard form to each funding contract, which includes the semiannually compounded annual percentage fee on the funded amount and the total amount for which the consumer will have repayment responsibility in specified intervals.[81] As to fee structures, Maine's TPLF statute bars TPLF providers from assessing fees for more than forty-two months from the contract date, compounding fees on a less than semiannual basis, or calculating the applicable interest rate on amounts never actually received by the consumer.[82]

In West Virginia, consumer TPLF providers are statutorily subject to registration requirements, maximum chargeable interest rates, and consumer disclosure requirements.[83] Like Maine's statute, West Virginia's consumer TPLF statute mandates that funding contracts disclose in an intervallic fashion the total amount owed by the consumer, inclusive of all charges and fees, and bars providers from assessing fees beyond a forty-two month period.[84] Rather than incorporating a separate usury statute, West Virginia's TPLF statute explicitly applies an 18% maximum chargeable interest rate to all consumer TPLF Agreements.[85] Notably, the statute also requires the recipient of funds from a consumer TPLF Agreement to disclose any such Agreement to other parties to the litigation, regardless of whether or not it is subject to a formal discovery request.[86]

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[80] ME. STAT. tit. 9-A, §§ 12-104, -105, -106 (2022).

[81] *Id.* § 12-104. The total amount for which the consumer is responsible must be broken out in six-month intervals. *Id.*

[82] *Id.* § 12-105.

[83] W. VA. CODE § 46A-6N (2022).

[84] *Id.* §§ 46A-6N-5, -9; *see supra* notes 80–82 and accompanying text (describing Maine's statutory requirements for consumer TPLF Agreements).

[85] *See* W. VA. CODE § 46A-6N-9(a) (prohibiting a TPLF provider from charging an annual fee greater than 18% of the amount of money originally advanced); *supra* note 77 and accompanying text (discussing Arkansas' 17% interest rate cap on consumer TPLF Agreements).

[86] W. VA. CODE § 46A-6N-6. Although it is beyond the scope of this Note, whether parties receiving funds from TPLF Agreements must disclose such arrangements to other parties or to the court handling the dispute has emerged as a corollary to the debate over TPLF regulation. *See, e.g.*, Nimitz Techs. LLC v. CNET Media, Inc., No. CV 21-1247-CFC, 2022 WL 17338396, at *1–2 (D. Del. Nov. 30, 2022) (expressing Judge Colm F. Connolly's defense of his authority to order litigants to produce evidence disclosing the involvement of specific TPLF providers in their various patent lawsuits); *see also* Alison Frankel, *Delaware Judge Justifies Litigation Funding 'Inquisition' in Thriller Order*, REUTERS (Dec. 2, 2022), https://www.reuters.com/legal/government/delaware-judge-justifies-litigation-funding-inquisition-thriller-order-2022-12-02/ [https://perma.cc/7M3G-LGWF] (describing the timeline and background of the evidence production orders at issue in *Nimitz*); *In re* Nimitz Techs. LLC, No. 2023-103, 2022 WL 17494845, at *1 (Fed. Cir. Dec. 8, 2022) (denying the plaintiff's writ of mandamus petition seeking to vacate the United States District Court for the District of Delaware's evidence production order as to the plaintiff's possible TPLF arrangements).

D. Federal Securities Regulation: The Howey Test

Although TPLF Agreements have been scrutinized by federal legislators and judges, there is currently no direct federal regulation of TPLF.[87] In 2021, for example, several members of Congress proposed legislation mandating the disclosure of underlying TPLF Agreements in certain types of federal cases.[88] Similarly, in 2022, legal advocacy groups sought revision of Federal Rule of Civil Procedure 16(c)(2) to provide a basis on which judges could more readily probe the financial involvement of TPLF providers.[89] Such initiatives, however, have failed to launch.[90]

Some scholarship suggests that TPLF Agreements, by virtue of their terms and structure, may come under the regulatory purview of the Securities Act of 1933 and Securities Exchange Act of 1934, which regulate transactions

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[87] *See* Austin T. Popp, Note, *Federal Regulation of Third-Party Litigation Finance*, 72 VAND. L. REV. 727, 730 (2019) (advocating for a federal regulatory system for TPLF under the purview of the Consumer Financial Protection Bureau); *infra* notes 88–90 and accompanying text (describing attempts to regulate TPLF through federal legislation and changes to the Federal Rules of Civil Procedure). *See generally* Consumer Fin. Prot. Bureau v. RD Legal Funding, LLC, 332 F. Supp. 3d 729, 745–46 (S.D.N.Y.)*, amended*, No. 17-CV-890, 2018 WL 11219167 (S.D.N.Y. Sept. 12, 2018*), vacated and remanded*, 828 F. App'x 68 (2d Cir. 2020), and *aff'd in part, rev'd in part and remanded*, 828 F. App'x 68 (2d Cir. 2020) (describing the suit through which the Consumer Financial Protection Bureau and New York Attorney General jointly sued two TPLF providers for alleged violations of the Consumer Financial Protection Act and New York law).

[88] Litigation Funding Transparency Act of 2021, S.840, 117th Cong. § 28 (2021). In 2021, Senator Chuck Grassley reintroduced the Litigation Funding Transparency Act, which would require plaintiffs in federal civil class actions or multi-district actions to disclose any TPLF Agreements into which they have entered. *Id.*; *see also* Litigation Funding Transparency Act of 2021, H.R.2025, 117th Cong. § 28 (2021) (introducing an identical bill, sponsored by Representative Darrell Issa, in the House of Representatives). The proposed Act was referred to the Senate Committee on the Judiciary and to the House of Representatives' Subcommittee on Courts, Intellectual Property, and the Internet, but no further action has been taken to date. *See All Actions: S.840—117th Congress (2021–2022)*, LIBR. OF CONG., https://www.congress.gov/bill/117th-congress/senate-bill/840/all-actions?overview=closed#tabs [https://perma.cc/SDV8-EGQB] (Mar. 18, 2021) (tracking actions taken on the proposed Act since its introduction); *All Actions: H.R.2025—117th Congress (2021-2022)*, LIBR. OF CONG., https://www.congress.gov/bill/117th-congress/house-bill/2025/all-actions?overview=closed#tabs [https://perma.cc/4JKW-XRR8] (Oct. 19, 2021) (same).

[89] Laws. for Civ. Just. & U.S. Chamber of Com. Inst. for Legal Reform, Rules Suggestion to the Advisory Committee on Civil Rules: An Important but Rarely Asked Question: Amending Rule 16(c)(2) to Prompt Judges to Consider Inquiring About Financial Interests Created by Third-Party Litigation Funding (Sept. 8, 2022), https://www.uscourts.gov/sites/default/files/22-cv-m_suggestion_from_lcj_and_ilr_-_rule_16c2_0.pdf [https://perma.cc/BN9Y-JGKK]. In 2022, Lawyers for Civil Justice and the United States Chamber of Commerce Institute for Legal Reform submitted a Rules Suggestion to the Judicial Conference's Advisory Committee on Civil Rules proposing that Federal Rule of Civil Procedure 16(c)(2) be amended to "prompt judges to consider inquiring about financial interests created by third-party litigation funding." *See id.*

[90] *See, e.g.*, FED. R. CIV. P. 16(c)(2) (as amended through September 2023, but including none of the proposed language regarding TPLF); *All Actions: S.840—117th Congress (2021-2022)* (showing no additional action on the Senate version of the Litigation Funding Transparency Act of 2021); *All Actions: H.R.2025—117th Congress (2021-2022)* (showing no additional action on the House version of the Act).

involving financial instruments and investments.[91] Both the Securities Act of 1933 (hereinafter "the 1933 Act") and Securities Exchange Act of 1934 (hereinafter "the 1934 Act") define a "security" in broad terms, including as an "investment contract."[92]

In 1946, in *SEC v. W. J. Howey Company*, the Supreme Court first examined the meaning of the term "investment contract" as contemplated by the 1933 Act.[93] In *Howey*, the SEC alleged that a Florida company's sale of orange groves and associated service contracts violated the 1933 Act as sales of unregistered securities.[94] Unlike the lower courts involved in the case, the Court held that the agreements at issue in *Howey* qualified as "investment contracts" for the purposes of the 1933 Act.[95]

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[91] Securities Exchange Act of 1934, 15 U.S.C. §§ 78a–78rr; Securities Act of 1933, 15 U.S.C. §§ 77a–77mm; *see* Couture, *supra* note 20, at 8, 16, 18 (analyzing terms of TPLF Agreements relative to existing securities law jurisprudence and suggesting that TPLF Agreements could be subject to regulation under the Securities Act of 1933 and the Securities Exchange Act of 1934). In an address to Congress in March 1933, President Franklin D. Roosevelt, drawing largely on the financial regulatory approach for which Supreme Court Justice Louis Brandeis advocated in his collection of essays on the topic, called on Congress to produce disclosure-driven legislation allowing the federal government to supervise investment securities in interstate commerce. Elizabeth Keller & Gregory A. Gehlmann, *Introductory Comment: A Historical Introduction to the Securities Act of 1933 and the Securities Exchange Act of 1934*, 49 OHIO ST. L.J. 329, 338–39 (1988). President Roosevelt, after rejecting an initial draft of the regulation authored by a former Federal Trade Commission chairman, assembled his own three-member drafting team, which drew on both existing state securities regulations and the United Kingdom's English Companies Act to produce draft legislation that was ultimately presented to a House of Representatives subcommittee. *Id.* at 339–42. Taken together, the Securities Act of 1933 and the Securities Exchange Act of 1934 require various disclosures to investors when securities are sold to the public, bar fraudulent activity in securities sales, regulate conduct in securities markets, and grant the Securities and Exchange Commission wide-reaching authority over the securities industry. *See Investor Bulletin: An Introduction to the U.S. Securities and Exchange Commission—Rulemaking and Laws*, SEC (Aug. 20, 2015), https://www.sec.gov/oiea/investor-alerts-and-bulletins/ib_rulemaking [https://perma.cc/Y32V-HZUF] (outlining the functions and core provisions of the major federal laws under which the securities industry is regulated).

[92] *See* 15 U.S.C. § 77b(a)(1) (including "investment contract" in the definition of "security" for the purposes of the Securities Act of 1933) (hereinafter "the 1933 Act"); 15 U.S.C. § 78c(a)(10) (including "investment contract" in the definition of "security" for the purposes of the Securities Exchange Act of 1934) (hereinafter "the 1934 Act").

[93] *See* SEC v. W.J. Howey Co., 328 U.S. 293, 297–98 (1946) (noting the term "investment contract," although part of the statutory definition of "security," was itself undefined within the statute and in associated legislative reporting). *See generally* Stephen G. Christianson, Annotation, *What Is "Investment Contract" Within Meaning of § 2(1) of Securities Act of 1933 (15 U.S.C.A. § 77b(1)) and § 3(a)(10) of Securities Exchange Act of 1934 (15 U.S.C.A. § 78c(a)(10)), Both Defining Term "Security" as Including Investment Contract*, 134 A.L.R. Fed. 289 (1996) (tracing the history of the term "investment contract" through federal court decisions).

[94] *Howey*, 328 U.S. at 294. The company, which owned both a hotel and orange groves adjacent to it, sold its hotel guests small tracts of land in the groves and, under a separate contract, provided for the management, harvesting, and profit-sharing from the sale of oranges grown in them. *Id.* at 294–97. Given the small size of each individual tract, the company pooled the oranges across purchasers' various tracts for eventual sale. *Id.* at 295–96. The company represented to purchasers that they could expect a 10% annual return over ten years. *Id.* at 296.

[95] *Id.* at 299, 301.

In arriving at its holding, the Court established what is now known as the *Howey* Test to determine whether an agreement or transaction is an "investment contract" falling under the purview of the 1933 Act.[96] To satisfy the *Howey* Test, the agreement or transaction must involve: (1) a money investment; (2) "in a common enterprise"; (3) with profits expected "solely" from others' efforts.[97] In 1967, in *Tcherepnin v. Knight*, the Supreme Court determined that the *Howey* Test was also the standard by which an "investment contract" should be defined for the purposes of the 1934 Act.[98] Each element of the *Howey* Test has been further refined by federal courts in the over seventy-five years since *Howey* was decided.[99] When an agreement is an "investment contract" under the *Howey* Test, the agreement and the parties to it are subject to the SEC's regulatory and enforcement authority under federal securities law.[100] The SEC, in turn, is able to leverage its statutory powers to protect everyday individuals on whose investments American markets rely.[101]

II. The Consumer TPLF Agreement: A Loan by Any Other Name?

Debate over the appropriate approach to regulating consumer TPLF Agreements belies a critical antecedent question: what is the appropriate legal characterization of a consumer TPLF Agreement?[102] Section A of this Part describes the characterization of consumer TPLF Agreements as loans through the lens of usury claims.[103] Section B describes the characterization of con-

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[96] *Id.* at 294, 301.

[97] *Id.* at 301. The *Howey* Test is sometimes characterized as a three-prong test, as described above, and sometimes characterized as a four-prong test, in which the expectation of profits and the source of their derivation are treated as two separate prongs. *Compare*, *e.g.*, Luzerne Cnty. Ret. Bd. v. Makowski, 627 F. Supp. 2d 506, 555 (M.D. Pa. 2007) (using the three-prong construction of the *Howey* Test), *with* Manchester Bank v. Conn. Bank & Tr., 497 F. Supp. 1304, 1311–12 (D.N.H. 1980) (using the four-prong construction of the *Howey* Test).

[98] Tcherepnin v. Knight, 389 U.S. 332, 337–38 (1967). In *Tcherepnin*, a group of petitioners held capital shares with withdrawal rights in a Chicago-based savings and loan association. *Id.* at 333. The petitioner filed suit against the association, alleging that such shares were securities for the purposes of the 1934 Act and, in violation of the Act, were sold via mail solicitations containing misleading and false statements. *Id.* at 333–34.

[99] *See* Jennifer Carlucci, *Litigation Funding Devices for Franchisees: Are They Securities?*, 25 HOFSTRA L. REV. 353, 365–69 (1996) (discussing judicial sub-tests that have emerged for each of the elements of the *Howey* Test); *infra* notes 120–161 and accompanying text (same).

[100] *See* Couture, *supra* note 20, at 9 (noting that the scope of federal securities law encompasses investment contracts).

[101] *See, e.g.*, SEC, STRATEGIC PLAN FISCAL YEARS 2022–2026, at 6 (2022), https://www.sec.gov/files/sec_strategic_plan_fy22-fy26.pdf [https://perma.cc/TV2B-3A85] (listing the SEC's first strategic goal for fiscal years 2022 through 2026 as protection of the "investing public" from various forms of financial misconduct).

[102] *See supra* notes 31–86 and accompanying text (describing various attempts to categorize and regulate TPLF Agreements).

[103] *See infra* notes 105–119 and accompanying text.

sumer TPLF Agreements as "investment contracts" through the lens of the *Howey* Test.[104]

A. TPLF Agreements as Loans

Cases in which consumer TPLF Agreements have been challenged on usury grounds, such as the aforementioned *Oasis Legal Finance Group, LLC v. Coffman* out of Colorado, provide insight into the legal treatment of such agreements as loans.[105] In *Coffman*, two consumer TPLF providers doing business in Colorado sought a declaratory judgment that their TPLF Agreements did not constitute loans for the purposes of regulation under the Uniform Commercial Code of Colorado (UCCC).[106]

In considering the character of the TPLF Agreements at issue in *Coffman*, the Colorado Supreme Court examined three dimensions inherent to the definition of a consumer loan falling under the purview of the UCCC: (1) the meaning of "debt" as that term was used in the UCCC; (2) the function of the relevant repayment requirement; and (3) the growth of the amount owed over time under the arrangement.[107]

Although the UCCC defines a loan in a variety of ways, the Colorado Supreme Court found the "creation of debt" to be the most salient to the question of TPLFs.[108] As the term "debt" is not defined in the UCCC, the court drew on various external sources of law to read a basic definition into the UCCC: "an obligation to repay."[109] With this definition as the standard, the court concluded that the TPLF Agreements provided by Oasis and LawCash constituted debt—a necessary, but not sufficient, condition for the TPLF Agreements to be considered "loans" for the purposes of the UCCC.[110]

Next, the court in *Coffman* determined that, for the purposes of the UCCC, the recourse versus nonrecourse nature of the debt is immaterial.[111] To do so, the court relied on a fusion of statutory interpretation and a practical assessment of Oasis and LegalBucks' business models.[112] As a matter of statu-

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[104] *See infra* notes 120–181 and accompanying text.

[105] *See supra* notes 45–73 and accompanying text (defining usury and detailing various state cases in which consumer TPLF Agreements have been challenged on state usury law grounds).

[106] *See* Oasis Legal Fin. Grp., LLC v. Coffman, 361 P.3d 400, 401–02 (Colo. 2015) (reviewing the factual background of the case).

[107] *See id.* at 407–10 (mapping out the contours of the court's analysis).

[108] *See id.* at 407 (comparing the UCCC's loan definitions); *see, e.g.*, COLO. REV. STAT. § 5-1-301(25)(a)(I)–(IV) (2018) (listing the UCCC's four definitions of the term "loan").

[109] *See Coffman*, 361 P.3d at 407 (synthesizing definitions of "debt" from *Black's Law Dictionary*, the Colorado Fair Debt Collections Practices Act, the Federal Bankruptcy Code, and the Colorado Uniform Fraudulent Transfer Act).

[110] *See id.* at 406, 408–09 (noting forms of debt exist to which the UCCC's loan regulations explicitly do not apply, such as consumer credit sales).

[111] *See id.* at 409 (rejecting plaintiffs' argument).

[112] *See id.* (same).

tory construction, the court declined to read a recourse requirement into the UCCC's loan definition because modifiers to the word "debt" were absent from its text.[113] Second, the court found that, although the funds disbursed to individual litigants by Oasis and LegalBucks were nominally nonrecourse, their collections activities were not meaningfully impacted by this legal status.[114]

Finally, the *Coffman* court concluded that the growth of the amount owed to the TPLF providers via pre-determined finance charges, rather than according to changes in market conditions, solidified the TPLF Agreements' status as loans.[115] Colorado's UCCC, as noted by the court, explicitly states that a consumer loan for the purposes of the UCCC features finance charges, including interest payments.[116] Here, the TPLF providers charged consumers regular fees at pre-determined fixed rates on the amounts advanced, with the total amount paid to the TPLF providers directly tied to the length of time for which the advances were outstanding.[117] Although not referred to as such by either company, in the eyes of the court such fees were plainly a mechanism to charge and collect interest.[118] The logical path connecting consumer TPLF Agreements and usury prohibitions in *Coffman* typifies the underlying rationale for TPLF regulation via state usury laws.[119]

B. TPLF Agreements as Investment Contracts Under the Howey Test

As described above, an "investment contract" for the purposes of the 1933 and 1934 Acts must satisfy the three elements set out by the Supreme Court's *Howey* Test: (1) a money investment; (2) "in a common enterprise"; (3) with profits expected "solely" from others' efforts.[120]

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[113] *See id.* (expressing discomfort with reading a recourse requirement into the plain language of the definition); COLO. REV. STAT. § 5-1-301(25)(a)(I) (defining a loan as "the creation of debt by the lender's payment of or agreement to pay money to the consumer or to a third party for the account of the consumer").

[114] *See Coffman*, 361 P.3d at 408 (reviewing the TPLF providers' collection mechanisms and typical collection rate). As noted by the Colorado Supreme Court, the plaintiffs in *Coffman* collected in full on 85% of funded cases. *Id.*

[115] *See id.* at 409–10 (discussing the interest charges on the litigation advances collected by both Oasis and LawCash).

[116] *See id.* at 410 (describing the way in which the payment obligation grew over time). The UCCC, in relevant part, defines a "finance charge" as "interest or any amount payable under a point, discount, or other system of charges, however denominated." COLO. REV. STAT. § 5-1-301(20)(a)(I).

[117] *See Coffman*, 361 P.3d at 408, 410 (describing the fee mechanisms of the TPLF providers).

[118] *See id.* at 410 (emphasizing the character of the fees). Oasis referred to these charges as a "multiplier," while LawCash referred to them as "monthly use fee[s]." *Id.*

[119] *See supra* notes 45–73 and accompanying text (discussing the application of state usury laws to consumer TPLF Agreements and noting decisions in sample cases from several jurisdictions).

[120] *See* SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946) (laying out the Supreme Court's test for an "investment contract" under the 1933 Act); Tcherepnin v. Knight, 389 U.S. 332, 338 (1967) (determining that the *Howey* Test is also the appropriate standard for defining an "investment contract" under the 1934 Act).

Subsections 1[121], 2[122], and 3[123] of this Section apply each of the *Howey* Test's three prongs to consumer TPLF Agreements, with the TPLF provider assuming the role of the investor and the TPLF fund recipient as the investee. Subsection 4 describes the enforcement role of the 1934 Act's Section 10(b) and its associated regulatory rule, Rule 10b-5.[124] Subsection 5 examines the complementary public policy goals of both the *Howey* Test and consumer TPLF more broadly.[125]

1. A Money Investment

Under the *Howey* Test, an "investment contract" necessarily involves a money investment.[126] In practice, courts have eschewed a textual reading of *Howey*'s call for an "investment of money."[127] Instead, courts have embraced a broader definition of the term "money," such that the presence of an "exchange of value" through which investors expose themselves to financial risk satisfies this first prong of the *Howey* Test.[128]

In a typical consumer TPLF Agreement structure, a TPLF provider gives an agreed-upon amount of money to a consumer litigant.[129] In return, the litigant promises a portion of his or her ultimate monetary recovery to the provider, plus any agreed-upon fees or accumulated interest charges.[130] Such agreements are structured as nonrecourse, such that the TPLF provider risks losing any funds provided to the litigant and any associated fees or interest if the litigant's suit is unsuccessful.[131] Under existing precedent, then, such an agree-

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[121] *See infra* notes 126–132 and accompanying text.

[122] *See infra* notes 133–150 and accompanying text.

[123] *See infra* notes 151–161 and accompanying text.

[124] *See infra* notes 162–166 and accompanying text.

[125] *See infra* notes 167–181 and accompanying text.

[126] *See* SEC. v. W.J. Howey Co., 328 U.S. 293, 301 (1946) (providing the Supreme Court's test for an "investment contract" under the 1933 Act).

[127] *Compare id.* (referring to an "investment of money" in its definition of an "investment contract"), *with, e.g.*, Int'l Bhd. of Teamsters v. Daniel, 439 U.S. 551, 560 n.12 (1979) (noting that the *Howey* Test's first prong does not require cash-only investments); Uselton v. Com. Lovelace Motor Freight, Inc., 940 F.2d 564, 574 (10th Cir. 1991) (holding that an employee's voluntary surrender of wages to obtain an interest in a stock plan for employees satisfied *Howey's* "investment of money" requirement); Hocking v. Dubois, 885 F.2d 1449, 1471 (9th Cir. 1989) (finding the *Howey* Test's first prong to be satisfied when an individual chose to commit the condominium he owned to a rental pool with other condominium owners).

[128] *See* Michael Mendelson, *From Initial Coin Offerings to Security Tokens: A U.S. Federal Securities Law Analysis*, 22 STAN. TECH. L. REV. 52, 73–74 (2019) (discussing the expansion of *Howey*'s "investment of money" prong through federal case law); Carlucci, *supra* note 99, at 365–66 (same).

[129] *See* Avraham & Sebok, *supra* note 20, at 1135 (describing the basic mechanics of a consumer TPLF Agreement); Couture, *supra* note 20, at 6 (same).

[130] *See* Avraham & Sebok, *supra* note 20, at 1135 (describing the basic mechanics of a consumer TPLF Agreement); Couture, *supra* note 20, at 6 (same).

[131] *See* POPOLIZIO, *supra* note 26 (describing the basic TPLF Agreement's structure in the United States, including such an Agreement's nonrecourse nature).

ment involves an "exchange of value" in the form of actual money and exposes the TPLF provider to the risk of financial loss, in satisfaction of the *Howey* Test's first prong.[132]

2. "In a Common Enterprise"

The second prong of the *Howey* Test requires that the money investment is made "in a common enterprise."[133] The Supreme Court in *Howey* declined to define a "common enterprise," leading to the development of two different standards across federal circuit courts: horizontal commonality and vertical commonality.[134] Among courts who recognize vertical commonality, there is a further subdivision between broad vertical commonality and narrow vertical commonality.[135]

The Third, Sixth, and Seventh Circuits require, and the First, Second, Fourth, Ninth, and D.C. Circuit Courts of Appeals recognize, horizontal commonality to satisfy the *Howey* Test's "common enterprise" prong.[136] Horizontal commonality is present when investors' contributions are pooled, such that the success or failure of the individual investor is tied to the success or failure of the overall undertaking.[137] As a threshold matter, the lack of contribution pooling would preclude TPLF Agreements from satisfying the "common enterprise" interpretation in a horizontal commonality jurisdiction.[138] By definition, TPLF Agreements—at least in the consumer context—involve a one-to-one relationship between a TPLF provider and an individual litigant.[139]

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[132] *See* Mendelson, *supra* note 128, at 73–74 (referring to the flexible, broader approach to "investment of money" generally embraced by federal courts when applying the *Howey* Test); Carlucci, *supra* note 99, at 365–66 (same).

[133] *See* SEC. v. W.J. Howey Co., 328 U.S. 293, 301 (1946) (listing the elements of an "investment contract" for the purposes of the 1933 Act).

[134] *See id.* (declining to provide further explanation of "common enterprise" as used in the *Howey* Test); *see also* James D. Gordon III, *Defining a Common Enterprise in Investment Contracts*, 72 OHIO ST. L.J. 59, 66–67 (2011) (explaining the development of the horizontal and vertical commonality concept under *Howey* and the ensuing circuit split).

[135] *See* Couture, *supra* note 20, at 12 (summarizing the three commonality approaches under which a potential "investment contract" may be analyzed for the purposes of the *Howey* Test).

[136] *See* Gordon III, *supra* note 134, at 68–69 (listing the approaches taken by each federal circuit for the *Howey* Test's commonality requirement).

[137] *See, e.g.*, SEC v. Infinity Grp. Co., 212 F.3d 180, 187–88 (3d Cir. 2000) (describing horizontal commonality as present where investors' contributions are pooled and losses and profits are distributed based on investors' pro rata contribution share); Wals v. Fox Hills Dev. Corp., 24 F.3d 1016, 1018–19 (7th Cir. 1994) (declining to find horizontal commonality where agreements for the rental and purchase of condo time-sharing involved pooling of weeks of rental time but not profit pooling from such rentals); Revak v. SEC Realty Corp., 18 F.3d 81, 88 (2d Cir. 1994) (rejecting vertical commonality and declining to find horizontal commonality where the rents and costs associated with investment condominium properties were not pooled or shared among owners of the units).

[138] *See* Couture, *supra* note 20, at 12 (arguing that TPLF Agreements do not satisfy horizontal commonality because the TPLF provider is the sole investor in such arrangements).

[139] *See id.* (same).

Both broad and narrow vertical commonality emphasize the relationship between the investor and the manager of that investment, albeit with different foci.[140] Although the First, Fourth, and D.C. Circuits have not ruled on vertical commonality generally, the Fifth and Eleventh Circuits recognize broad vertical commonality for the purposes of the *Howey* Test.[141] Only the Ninth Circuit explicitly recognizes narrow vertical commonality at this time, although not all Circuits have explicitly ruled on it.[142]

To satisfy broad vertical commonality, the investor's profit or loss must depend on the effectiveness of the manager's actions or decisions with respect to the funds.[143] In the context of consumer TPLF Agreements, broad vertical commonality is likely satisfied given that the investor—the TPLF provider—is dependent upon the actions and decisions of the individual litigant's lawyer in each lawsuit for which the provider has advanced funds.[144] To satisfy narrow vertical commonality, the investor's profits and the manager's profits must move together.[145] This interpretation of vertical commonality is likely also satisfied by a consumer TPLF Agreement, as the TPLF provider receives a return

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[140] *See* Gordon, *supra* note 134, at 67 (defining broad and narrow vertical commonality in the context of the *Howey* Test); Couture, *supra* note 20, at 12–13 (considering the application of broad and narrow vertical commonality to the typical TPLF Agreement structure).

[141] *See* Gordon, *supra* note 134, at 68–69 (listing the approaches taken in each federal circuit to the *Howey* Test's commonality requirement).

[142] *See id.* (same). The Eighth Circuit is conspicuously absent from this categorization of the federal appellate courts by their commonality approach, as the Eighth Circuit has not addressed whether the horizontal commonality standard, vertical commonality standard, or some combination thereof controls. *See* Andrew v. BLH Dev. Co., LLC, No. 12-3081-CV-S-DW, 2013 WL 12146382, at *2 (W.D. Mo. Aug. 23, 2013) (explaining that the Eighth Circuit has yet to rule on this issue); De Wit v. Firstar Corp., 879 F. Supp. 947, 979-80 (N.D. Iowa), *on reconsideration*, 904 F. Supp. 1476 (N.D. Iowa 1995) (also noting the Eighth Circuit's "long silence" on the issue, but ultimately opting for horizontal commonality in its decision-making).

[143] *See* Gordon, *supra* note 134, at 176 (describing the requirements for a finding of broad vertical commonality); *see also* Eberhardt v. Waters, 901 F.2d 1578, 1580–81 (11th Cir. 1990) (quoting Villeneuve v. Advanced Bus. Concepts Corp., 698 F.2d 1121, 1124 (11th Cir. 1983)) (describing the common enterprise as defined by the Eleventh Circuit as an arrangement in which the "fortunes of the investor are interwoven with and dependent upon the efforts and success of those seeking the investment or of third parties"); Long v. Schultz Cattle Co., 881 F.2d 129, 140 (5th Cir. 1989) (rejecting horizontal commonality and stating that the Fifth Circuit looks to investors' dependence on the expertise of the investment's promoter to determine whether the "common enterprise" prong is satisfied).

[144] *See* Couture, *supra* note 20, at 12 (noting that most TPLF providers, at least in the consumer context, refrain from exercising material control over a client's litigation, largely to avoid conflicts of interest that may cause the client's attorney to withdraw from representation).

[145] *See, e.g.*, SEC v. Eurobond Exch., Ltd., 13 F.3d 1334, 1340 (9th Cir. 1994) (finding narrow vertical commonality where the defendant and its investors shared in the profits and default risk of foreign currency loans); Brodt v. Bache & Co., 595 F.2d 459, 461–62 (9th Cir. 1978) (declining to find satisfaction of the *Howey* Test's "common enterprise" prong where the appellee provided investment counsel on a commission basis).

on its funded amounts and any associated fees or interest charges only if the individual litigant also receives a monetary award from his or her lawsuit.[146]

The Tenth Circuit, as an outlier, looks to the "economic reality" of a given agreement or contract to determine whether the *Howey* Test's second prong is satisfied.[147] In 1985, in *McGill v. American Land Exploration Company*, the Tenth Circuit differentiated between "purely commercial" transactions, which do not give rise to a "common enterprise," and transactions that are "in reality an investment."[148] While it is perhaps difficult to conform the Tenth Circuit's standard to a typical consumer TPLF Agreement, the flexibility inherent to the Tenth Circuit's approach is reflected in the SEC's approach to the *Howey* Test's second prong.[149] Neither vertical nor horizontal commonality are absolute requirements in the Commission's understanding of the *Howey* Test.[150]

3. Profits Expected "Solely" from Others' Efforts

The third prong of the *Howey* Test requires that the investor expects profits "solely" from others' efforts.[151] In 1973, in *SEC v. Glenn W. Turner Enterprises, Inc.*, the Ninth Circuit rejected a textualist reading of the term "solely" from the *Howey* Test.[152] Instead, the Ninth Circuit relied on a functional interpretation of the term "solely," in which the third prong would be satisfied

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[146] *See* Couture, *supra* note 20, at 12–13 (opining that the nonrecourse nature of TPLF Agreements, such that the TPLF provider is paid only if the litigant receives a monetary award from his or her litigation, likely satisfies narrow vertical commonality).

[147] *See* Gordon, *supra* note 134, at 68–69 (noting that the Tenth Circuit uses an idiosyncratic approach to the *Howey* Test's "common enterprise" prong).

[148] *See* 776 F.2d 923, 924–25 (10th Cir. 1985) (rejecting the lower court's application of horizontal commonality). Per the Court, when a transaction is "in reality an investment," it is "of a type in which stock is often given" in the course of such transactions. *Id.* at 925. In reaching its "economic reality" standard, the Tenth Circuit drew on the policy views expressed by the Supreme Court in both *Howey* and in *Tcherepnin v. Knight*. *See id.* (tracing both the term "economic reality" and the definition given to it by the Tenth Circuit to the Court's opinions in these cases). *See generally* Tcherepnin v. Knight, 389 U.S. 332 (1967); SEC v. W. J. Howey Co., 328 U.S. 293 (1946).

[149] *See McGill*, 776 F.2d at 925 (observing the rigidity inherent to horizontal commonality); *see also* Strategic Hub for Innovation and Financial Technology, *Framework for "Investment Contract" Analysis of Digital Assets*, SEC (Apr. 3, 2019), https://www.sec.gov/corpfin/framework-investment-contract-analysis-digital-assets [https://perma.cc/45LM-KA2G] (discussing in a footnote the Commission's approach to the *Howey* Test's "common enterprise" requirement).

[150] *See* Strategic Hub for Innovation and Financial Technology, *supra* note 149 (noting the SEC's lack of an essential requirement for horizontal or vertical commonality under the *Howey* Test); *Barkate*, 57 S.E.C. 488, 496 n.13 (2004) (expressing the Commission's disagreement with the concept that *Howey* requires a "common enterprise" to find an investment contract).

[151] *See* SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946) (listing the elements of an "investment contract" for the purposes of the Securities Act of 1933).

[152] *See* SEC v. Glenn W. Turner Enters., 474 F.2d 476, 482–83 (9th Cir. 1973) (expressing concern that a literal reading of "solely" as applied to the *Howey* Test would lead to mechanical determinations of what is or is not a security for the purposes of federal securities regulation, contrary to the policy views expressed in *Howey*).

where decisions of non-investors are the "undeniably significant ones" that influence the realization of profit or losses from the enterprise.[153] In 1975, in *United Housing Foundation, Inc. v. Forman*, the Supreme Court took notice of the Ninth Circuit's reading of "solely" for the purposes of the *Howey* Test but declined to express a view as to *Forman*'s holding.[154] Still, other federal circuit courts have explicitly applied the Ninth Circuit's functional approach.[155]

Particularly in the consumer context, TPLF providers frequently disclaim any role in an individual litigants' lawsuit beyond that of the monetary advance.[156] Moreover, TPLF providers must provide funding within the limits of applicable attorney conduct rules, including those requiring a TPLF client's attorney to maintain professional independence.[157] Taken together, the ostensibly limited role of the consumer TPLF provider allows the litigant's attorney to take the "undeniably significant" actions and decisions that will dictate the monetary success of the funded lawsuit.[158]

As to the expectation of profits more generally, in 2004, in *SEC v. Edwards*, the Supreme Court determined that an investment contract may involve promises of variable or fixed returns.[159] From the perspective of the consumer

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[153] *See id.* (setting out the Ninth Circuit's test for the third prong of the *Howey* Test with respect to the "solely" language in Court's opinion).

[154] *See* 421 U.S. 837, 869 n.16 (1975) (referencing, but explicitly taking no view on, the Ninth Circuit's interpretation).

[155] *See* Carlucci, *supra* note 99, at 368–69 (noting both *Forman* and the use of the Ninth Circuit's approach by other appellate courts).

[156] *See* Couture, *supra* note 20, at 11 (analyzing the application of the third prong of the *Howey* test to TPLF Agreements). On its public-facing website, for example, Cartiga, a consumer TPLF provider, states explicitly that it "does not provide legal assistance or advice beyond the funding process." *See Consumers & Plaintiffs: How Legal Funding Works*, CARTIGA, https://cartiga.com/how-it-works/ [https://perma.cc/7HQC-QTGP] (2023) (describing the basic terms of the company's generic TPLF Agreements). Likewise, Tribeca Lawsuit Loans, another consumer TPLF provider, notes on its public-facing website that the company does not "try to 'protect [Tribeca's] investment' by hijacking your lawsuit" and asserts that it will not interfere or attempt to influence the client's decisions about his or her case. *See Litigation Funding Services*, TRIBECA LAWSUIT LOANS, https://tribecalawsuitloans.com/litigation-funding/ [https://perma.cc/DL6R-KLB4] (2023) (providing an overview of Tribeca Lawsuit Loans' TPLF services and agreements).

[157] *See* Couture, *supra* note 20, at 11 (discussing the potential implication of attorney professional conduct rules on the *Howey* Test as it applies to TPLF Agreements). The American Bar Association's Model Rule of Professional Conduct 2.1, for example, mandates that an attorney "exercise[s] *independent* professional judgment and render candid advice." MODEL RULES OF PRO. CONDUCT r. 2.1 (2020) (emphasis added).

[158] *See* Couture, *supra* note 20, at 11 (concluding that, in practice, the role of the attorney of a litigant who has contracted with a TPLF provider is sufficient for a TPLF Agreement to satisfy the third prong of the *Howey* Test); SEC v. Glenn W. Turner Enters., 474 F.2d 476, 482–83 (9th Cir. 1973) (asserting the Ninth Circuit's functionalist approach to the *Howey* Test's third prong).

[159] 540 U.S. 389, 394 (2004). In *Edwards*, the respondent's company sold payphones to members of the public via agreements structured as five-year leasebacks, through which purchasers received an annual 14% return. *Id.* at 391. The company ultimately filed for bankruptcy, and the SEC brought a civil action alleging violations of both the Securities Act of 1933 and the Securities Exchange Act of 1934. *Id.* at 391–92. Per the district court, the leaseback arrangements constituted an "investment

TPLF provider, as the purported investor here, the cumulative promised return on a TPLF Agreement will generally involve fixed return components based on the interest rate and funding terms to which the parties agree prior to funding.[160] Per *Edwards*, the typical fixed return structure of a consumer TPLF Agreement would not bar treatment of the Agreement as an "investment contract" under the *Howey* test.[161]

4. Leveraging Existing Remedies for a Novel Application

Among the many remedial provisions of the 1933 and 1934 Acts, Section 10(b) of the 1934 Act is particularly salient to consumer-facing issues inherent to TPLF Agreements.[162] Section 10(b) prohibits the use of deception and ma-

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contract" under federal securities law. *Id.* at 392. The Eleventh Circuit reversed, in part because it determined that arrangements in which the rate of return is fixed are definitionally excluded from being an "investment contract" under the *Howey* Test. *Id.* at 392–93.

[160] *See supra* notes 21–26 and accompanying text (discussing the mechanics of consumer TPLF Agreements).

[161] *See* 540 U.S. at 393 (rejecting the Eleventh Circuit's determination that there should be a distinction between fixed returns and variable returns for the purposes of the *Howey* Test); SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946) (listing the elements of an "investment contract" for the purposes of the Securities Act of 1933).

[162] *See* Couture, *supra* note 20, at 18–19 (arguing that Section 10(b)'s anti-fraud provisions could be used to address fraud risks and information gaps in TPLF Agreements). All securities transactions are subject to these anti-fraud provisions, but such broad applicability is not true of all provisions and requirements of the 1933 and 1934 Acts. *Frequently Asked Questions About Exempt Offerings*, SEC, https://www.sec.gov/education/smallbusiness/exemptofferings/faq?auHash=rh5WfJi9h3wRzP6X2anOmgYLdhPHNuo-3Vw0YNZyR_M#faq1 [https://perma.cc/RYH5-YFU9] (Apr. 6, 2023). Of relevance to this Note, under Section 4(a)(2) of the 1933 Act, issuers are exempt from the SEC's registration requirements when no public offering of securities is involved. 15 U.S.C. § 77d(a)(2). This so-called "private placement" exemption applies so long as the purchasers of such securities are either sophisticated actors or sufficiently resourced to bear the investment's risk, have access to information about the offering that is sufficiently similar to that which would be provided for a registered offering, and agree to refrain from reselling or otherwise distributing the securities to members of the public. *Id.*; *Private Placements—Rule 506(b)*, SEC, https://www.sec.gov/education/smallbusiness/exemptofferings/rule506b [https://perma.cc/M9A9-GK3G] (Aug. 27, 2023). Advertising to, or solicitation of, the public are also typically barred. *Id.* Rule 506(b) of the SEC's Regulation D lays out objective standards on which a potential issuer can rely to ensure that they are covered by Section 4(a)(2) and therefore exempt from registration. *Id.*; *see* 17 C.F.R. § 230.506(b) (2022) (requiring in part that (1) there must be only thirty-five or fewer purchasers of the securities in a ninety-day period and (2) such purchasers are either accredited investors or, if they are non-accredited, have "such knowledge and experience in financial and business matters that [they are] capable of evaluating the merits and risks of the prospective investment, or the issuer reasonably believes immediately prior to making any sale that such purchaser[s] [come] within this description"). Importantly, the private placement exemption from registration and its attendant burdens on an issuer would likely apply to an agreement between a TPLF recipient and a TPLF provider, with the recipient as the securities issuer and the provider as the sophisticated purchaser. *See* 15 U.S.C. § 77d(a)(2); 17 C.F.R. § 230.506(b). Note, too, that TPLF Agreements would also likely be exempt from statutory registration and associated reporting requirements under the 1934 Act and its attendant regulations. *See* 15 U.S.C. § 78l(g)(1) (requiring SEC registration and periodic disclosures only if an issuer's total assets are greater than $10,000,000 and its securities are held by either 2,000 or more individuals or at least 500 non-accredited investors).

nipulation "in connection" with security purchases or sales.[163] To implement Section 10(b), the SEC promulgated Rule 10b-5, which further defines Section 10(b)'s prohibitions to extend to material untrue statements or omissions, fraudulent or deceitful actions, and actions intended to defraud.[164] In more traditional securities arrangements, Section 10(b) actions have been successfully utilized to counteract fraudulent activities ranging from insider trading to nondisclosure and informational misrepresentations.[165] Notably, both buyers *and* sellers in security transactions have standing to sue in a private right of action brought under Section 10(b).[166]

5. *Howey* and Consumer TPLF: Complementary Public Policies

Regulating consumer TPLF Agreements as investment contracts under the *Howey* Test is also viable with respect to the underlying policies at play with such a regulatory dynamic.[167] Subsection a[168] describes recent judicial emphasis on *Howey*'s intended flexibility in addressing emerging and heretofore unregulated financial arrangements, while Subsection b[169] describes the value of this flexibility in regulating consumer TPLF Agreements.

a. Renewed Attention to Adaptability as a Defining Feature of Howey

In opinions involving the *Howey* Test, the Supreme Court has consistently called on courts to apply *Howey* flexibly.[170] The Court has been particularly

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[163] 15 U.S.C. § 78j(b). Recall that, for the purposes of federal securities law, an "investment contract" within the meaning of the *Howey* Test is a "security." *See* Tcherepnin v. Knight, 389 U.S. 332, 338 (1967) (applying the *Howey* Test to the term "investment contract" as that term is used in the 1934 Act).

[164] *See* 17 C.F.R. § 240.10b-5 (2022) (codifying the SEC's regulations deriving from the authority of Section 10(b)).

[165] *See* Eric C. Chaffee, *Standing Under Section 10(b) and Rule 10(b)-5: The Continued Validity of the Forced Seller Exception to the Purchaser-Seller Requirement*, 11 U. PA. J. BUS. L. 843, 844 (2009) (providing background on the scope of Section 10(b) and Rule 10b-5).

[166] *See* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 735–36, 754–55 (1975) (holding that, under Section 10(b) and Rule 10b-5, buyers and sellers of securities subject to deceptive or manipulative conduct had standing for private suit); 5B ARNOLD S. JACOBS, DISCLOSURE & REMEDIES UNDER THE SECURITIES LAWS § 9:5 (Supp. 2023) (outlining standing law for the purposes of Section 10(b) and citing to major cases); Couture, *supra* note 20, at 18 (stating that both buyers and sellers have standing for the purposes of Section 10(b)).

[167] *See infra* note 172 and accompanying text (tracing the central policy argument at work in *Howey* and its Supreme Court progeny); *infra* note 180 and accompanying text (describing the potential role of consumer TPLF Agreements in lessening the economic burden of pursuing civil litigation).

[168] *See infra* notes 170–177 and accompanying text.

[169] *See infra* notes 178–181 and accompanying text.

[170] *See Howey*, 328 U.S. at 299 (describing the *Howey* Test as "embo[dying] a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits"). Given the variety of arrangements categorized by lower courts as "investment contracts," such an exhortation appears to be

sensitive to the potential exploitation of a strict *Howey* Test construction by innovative investment devices and vehicles.[171] Against this backdrop, the Court has reinforced the notion that a *Howey* Test analysis should preference substance over form and reflect "economic reality."[172]

The seriousness with which courts treat the importance of malleability in applying *Howey* to novel financial arrangements has become newly apparent in the context of the burgeoning cryptocurrency market.[173] In 2017, for example, the SEC employed the *Howey* Test to determine that crypto tokens sold by virtual blockchain group The Decentralized Autonomous Organization constituted "investment contracts" and, by extension, regulable securities under federal securities law.[174] Between 2019 and 2020, the U.S. District Court for the Southern District of New York similarly stressed the *Howey* Test's core flexibility and role as an analytical framework for "unconventional" arrangements

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taken seriously. *See, e.g.*, Smith v. Gross, 604 F.2d 639, 642–43 (9th Cir. 1979) (finding an "investment contract" in an agreement to purchase earthworm offspring); Miller v. Cent. Chinchilla Grp., 494 F.2d 414, 415, 417–18 (8th Cir. 1974) (finding an "investment contract" in an agreement to purchase and resell chinchillas); Glen-Arden Commodities, Inc. v. Costantino, 493 F.2d 1027, 1031, 1034–35 (2d Cir. 1974) (finding an "investment contract" in an agreement to warehouse, insure, and sell Scotch whisky casks); Kemmerer v. Weaver, 445 F.2d 76, 78–79 (7th Cir. 1971) (finding an "investment contract" in a purchase, care, and resale agreement for domesticated beavers).

[171] *See* Reves v. Ernst & Young, 494 U.S. 56, 60–61 (1990) (explaining that, in passing the 1933 and 1934 Acts, Congress sought to define a security in a manner cognizant of the "virtually limitless scope of human ingenuity" and broad enough to "encompass virtually any instrument that might be sold as an investment").

[172] *See id.* at 61 (describing the congressional purpose of the federal securities laws as "regulat[ing] *investments*, in whatever form they are made and by whatever name they are called"); United Hous. Found. v. Forman, 421 U.S. 837, 849 (1975) (determining that Congress "intended the application [of the Security Act of 1933 and the Security Exchange Act of 1934] to turn on the economic realities underlying a transaction, and not on the name appended thereto"); Tcherepnin v. Knight, 389 U.S. 332, 336 (1967) (citing to *Howey* in its assertion that "form should be disregarded for substance" in the analysis of possible securities).

[173] *See, e.g.*, Carol R. Goforth, *Cinderella's Slipper: A Better Approach to Regulating Cryptoassets as Securities*, 17 HASTINGS BUS. L.J. 271, 313–15 (2021) (noting potential modifications to the *Howey* Test to better capture the realities of cryptoassets); John Marinelli, *Meet the New Boss, Same as the Old Boss: How Federal Agencies Have Leveraged Existing Law to Regulate Cryptocurrency*, 57 AM. CRIM. L. REV. ONLINE 34, 40–41 (2020) (explaining the SEC's use of *Howey* to establish jurisdiction over certain cryptocurrency tokens); Mendelson, *supra* note 128, at 73–82 (analyzing the potential application of the *Howey* Test to cryptocurrencies and initial coin offerings). For background information on the technology behind, and various use cases for, cryptocurrency, see generally Kevin Roose, *The Latecomer's Guide to Crypto*, N.Y. TIMES (Mar. 18, 2022), https://www.nytimes.com/interactive/2022/03/18/technology/cryptocurrency-crypto-guide.html [https://perma.cc/JVB3-4GKR].

[174] *See* Mendelson, *supra* note 128, at 66–67. *See generally* Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The DAO, Exchange Act Release No. 81207 (July 25, 2017) (detailing the SEC's investigation into, and findings with respect to, The Decentralized Autonomous Organization). The Decentralized Autonomous Organization, or "The DAO," raised roughly $150 million in an initial offering of crypto tokens and was subsequently hacked. *Id.* In coming to its inclusion about the categorization of the tokens as "investment contracts," the SEC drew on the principles expressed in *Howey*, *Tcherepnin*, and *Forman*. *Id.*

of exchange in addressing three novel cryptoasset determinations.[175] Other jurisdictions have followed suit.[176] Within this recently renewed framing of the *Howey* Test as an appropriate regulatory tool for even the most cutting edge financial instruments, courts are arguably primed to extend *Howey*'s reach to other yet-untouched arrangements like consumer TPLF Agreements.[177]

b. Consumer TPLF Agreements: In Service of a Broader Goal

Although it is a for-profit industry, consumer TPLF is, at least in theory, intended to improve access to justice among lower-income populations.[178] Proponents of consumer TPLF Agreements argue that, through for-profit TPLF funding, private market forces can efficiently distribute funding to litigants with meritorious claims but limited financial resources.[179] In this way, consumer TPLF funding can be an important backstop for litigants who cannot independently afford to enter into litigation and are not covered under existing safety nets provided by public interest and legal services organizations.[180] Viewing consumer TPLF through this lens, a flexible regulatory approach

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[175] *See* SEC v. Kik Interactive, Inc., 492 F. Supp. 3d 169, 177 (S.D.N.Y. 2020) (acknowledging that, with little to no precedent on which to rely, the presiding judge's determination would be informed by the flexibility mandated in *Howey*); SEC v. Telegram Grp. Inc., 448 F. Supp. 3d 352, 358–59, 364–65 (S.D.N.Y. 2020) (reiterating the purpose of the *Howey* Test in the context of relevant Supreme Court decisions); Balestra v. ATBCOIN LLC, 380 F. Supp. 3d 340, 352–53 (S.D.N.Y. 2019) (stressing, in the context of a cryptoasset case, the importance of a flexible, fact-based inquiry that prioritizes form over substance when applying the *Howey* Test).

[176] *See, e.g.*, SEC v. NAC Found., 512 F. Supp. 3d 988, 995 (N.D. Cal. 2021) (noting that, in deciding that the SEC sufficiently pled the three prongs of the *Howey* Test against the sponsors of an initial coin offering, the court "[bore] in mind the Supreme Court's repeated rejection of a narrow and literal reading of the definition of securities") (internal quotations omitted); Diamond Fortress Techs., Inc. v. EverID, Inc., 274 A.3d 287, 299–300, 304 (Del. Super. Ct. 2022) (emphasizing the fact-intensive nature of applying the *Howey* Test and basing its determination, in part, on the "economic reality" of the token transaction at issue in the case).

[177] *See supra* notes 170–176 and accompanying text (exploring courts' understanding and application of the *Howey* Test in accord with Supreme Court guidance).

[178] *See* Roni Elias, *Mythbusting: Why the Critics of Litigation Finance Are Wrong*, 13 FLA. A & M U.L. REV. 111, 114 (2017) (arguing that TPLF Agreement serve an important social good).

[179] *Id.* Writing from a law and economics perspective, Professor Ronen Perry characterizes TPLF as a form of "investment-based litigation crowdfunding" that is "generally a welcome phenomenon, because it enables parties to pursue meritorious claims and defenses without generating a significant risk of frivolous litigation." Ronen Perry, *Crowdfunding Civil Justice,* 59 B.C. L. REV. 1357, 1360 (2018).

[180] Elias, *supra* note 178, at 114. The existence of an income-driven "justice gap" in America is statistically borne out. *See, e.g.*, *The Justice Gap: The Unmet Civil Legal Needs of Low-Income Americans*, LEGAL SERVS. CORP. (2022) (studying barriers to civil legal access among low-income American households, defined as households with a total income under 125% of the national poverty threshold). In one study, researchers found that 74% of low-income American households experienced one or more civil legal issues in 2021, but such households sought legal help for only 25% of such issues. *Id.* Over half of low-income households are unsure they could locate and afford to hire an attorney if needed. *Id.*

available under *Howey* that can grow and change with the industry is preferable to the more rigid approach available under alternative regulatory methods.[181]

III. Bringing TPLF Under the Umbrella of Securities Regulation

Consumer TPLF Agreements fill a funding gap for individual litigants and, by extension, a gap in access to justice that would leave certain consumer plaintiffs without bargaining power in otherwise meritorious lawsuits.[182] The risk of abuse inherent to such agreements, however, necessitates a nuanced regulatory approach.[183]

Section A of this Part argues that consumer TPLF Agreements should be treated as investment contracts subject to the 1933 and 1934 Acts, rather than as loans subject to state law.[184] Section B describes the most likely remedies available to individual litigants involved in consumer TPLF Agreements under this approach.[185]

A. A Securities-Based Approach Strikes a Better Regulatory Balance

At the state level, the characterization of consumer TPLF Agreements as loans, to which usury may apply, is far from settled.[186] The nonrecourse nature of typical TPLF Agreements calls into question both the obviousness and appropriateness of leveraging usury as a regulatory tool.[187] In *Oasis Legal Fi-*

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[181] *See supra* notes 170–177 and accompanying text (describing the flexibility of *Howey* as a regulatory tool); *supra* notes 178–180 and accompanying text (outlining the function of consumer TPLF as a potential equitable tool in civil litigation).

[182] *See infra* note 195 and accompanying text (noting the implications of consumer TPLF Agreements for access to justice issues in civil litigation).

[183] *See infra* note 198 and accompanying text (describing critiques of consumer TPLF Agreements that emphasize the predatory potential of such Agreements).

[184] *See infra* notes 186–195 and accompanying text.

[185] *See infra* notes 196–204 and accompanying text.

[186] *See supra notes* 31–44 and accompanying text (discussing the role of champerty and maintenance in state TPLF regulation); *supra notes* 45–73 and accompanying text (examining usury in the context of state TPLF regulation); *supra notes* 74–86 and accompanying text (describing direct statutory regulation of TPLF Agreements at the state level).

[187] *See* Bernardo M. Cremades, Jr., *Usury and Other Defenses in U.S. Litigation Finance*, 23 KAN. J.L. & PUB. POL'Y 151, 161–62 (2014) (noting the ongoing debate in legal scholarship around the applicability of usury laws to TPLF Agreements given that such agreements do not satisfy the traditional definition of a loan by virtue of their nonrecourse nature). Recall that traditional usury doctrine requires a definite obligation to repay borrowed amounts, where the nonrecourse structure of consumer TPLF Agreements requires repayment only if a litigant's lawsuits result in a monetary award. *See* WILLISTON, *supra* note 52, § 20:18 (putting forth the traditional requirements for an instrument to be considered a loan); RESTATEMENT (FIRST) OF CONTRACTS § 527 cmt. A (AM. L. INST.1932) ("[U]sury laws do not forbid the taking of business chances in the employment of money . . . ."). *Compare, e.g.*, Anglo-Dutch Petroleum Int'l, Inc. v. Haskell, 193 S.W.3d 87, 96–97 (Tex. App. 2006) (viewing the lack of a guaranteed repayment to a TPLF provider as dispositive of a TPLF

nance Group, LLC v. Coffman, for example, significant judicial discretion was necessarily exercised to bring consumer TPLF Agreements under Colorado's existing consumer loan regulations.[188] Moreover, inconsistencies among state regulatory approaches to consumer TPLF Agreements—whether such regulation is effected through statute, dictated by common law, or is simply nonexistent—encourages forum-shopping among TPLF providers, rather than reform or self-regulation.[189]

In contrast, a uniform federal regulatory approach leveraging existing federal securities laws better reflects the realities of the consumer TPLF market.[190] As a threshold matter, TPLF Agreements fit more naturally under the *Howey* Test's definition of "investment contract" as contemplated by the 1933 and 1934 Acts—at least in the many jurisdictions where horizontal commonality is not required.[191] Courts' ongoing recognition of the flexibility of the *Howey* Test, in light of innovation inherent to the growth of cryptoassets and other novel financial arrangements, is critical to the development of case law that can adapt to the rapidly growing TPLF industry with relative ease.[192]

The uniformity of federal regulation under the 1933 and 1934 Acts may also discourage forum shopping among TPLF providers, with two important

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Agreement's status as a non-loan and, therefore, an instrument to which usury protections could not attach), *and* Kraft v. Mason, 668 So. 2d 679, 684 (Fla. Dist. Ct. App. 1996) (holding that a lending agreement to which lender repayment is uncertain cannot be usurious), *with* Odell v. Legal Bucks, LLC, 665 S.E.2d 767, 777 (N.C. Ct. App. 2008) (holding that a consumer TPLF Agreement was subject to the state's usury statute because of its inherent reimbursement expectation).

[188] *See supra* notes 106–118 and accompanying text (analyzing the analytical steps taken by the Colorado Supreme Court to bring two consumer TPLF Agreements under the purview of the UCCC).

[189] *See* Popp, *supra* note 87, at 749 (arguing that the variety of TPLF regulatory approaches at the state level incentivizes forum-shopping, in which TPLF providers seek to generate revenue in the least restrictive states and subject consumer litigants to choice-of-law and choice-of-forum provisions). The Institute for Legal Reform, as the advocacy arm of the United States Chamber of Commerce, has voiced forum-shopping concerns with respect to TPLF. *See* U.S. CHAMBER OF COM. INST. FOR LEGAL REFORM, STOPPING THE SALE ON LAWSUITS: A PROPOSAL TO REGULATE THIRD-PARTY INVESTMENTS IN LITIGATION 1, 9 (2012) (arguing that "a checkerboard of disparate state laws, rules, and regulations that apply only within any given state . . . likely would funnel TPLF-financed cases to the state courts in the jurisdiction with the weakest oversight regimes"). The wide variety of state TPLF legal regimes lends itself to a potential "regulatory race," which can emerge in the context of three antecedent conditions: (1) regulatory differences across jurisdictions; (2) a valid threat that where a firm chooses to do business will be influenced by such differences, and; (3) actions to adjust regulations as a threat-response by the jurisdictions with more onerous regulations. *See* Bruce V. Carruthers & Naomi R. Lamoreaux, *Regulatory Races: The Effects of Jurisdictional Competition on Regulatory Standards*, 54 J. ECON. LITERATURE 52, 54 (2016) (defining the necessary conditions for a "regulatory race" between jurisdictions to arise).

[190] *See infra* notes 191–195 and accompanying text (describing the benefits of using existing federal securities law to regulate consumer TPLF Agreements).

[191] *See supra* notes 120–161 and accompanying text (walking through the required elements of an "investment contract" under the *Howey* Test as they may apply to TPLF Agreements).

[192] *See supra* notes 173–177 and accompanying text (collecting cases that have extended the definition of "investment contract" to certain cryptoassets and offerings, in reliance at least in part on *Howey*'s underlying policy of flexibility).

implications.[193] First, unlike a state-by-state regulatory approach, a federally imposed regulatory system would discourage a potential "race to the bottom" among consumer TPLF providers.[194] Second, a federally imposed system would serve the broader goal of improving access to justice, particularly among lower-income litigants.[195]

B. Federal Securities Law Provides More Appropriate Remedies

In the context of consumer TPLF regulation, Section 10(b) of the 1934 Act would provide a ready-made private right of action to individual litigants who have entered into consumer TPLF Agreements.[196] That both buyers *and* sellers in security transactions have standing to sue under Section 10(b) is critical with respect to consumer TPLF Agreements, as the structure of a TPLF Agreement would place the individual litigant in the role of the security seller and the TPLF provider in the role of the security buyer.[197]

The breadth of the mandate under which Section 10(b) actions may be brought is well-suited to address the diverse concerns of consumer TPLF critics.[198] In particular, the issue of information asymmetry between consumer TPLF funders and individual litigants, to which the disclosure-based provisions of state statutory TPLF regulations often give voice, has an appropriate

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[193] *See supra* note 189 and accompanying text (discussing the ways in which a lack of uniformity across state TPLF regulation may promote forum-shopping and incentivize de-regulation at the state level as a matter of competition).

[194] *See supra* note 189 and accompanying text (same).

[195] *See* Popp, *supra* note 87, at 745–46 (noting that, given the lack uniformity among state approaches to, and approval of, TPLF Agreements, consumer access to TPLF services is itself dependent on geography); *supra* notes 178–181 and accompanying text (describing consumer TPLF's potential role in increasing lower-income litigants' access to the civil litigation process and providing quantitative data on the "justice gap" in America).

[196] *See* Couture, *supra* note 20, at 18 (noting the purposes of Section 10(b), including its conferral of a private right of action on parties to securities transactions).

[197] *See supra* note 166 and accompanying text (noting the standing granted to both buyers and sellers under Section 10(b)); *supra* notes 162–166 and accompanying text (describing the relative positioning of the individual litigant as the investment seller when he or she enters into a consumer TPLF Agreement in the context of the *Howey* Test).

[198] *See, e.g.*, CONSUMERS FOR FAIR LEGAL FUNDING, https://fairlegalfunding.org/ [https://perma.cc/7J7B-W5FY] (2022) (describing contentions by Consumers for Fair Legal Funding, an activist group calling for state regulation of TPLF in New York, that certain TPLF funders "fleec[e]" homeless individuals by encouraging them to file funded lawsuits and later charging interest rates on funded amounts in excess of 100%); U.S. CHAMBER INST. FOR LEGAL REFORM, SELLING MORE LAWSUITS, BUYING MORE TROUBLE: THIRD PARTY LITIGATION FUNDING A DECADE LATER 26–27 (2020) (calling for mandated disclosure of TPLF Agreements to combat conflicts of interest, inhibit fee-sharing between attorney and non-attorney funders in violation of attorney professional conduct rules, and support both litigant control over his or her lawsuit and the continued viability of maintenance and champerty as common-law doctrines); Terrence Cain, *Third Party Funding of Personal Injury Tort Claims: Keep the Baby and Change the Bathwater*, 89 CHI.-KENT L. REV. 11, 12–13 (2014) (noting that TPLF providers have been criticized for, among other things, promoting abusive litigation and taking advantage of "vulnerable, desperate, and unsophisticated persons").

outlet in Section 10(b)'s prohibition on both material misrepresentations and material omissions.[199]

Moreover, bringing consumer TPLF Agreements under federal securities law would empower not only affected individuals, but also the SEC itself in taking direct civil enforcement actions against abusive consumer TPLF providers.[200] Such actions could also form the basis of federal criminal prosecutions as needed.[201] The SEC, backed by the resources and signaling power of the federal government, is well-suited to move efficiently and flexibly to address the evolving contours of emerging markets like that of consumer TPLF Agreements.[202]

In comparison to federal securities regulation, usury and statutory interest rate caps on consumer TPLF Agreements are arguably blunt tools for a nuanced situation.[203] Whereas dictation of consumer TPLF Agreement terms under such approaches may discourage growth of the TPLF industry, a regulatory

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[199] *See* 17 C.F.R. § 240.10b-5(b) (2022) (interpreting Section 10(b) to bar a seller or buyer of securities both from "mak[ing] any untrue statement of a material fact or . . . omit[ting] to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading"). Many state statutes specifically targeting consumer TPLF loans include mandatory disclosure provisions. *See, e.g.*, ARK. CODE. ANN. § 4-57-109(c) (2020), discussed *supra* note 79 (describing Arkansas' consumer TPLF statute's requirement of "prominent disclos[ure]" of a TPLF Agreement's annual interest rate); ME. STAT. tit. 9-A, § 12-104 (2022), discussed *supra* note 81 (describing Maine's statutory requirement that consumer TPLF providers furnish litigants with the state's standardized disclosure form); W. VA. CODE § 46A-6N-5 (2022), discussed *supra* note 84 (describing West Virginia's statutory disclosure requirements for consumer TPLF Agreements).

[200] 15 U.S.C. §§ 78u(a), (d); *see* Steve Thel, *Taking Section 10(b) Seriously: Criminal Enforcement of SEC Rules*, 2014 COLUM. BUS. L. REV. 1, 9–10 (describing the SEC's authority to pursue injunctive relief, punitive fines, and administrative sanctions for violations of the 1934 Act).

[201] 15 U.S.C. § 78ff(a); *see* Thel, *supra* note 200, at 11 (explaining the criminal penalty mechanisms in the statutory scheme).

[202] *See, e.g.*, Rohan Goswami & MacKenzie Sigalos, *SEC Proposes Rules That Would Change Which Crypto Firms Can Custody Customer Assets*, CNBC, https://www.cnbc.com/2023/02/15/sec-chair-gensler-crypto-firms-need-to-register-to-custody-assets.html [https://perma.cc/9D8A-H6N5] (Feb. 15, 2023) (reporting on the SEC's proposal to expand custody requirements at the federal level to better encompass crypto exchanges); Press Release, SEC, SEC Proposes Rules to Enhance Disclosure and Investor Protection Relating to Special Purpose Acquisition Companies, Shell Companies, and Projections (Mar. 30, 2022), https://www.sec.gov/news/press-release/2022-56 [https://perma.cc/T2QV-Q8K3] (notifying the public of the SEC's new rule proposal to address Special Purpose Acquisition Companies (SPACs) in the wake of the "SPAC boom" in 2021); Jacob Rund, *Startups and Crowdfunding Limits: SEC Rule Changes Explained*, BLOOMBERG L. (Mar. 30, 2021), https://news.bloomberglaw.com/securities-law/startups-and-crowdfunding-limits-sec-rule-changes-explained [https://perma.cc/97HZ-BVE9] (describing the SEC's changes, known as "Regulation Crowdfunding," to loosen registration requirements on startups offering stock sales via crowdfunding as a capital-raising mechanism).

[203] *See* Susan Lorde Martin, *Litigation Financing: Another Subprime Industry That Has a Place in the United States Market*, 53 VILL. L. REV. 83, 115 (2008) (pushing back against usury prohibitions as an appropriate regulatory measure for TPLF Agreements and arguing that price caps, including interest rate ceilings, "often . . . hurt just the people they are supposed to protect").

approach built on federal securities law would instead seek to discourage growth of exploitative impulses within that industry.[204]

CONCLUSION

Presently, consumer TPLF Agreement regulation is at the discretion of the individual states. Among states who exercise some regulatory control over consumer TPLF Agreements, there is no cohesive or even particularly dominant mode of regulation. Instead, state regulations are an assortment of common-law doctrines, usury prohibitions, and bespoke statutes. Consumer TPLF Agreements are currently not subject to federal regulation.

Under the standard established by the Supreme Court in *SEC v. W. J. Howey Company,* consumer TPLF Agreements fit comfortably within the definition of an "investment contract" for the purposes of federal securities law. Moreover, recent applications of the *Howey* Test to cryptoassets and other novel financial arrangements underscore its policy of high flexibility relative to innovations in financial transactions and contracting. Therefore, consumer TPLF Agreements should be federally regulated as securities under the Securities Act of 1933 and the Securities Exchange Act of 1934. The Securities Exchange Act of 1934's Section 10(b) is a particularly suitable statutory provision for this purpose.

Consumer TPLF Agreements can be a vital funding source for individual litigants and an effective tool in bridging a wealth-based gap in access to justice in civil matters. With this fundamental policy consideration in mind, consumer TPLF Agreements should be regulated under a uniform system that is cognizant of both the benefits of a robust consumer TPLF market and the potential for abuses within such a market. Regulating consumer TPLF Agree-

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[204] *See* Cain, *supra* note 198, at 38 (declining to include mandatory caps on interest rates in his proposal for national legislation to regulate consumer TPLF Agreements in the personal injury context). Professor Susan Lorde Martin, through an access to justice lens, encapsulates the core argument against applying usury law or interest rate caps to consumer TPLF Agreements as follows:

> Government should not be so paternalistically protective of people who do not have access to traditional forms of credit that it keeps those people from owning homes, having washers and dryers, or pursuing meritorious lawsuits. More widely available credit creates important opportunities for those with a poor credit history or without any credit history at all. Thus legislatures and courts must recognize that subprime credit is going to be more expensive, because the risks are greater for the lender, and not seek, because of sympathy for subprime borrowers, to compare subprime rates with those of traditional lenders. Doing so will discourage litigation funders, decreasing competition and opportunities instead of expanding them, and forcing plaintiffs with no resources to accept unfairly low settlement offers because they cannot afford to wait for a better offer or to go to trial.

Martin, *supra* note 203, at 116.

ments under existing federal securities law is an approach well-suited to balancing these competing interests.

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