

SHOULD THE LAW PRESERVE PARTY CONTROL?  
LITIGATION INVESTMENT, INSURANCE LAW, AND  
DOUBLE STANDARDS

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ABSTRACT

*Litigation investment, sometimes known as litigation finance, is increasingly accepted around the world. Once prohibited as champerty, litigation investment is now embraced in England, Canada, and Australia, as well as in many civil law nations. In the United States, the development of a robust market for investment in litigation has been met by various objections. One objection is that litigation investment interferes with the autonomy of lawyers. A second objection is that it promotes frivolous litigation.*

*This Article takes up a popular argument against litigation investment: the legal system should not encourage parties to sell their control over litigation that would vindicate their rights. This criticism is based on an unspoken assumption that private law theory requires party control to stay with the original rightholder and contracts that allow the sale of party control to a stranger should be struck down, either for being contrary to public policy or for some other legal basis.*

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*Although I briefly consider justifications rooted in moral philosophy, which support the view that party control should not be sold, I focus mostly on arguments based on the common law. I propose that arguments against the sale of party control based on the structure or nature of the common law are anachronistic. As society evolved, courts and legal commentators abandoned such arguments, which once constrained the sale of party control before the middle of the nineteenth century. Liberal attitudes about the sale of party control were first seen in the gradual elimination of rules limiting the assignment of choses in action. Liberalization was next seen in insurance. I will demonstrate that as the role of insurance in society grew, courts reinterpreted common law practices to permit the alienation of control of litigation for profit in various contexts, including subrogation and liability insurance.*

*This Article concludes that by looking at the evolution of insurance law, we can learn how rigid attitudes about the relationship between victims and wrongdoers can be bent to fit social needs. The Article takes note of the growing consensus in the United States, as well as in other common law nations, regarding the social benefits of litigation investment. Finally, I argue that given the appetite for litigation investment among the public, courts and policymakers should be skeptical of arguments that use party control as a justification to block this new form of financing for lawsuits.*

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## INTRODUCTION

Along with other common law nations, the United States is experiencing a dramatic increase in litigation investment.<sup>1</sup> Litigation investment is a contract between strangers whereby one takes an interest in the future recovery of the other's lawsuit in exchange for something of value.<sup>2</sup> As litigation investment has become more common, drawing the attention of sophisticated financial institutions, it has also garnered some critical attention as well.<sup>3</sup> Among the many arguments against litigation investment is that it impermissibly interferes with the control of litigation by the parties to the dispute.<sup>4</sup> This Article responds to the "control argument" by making two points: first, that the common law permits parties to alienate their control over litigation by contract in numerous contexts; and second, that the fact that the common law has enforced contracts permitting the alienation of control over litigation in contexts other than litigation investment (specifically the insurance context) should make us skeptical of the argument that litigation investment represents a new threat to civil litigation as it is practiced in the United States today.<sup>5</sup>

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1. See Maya Steinitz & Abigail C. Field, *A Model Litigation Finance Contract*, 99 IOWA L. REV. 711, 713-19 (2014) (describing the commercial litigation investment market). According to the New York City Bar Association, "the aggregate amount of litigation financing outstanding is estimated to exceed \$ 1 billion." Ass'n of the Bar of the City of N.Y. Comm. on Prof'l Ethics, Formal Op. 2011-2 (2011), available at <http://perma.cc/PY3Q-4ADT> (discussing third-party litigation financing).

2. "[C]hamperty is maintaining a suit in return for a financial interest in the outcome." *Osprey, Inc. v. Cabana Ltd. P'ship*, 532 S.E.2d 269, 273 (S.C. 2000) (quoting *In re Primus*, 436 U.S. 412, 424 n.15 (1978)).

3. See, e.g., Binyamin Appelbaum, *Lawsuit Loans Add New Risk for the Injured*, N.Y. TIMES, Jan. 17, 2011, at A1; Binyamin Appelbaum, *Lobby Battle over Loans for Lawsuits*, N.Y. TIMES, Mar. 10, 2011, at B1; Binyamin Appelbaum, *Putting Money on Lawsuits, Investors Share in the Payouts*, N.Y. TIMES, Nov. 15, 2010, at A1; *Investing in Someone Else's Lawsuit*, N.Y. TIMES: ROOM FOR DEBATE (Nov. 15, 2010), [www.nytimes.com/roomfordebate/2010/11/15/investing-in-someone-elses-lawsuit](http://www.nytimes.com/roomfordebate/2010/11/15/investing-in-someone-elses-lawsuit) [<http://perma.cc/7NV8-RFQU>].

4. See, e.g., U.S. CHAMBER INST. FOR LEGAL REFORM, *SELLING LAWSUITS, BUYING TROUBLE: THIRD-PARTY LITIGATION FUNDING IN THE UNITED STATES* 8 (2009), available at <http://perma.cc/3S5J-59JR> ("[Third-party funding thus] places the power to make strategic decisions about [litigation] in the hands of the funder.").

5. See Anthony J. Sebok, *What Do We Talk About When We Talk About Control?*, 82 FORDHAM L. REV. 2939, 2941, 2955-56 (2014).

Litigation investment, as the next Part explains in greater detail, occurs when nonlawyers invest for profit in litigation in which they otherwise have no interest.<sup>6</sup> “[L]itigation is the expenditure of money by a party to enforce (or defend) an existing or anticipated legal claim, when the money is used either to purchase the services of an attorney in anticipation of an appearance before, or submission of materials to, an adjudicative body.”<sup>7</sup> At the end of the twentieth century, some critics argued that the American litigation system needed reform because plaintiffs’ attorneys thought of litigation as an investment, which increased the amount of socially unproductive and frivolous claims.<sup>8</sup> “Litigation investment is now the object of a similar sort of critique based on the fear that litigation will be subject to a new round of commercialization.”<sup>9</sup>

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6. For an excellent review, see STEVEN GARBER, RAND CORP., ALTERNATIVE LITIGATION FINANCING IN THE UNITED STATES: ISSUES, KNOWN, AND UNKNOWN 1, 13 (2010), [http://www.rand.org/content/dam/rand/pubs/occasional\\_papers/2010/RAND\\_OP306.pdf](http://www.rand.org/content/dam/rand/pubs/occasional_papers/2010/RAND_OP306.pdf) [<http://perma.cc/UV3V-UWLP>], and MAX VOLSKY, INVESTING IN JUSTICE: AN INTRODUCTION TO LEGAL FINANCE, LAWSUIT ADVANCES AND LITIGATION FUNDING 25 (2013).

7. Sebok, *supra* note 5, at 2939. Under this definition, litigation investment includes arbitration. See generally LISA BENCH NIEUWVELD & VICTORIA SHANNON, THIRD-PARTY FUNDING IN INTERNATIONAL ARBITRATION (2012); Catherine A. Rogers, *Gamblers, Loan Sharks & Third-Party Funders*, in ETHICS IN INTERNATIONAL ARBITRATION (2014). This definition might be too narrow for some. “Any investment of time and money, even by a layperson—such as the drafting of a demand letter to a debtor by a creditor—could, in theory, count as litigation.” Sebok, *supra* note 5, at 2939 n.4 (citing Marc Galanter, *Reading the Landscape of Disputes: What We Know and Don’t Know (and Think We Know) About Our Allegedly Contentious and Litigious Society*, 31 UCLA L. REV. 4, 11-18 (1983)). The definition used in this Article tracks conventional practice. See, e.g., Jonathan T. Molot, *The Feasibility of Litigation Markets*, 89 IND. L.J. 171 (2014) (reviewing limitations of market for litigation investment).

8. Sebok, *supra* note 5, at 2939. “[T]he plaintiffs’ bar has strong monetary incentives to create liability through repeated litigation of presently non-meritorious claims.” *Id.* at 2939-40 n.5 (quoting Jeremy Kidd, *To Fund or Not to Fund: The Need for Second-Best Solutions to the Litigation Finance Dilemma*, 8 J.L. ECON. & POL’Y 613, 630 (2012)); see also WILLIAM HALTOM & MICHAEL MCCANN, DISTORTING THE LAW: POLITICS, MEDIA, AND THE LITIGATION CRISIS (2004); HERBERT M. KRITZER, RISKS, REPUTATIONS, AND REWARDS: CONTINGENCY FREE LEGAL PRACTICE IN THE UNITED STATES (2004); Anthony J. Sebok, *Dispatches from the Tort Wars*, 85 TEX. L. REV. 1465, 1466 (2007) (reviewing TOM BAKER, THE MEDICAL MALPRACTICE MYTH (2005)) (discussing tort reform and the attack on the entrepreneurial plaintiffs’ bar). Nora Engstrom gives a very different evaluation of the entrepreneurial plaintiffs’ bar, arguing that the settlement mills operated by lawyers with an “entrepreneurial (rather than professional) orientation” serve a valuable social function. Nora Freeman Engstrom, *Sunlight and Settlement Mills*, 86 N.Y.U. L. REV. 805, 810, 819 (2011).

9. Sebok, *supra* note 5, at 2939 n.6.

The plan of this Article is as follows: In Part I, I will explain what litigation investment is and its current status in American law. I also will review the three major arguments against litigation investment, which I call the “consequentialist,” “perfectionist,” and “rule-of-law” critiques. In Part II, I will further examine the rule-of-law critique. Although rooted in the tort reform movement of the 1980s and 1990s,<sup>10</sup> which was concerned primarily with plaintiffs’ lawyers’ abuse of the civil justice system, the rule-of-law critique of litigation investment is concerned with protecting the civil justice system from outside forces such as investment firms. If the law discourages (or prohibits) parties from giving away control over the litigation to strangers who have a financial stake in the outcome, the proper functioning of the courts—including the professional independence of plaintiffs’ lawyers—will be compromised. Part III takes up the question of whether party control over litigation was ever central to the proper functioning of the civil justice system, as the critics seem to assume. In this Part, I will demonstrate that courts have permitted parties to give up control over their claims in litigation and have not blocked the party’s choice because it violated a formal legal value intrinsic to the law known as party control. In fact, in the context of insurance law, courts have permitted strangers to take total control over a party’s litigation.<sup>11</sup> My point is that we should be skeptical of arguments against litigation investment that are based on principles rejected in other areas of tort and insurance law, although the problem of reconciling such a contradiction should not be minimized.<sup>12</sup> My larger goal is to shift the debate

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10. See generally F. Patrick Hubbard, *The Nature and Impact of the “Tort Reform” Movement*, 35 HOFSTRA L. REV. 437 (2006).

11. The liberal attitude toward the alienation of party control in the insurance context is not often explicitly justified in judicial opinions. Insurance law scholars have pointed out that in a legal regime that imposes a duty to defend on insurers, it is rational for insureds to contract away party control in exchange for other benefits, such as coverage. See, e.g., Michelle Boardman, *Insurers Defend and Third Parties Fund: A Comparison of Litigation Participation*, 8 J.L. ECON. & POL’Y 673, 687-89 (2012); James M. Fischer, *Insurer-Policyholder Interests, Defense Counsel’s Professional Duties, and the Allocation of Power to Control the Defense*, 14 CONN. INS. L.J. 21, 44-48 (2008); Charles Silver, *Does Insurance Defense Counsel Represent the Company or the Insured?*, 72 TEX. L. REV. 1583, 1596-98 (1994).

12. As I will suggest in the Article’s conclusion, courts should adopt a liberal attitude toward the alienation of party control in litigation investment for the same reasons they have adopted liberal attitudes toward the alienation of party control in insurance. The reasons for this adoption are not just respect of freedom of contract and efficiency; although those are the

about litigation investment away from the alleged risk it poses to party control toward the question of how to regulate investment in litigation so that it (1) provides increased access to the courts while (2) protecting both parties to the litigation investment contract from opportunistic behavior by the other.<sup>13</sup>

### I. LITIGATION INVESTMENT AND ITS CRITICS

Litigation can be financed with funds from various sources.<sup>14</sup> In common law systems, the most likely source of funds is the litigant herself. On both the plaintiff and defendant side, parties can spend their own money to pay attorneys, purchase litigation support services, and cover litigation-related expenses. Under the “English Rule,” the prevailing party can recover these costs from the losing party; although it must be noted that recovery of legal expenses is not guaranteed when cases settle because these may be themselves the subject of adjustment.<sup>15</sup> In the United States, where each side

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justifications that many insurance law scholars have identified most recently. *See supra* note 11. Beyond simple freedom of contract lies the larger point that like insurance, litigation investment is a “social instrument.” Jeffrey W. Stempel, *The Insurance Policy as Social Instrument and Social Institution*, 51 WM. & MARY L. REV. 1489, 1495 (2010). Following Stempel, this Article takes the position that just as courts promoted freedom of contract in insurance in order to achieve larger social and economic ends, courts should uphold freedom of contract to alienate control in litigation finance in order to achieve similar social and economic ends. *Id.* at 1580-82. As Lord Neuberger’s 2012 lecture suggests, the social benefits of a regulated but broad market in litigation investment have been recognized in other common law systems and are likely to have parallels in the United States. Lord Neuberger, President, Sup. Ct., U.K., Harbour Litigation Funding First Annual Lecture: From Barretery, Maintenance, and Champerty to Litigation Funding (May 8, 2013), <http://www.supremecourt.uk/docs/speech-130508.pdf> [<http://perma.cc/KMY4-ZL4H>].

13. For a discussion of legal approaches for the protection of the parties to the litigation investment contract, see generally Anthony J. Sebok & W. Bradley Wendel, *Duty in the Litigation-Investment Agreement: The Choice Between Tort and Contract Norms When the Deal Breaks Down*, 66 VAND. L. REV. 1831 (2013).

14. For a broad review of sources of civil litigation resources in the United States and Europe, see NEW HORIZONS IN LAW AND ECONOMICS, NEW TRENDS IN FINANCING CIVIL LITIGATION IN EUROPE (Mark Tuil & Louis Visscher eds., 2010), and THE COSTS AND FUNDING OF CIVIL LITIGATION (Christopher Hodges et al. eds., 2010).

15. *See generally* Herbert M. Kritzer, *Lawyer Fees and Lawyer Behavior in Litigation: What Does the Empirical Literature Really Say?*, 80 TEX. L. REV. 1943, 1946 (2002) (discussing the “English Rule” and the “American Rule” of fee shifting). Courts play an increasingly important role in deciding which costs may be shifted to the losing party in England, which has led to an increase in satellite litigation about costs after the primary litigation is completed. *See* LORD JUSTICE RUPERT JACKSON, REVIEW OF CIVIL LITIGATION COSTS: FINAL

bears its own costs absent certain contractual or statutory cost-shifting provisions, litigation costs mean that as a technical matter self-funded prevailing parties are not made whole. Defendants and plaintiffs pay a surcharge even when they are legally in the right because of the existence of good-faith resistance from their opponent.

Some forms of third-party litigation funding in the United States are pervasive features of contemporary life. Most familiar is the plaintiff's attorney who offers to represent a party in litigation on a contingent fee basis. Even though at one time this practice was strictly prohibited in the United States, contingency fees have become a mainstay of American legal culture and, even when criticized, are recognized as the chief means by which lower- and middle-class persons can secure plaintiff-side representation.<sup>16</sup> Even corporations use contingent fee agreements and are doing so with increasing frequency.<sup>17</sup> A second group of third-party litigation funders are insurance companies. Liability insurance, as will be explained in Part III.D, is really two kinds of insurance sold together: "litigation" insurance, which offers to pay for the cost of the insured's litigation under certain circumstances, and "judgment" insurance, which offers to pay for the cost of the insured's legal liabilities under certain circumstances. The two are not unrelated, which is why they are sold together, although in theory they could be broken apart. Someone confident that she will never legally wrong another party might want insurance to cover only the costs of proving that she is not liable. Another person, confident that if he legally wrongs another it will be in circumstances so clear that there would be no point contesting the judgment, might want insurance

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REPORT 29-38, 43-45 (2009), available at <http://perma.cc/43UY-PL59> (discussing the "Costs War").

16. See generally Peter Karsten, *Enabling the Poor to Have Their Day in Court: The Sanctioning of Contingency Fee Contracts, A History to 1940*, 47 DEPAUL L. REV. 231 (1998) (discussing the development of the contingency fee contract and noting that contingency fee contracts are pro-plaintiff); Herbert M. Kritzer, *Seven Dogged Myths Concerning Contingency Fees*, 80 WASH. U. L.Q. 739 (2002) (reviewing the history of contingency fees in the United States).

17. Contingent fees (sometimes referred to as "alternative fees") are no longer the exception among the firms ranked by the Am Law 100 survey. See Drew Combs, *The Am Law 100 2010: Alternative Fee Reality*, AM. L. DAILY (May 10, 2010, 7:01 PM), <http://amlawdaily.typepad.com/amlawdaily/2010/05/altfeereality.html> [<http://perma.cc/W4UG-XKSS>].



to cover only his liability. One could even imagine insurance for persons or corporations who expect to be plaintiffs but want to hedge the cost of legal representation; this need could be met with an insurance product that covers only plaintiff-side litigation costs.<sup>18</sup> Legal aid is a third type of third-party litigation funding.<sup>19</sup> Even though legal aid comprises an important source of civil litigation funds for liability claims in Europe, in the United States legal aid is not a significant source of funds for legal claims outside of housing and civil rights.<sup>20</sup> Legal aid probably occupies a larger role in America in the public's imagination than in the reality of the legal system.<sup>21</sup>

This Article will focus on a fourth kind of third-party funder of litigation: private-sector firms that invest in litigation for profit.<sup>22</sup> Although investment in litigation is not a new phenomenon, recently investment litigation has developed into an industry with a significant presence and a discrete identity. The emergence of litigation investment firms in the United States parallels the rise of similar firms around the world, in both common law and civilian systems.<sup>23</sup> This Article will refer to this last kind of third-party funding as "litigation investment."<sup>24</sup>

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18. Legal expenses insurance is not traditional liability insurance because it pays for the costs of being a plaintiff. This insurance is available in Europe. See Michael Faure & Jef De Mot, *Comparing Third-Party Financing of Litigation and Legal Expenses Insurance*, 8 J.L. ECON. & POL'Y 743, 746-51 (2012).

19. See CHRISTOPHER HODGES ET AL., LITIGATION FUNDING: STATUS AND ISSUES RESEARCH REPORT 17-18 (2012), available at <http://perma.cc/3A6P-PZL4>.

20. ALAN W. HOUSEMAN, CTR. FOR LAW & SOC. POLICY, CIVIL LEGAL AID IN THE UNITED STATES—AN UPDATE FOR 2013, at 5 (2013), available at <http://perma.cc/YL9R-RUSF>.

21. See Richard L. Abel, *Law Without Politics: Legal Aid Under Advanced Capitalism*, 32 UCLA L. REV. 474, 477, 508, 541-42 (1985).

22. See, e.g., Vanessa O'Connell, *Funds Spring Up to Invest in High-Stakes Litigation*, WALL ST. J., Oct. 3, 2011, at B1.

23. See generally VICKI WAYE, TRADING IN LEGAL CLAIMS: LAW, POLICY & FUTURE DIRECTIONS IN AUSTRALIA, UK & US (2008).

24. At various times in the history of American law, courts did not always draw such neat distinctions between different kinds of third-party funding of litigation. A century ago, most courts treated the contingent fee as legally identical to litigation investment by a stranger. See Anthony J. Sebok, *The Inauthentic Claim*, 64 VAND. L. REV. 61, 99-100 (2011). As late as the 1960s, some state courts allowed civil rights groups to be prosecuted under laws prohibiting litigation investment for profit. See *NAACP v. Button*, 371 U.S. 415, 423-26 (1963) (reversing Virginia lower courts that had upheld such a statute).

Although a complete review of the legal and economic landscape of the litigation investment industry is not possible in this Article, the structure of the industry can be laid out in a few broad strokes.<sup>25</sup> First, the industry has two quite different branches.<sup>26</sup> One branch consists of firms that invest in relatively low-dollar-value personal injury claims.<sup>27</sup> This part of the industry is known as “consumer” litigation investment.<sup>28</sup> Consumer litigation investment consists of firms purchasing a partial interest in the proceeds of litigation.<sup>29</sup> The purchase is not of a portion of the legal claim that might produce the proceeds. Instead, the purchase is of the proceeds that will come into existence if the legal claim—and a number of other contingencies—are satisfactorily resolved.<sup>30</sup> Consumer litigation investment is not allowed in all jurisdictions in the United States. There is some controversy over whether, even when consumer litigation investment is legally permissible, it nonetheless falls within the statutory definition of consumer credit, and therefore should be limited by the jurisdiction’s relevant usury laws.<sup>31</sup> Further, some might quibble with the use of the term “invest” in connection with consumer litigation investment because the funds paid to purchase litigation proceeds are almost never used for litigation expenses, such as the lawyer’s time or the costs associated with investigating and trying a claim.<sup>32</sup> This is a consequence of the fact that almost all personal injury suits are handled through contingent fee arrangements, which means that the cases in which

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25. For a review of the legal environment, see Sebok, *supra* note 24, at 99-100, and Maya Steinitz, *Whose Claim Is This Anyway? Third-Party Litigation Funding*, 95 MINN. L. REV. 1268, 1333 (2011). For a review of the economic and business environment, see GARBER, *supra* note 6, at 9-16, and Molot, *supra* note 7, 65-66.

26. GARBER, *supra* note 6, at 9, 13.

27. *See id.* at 9, 12.

28. *Id.* at 9.

29. *See id.* at 9, 12.

30. The proceeds of litigation come into existence when received as funds by the party selling the interest; not when there is a final judgment determining the legal rights of the party selling the interest to the litigation investor. *See id.* at 9-10, 12.

31. *See* Oasis Legal Fin. Grp., LLC v. Suthers, No. 12CA1130, 2013 Colo. App. LEXIS 780, at \*4-6 (May 23, 2013) (holding that litigation investment violates state consumer credit law), *cert. granted in part, and cert. denied in part*, No. 13SC497, 2014 Colo. LEXIS 19 (Jan. 21, 2014); Sebok, *supra* note 24, at 98-102 (review of legal status of litigation investment among the states).

32. *See* GARBER, *supra* note 6, at 12.

consumer litigation investment occurs are already funded by another third party, the plaintiff's attorney.<sup>33</sup> So why do parties sell litigation proceeds to consumer litigation investment firms? According to the consumer litigation investment firms, consumers use the money to pay for living expenses.<sup>34</sup> Because the bargaining strategy for settlement often produces delay until the so-called "eve of trial," plaintiffs are in a better position to maximize settlement value if they are not forced to settle early due to a need for money.<sup>35</sup>

The other branch consists of firms that invest in high-dollar commercial claims, typically involving millions of dollars, and sometimes more. This part of the industry is known as "commercial" litigation investment.<sup>36</sup> Like in consumer litigation investment, commercial litigation investment consists of firms purchasing litigation proceeds. Unlike consumer litigation investment, the funds paid to purchase litigation proceeds are typically used for litigation expenses.<sup>37</sup> Even though commercial litigation investment can involve virtually any sort of claim, it often involves commercial contract and tort disputes, as well as intellectual property and qui tam claims.<sup>38</sup> For a few reasons, the legal status of commercial litigation investment is not identical to that of consumer litigation investment. Although the doctrines of champerty generally do not distinguish between the consumer and commercial purposes of legal investment and, therefore, treat all such contracts as legal or illegal depending on their structure, consumer credit laws (as their name implies) do not typically apply to commercial litigation investment.<sup>39</sup>

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33. This is a product of certain features of contingency fee practice in the United States. In addition to the United States, there is third-party consumer litigation investment in England, Canada, and Australia. In fact, in Canada and Australia consumer class action litigation heavily depends on litigation investment. See Jasminka Kalajdzic et al., *Justice for Profit: A Comparative Analysis of Australian, Canadian and U.S. Third Party Litigation Funding*, 61 AM. J. COMP. L. 93, 113-28 (2013).

34. See GARBER, *supra* note 6, at 16.

35. See Stephen Gillers, *Waiting for Good Dough: Litigation Funding Comes to Law*, 43 AKRON L. REV. 677, 692 (2010).

36. See GARBER, *supra* note 6, at 13.

37. See *id.* at 15.

38. See *id.* at 13; Kalajdzic et al., *supra* note 33, at 132-33.

39. See GARBER, *supra* note 6, at 18 n.4; Sebok, *supra* note 24, at 98-102.

*A. Historical Rejection of Litigation Investment*

For centuries, litigation investment was prohibited in the common law.<sup>40</sup> Originally, the prohibition was seen as a companion to the larger and more sweeping prohibition of the assignment of choses of action. This doctrine, although analytically separate, was supported by the larger, general anxiety over the “commercialization” of litigation in premodern and modern societies.<sup>41</sup> Today, the few limitations on assignment are an anachronistic remnant of this earlier period and only rarely emerge to interfere with or block the fluid transfer of claims in complex commercial markets.<sup>42</sup> The larger anxiety over the commercialization of litigation persists in American society, however, and has its fullest expression along the fault line of champerty law: state law permitting partial ownership of proceeds—and under what circumstances—reveals how freely investment in litigation can occur in that jurisdiction.<sup>43</sup>

Resistance to litigation investment has been broad and varied over the centuries, starting with the Romans.<sup>44</sup> Blackstone strongly opposed any form of litigation investment. He objected that such investors were simply “officious intermeddlers” who would disturb the “repose” of defendants, and he repeated the concern shared by many in the English bar, that wealthy and titled elites would encourage their tenants and retainers to sue their rivals by supporting the costs of the suits—and maybe even rewarding the tenant or retainer with a side payment.<sup>45</sup> Radin hypothesized that some of the resistance was rooted even more deeply than that and reflected Christianity’s vestigial hostility to litigation and secular courts.<sup>46</sup> As these arguments fell aside, they were replaced by

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40. See Max Radin, *Maintenance by Champerty*, 24 CALIF. L. REV. 48, 50-53 (1936).

41. See Sebok, *supra* note 24, at 98-100.

42. *Id.* at 114-15.

43. See *id.* at 107-20.

44. See Radin, *supra* note 40, at 52-56 (describing Roman legal prohibitions on champerty).

45. See *Casserleigh v. Wood*, 59 P. 1024, 1026 (Colo. App. 1900) (“[In Blackstone’s time, the wealthy and powerful] would buy up claims, and, by means of their exalted and influential positions, overawe the courts, secure unjust and unmerited judgments, and oppress those against whom their anger might be directed.”); 4 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND \*134-36 (1769).

46. See Radin, *supra* note 40, at 58 (“[L]itigiousness... [was] an indication of a quarrelsome

arguments that reflected the concerns of the newly emerging market economy.<sup>47</sup> The arguments Radin encountered in 1936 have been supplanted by a new generation that are different—on the surface at least—from the old arguments.<sup>48</sup> The modern arguments can be grouped into three categories: (1) consequentialist, (2) perfectionist, or (3) rule of law (or jurisprudential).

### *B. The Three Modern Critiques*

#### *1. The Consequentialist Critique*

The consequentialist argument typically focuses on the putative, perverse incentives created by the introduction of self-interested third parties in litigation, who are not themselves lawyers. The fear is that by allowing self-interested nonlawyers to support litigation, the quality of litigation will decline, thus producing an increase in the amount of litigation that is fraudulent, frivolous, or specious.<sup>49</sup>

Needless to say, many questionable assumptions are built into the consequentialist argument. Because this Article is not the appropriate place to engage them, it may be more efficient to simply note that most, if not all, of the assumptions that are behind the consequentialist argument parallel the assumptions behind the arguments made by critics of the entrepreneurial plaintiffs bar.<sup>50</sup> The critics of American civil litigation argue that the contingent fee produces lawyer-driven litigation that is more likely to be fraudulent, frivolous, or specious compared to a system in which lawyers

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and un-Christian spirit.”).

47. *Id.* at 72 (noting that new arguments against champerty included its tendency to induce improper litigation, the likelihood that claimholders would be subjected to “hard bargains,” and its tendency to degrade the profession).

48. *See, e.g.*, Darren McKinney, Letter to the Editor, *Lawsuit Loans*, N.Y. TIMES (Jan. 22, 2011), [http://www.nytimes.com/2011/01/23/opinion/lweb23loans.html?\\_r=0](http://www.nytimes.com/2011/01/23/opinion/lweb23loans.html?_r=0) [<http://perma.cc/LG8K-BWPS>]. “[T]he ancient Greeks and Romans to Western lawmakers and jurists throughout much of the 20th century” prohibited litigation investment. *Id.* The traditional view was “encapsulated succinctly in an 1850 law lecture by Abraham Lincoln: ‘Never stir up litigation. A worse man can scarcely be found than one who does this.’” *Id.*

49. *See* Jeremy Kidd, *To Fund or Not to Fund: The Need for Second-Best Solutions to the Litigation Finance Dilemma*, 8 J.L. ECON. & POL’Y 613, 627-31 (2012).

50. *See, e.g.*, LESTER BRICKMAN ET AL., RETHINKING CONTINGENCY FEES 24-28 (1994); JEFFREY O’CONNELL, THE LAWSUIT LOTTERY 8-28 (1979).

do not directly share in the recoveries of their clients.<sup>51</sup> The key assumption shared by the consequentialist argument against litigation investment and the consequentialist argument against the contingent fee is that persons who seek to maximize their return on investment in litigation will not select claims based on their merit—or social value—but on their expected return as an investment. Further, some persons who seek to maximize their return on investment in litigation will either unconsciously or deliberately make legal claims that are invalid.<sup>52</sup> It does not matter at this point in the argument why it is rational for investors in claims to put forward invalid claims; it may be that the legal system is incapable of identifying invalid claims, or that even if the legal system is capable of identifying them in theory, in practice it will not because the relevant “transaction costs” are so high that it is cheaper for defendants to settle (that is, to pay a portion) of a zero-value claim than to defeat a zero-value claim on the merits.<sup>53</sup>

A variant of the consequentialist argument is that self-interested third parties will exploit vulnerable claimholders, taking from them a huge portion of their expected recovery in their litigation in exchange for a paltry amount.<sup>54</sup> This version of the consequentialist

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51. See, e.g., David E. Bernstein, *Procedural Tort Reform: Lessons from Other Nations*, 19 REG. 71, 79 (1996) (arguing that the contingent fee “encourages attorneys to engage in speculative litigation in the hopes of landing the occasional large jackpot”); LAWRENCE J. MCQUILLAN ET AL., PAC. RESEARCH INST., JACKPOT JUSTICE: THE TRUE COST OF AMERICA’S TORT SYSTEM 26-28 (2007), available at <http://perma.cc/Z7U7-9SGX>.

52. See Kidd, *supra* note 49, at 630; Geoffrey J. Lysaught & D. Scott Hazelgrove, *Economic Implications of Third-Party Litigation Financing on the U.S. Civil Justice System*, 8 J.L. ECON. & POL’Y 645, 662-65 (2012).

53. See Frank B. Cross, *Tort Law and the American Economy*, 96 MINN. L. REV. 28, 37 (2011) (“Defendants may choose to settle wholly illegitimate claims simply because the costs of litigation exceeded the settlement payments.”).

54. “[T]he main justification for [litigation investment] is that the practice is ‘proconsumer,’ but the reality is that [it] benefits only one group of people—the investors—and it does so at the expense of all the other parties involved in litigation.” *Public Policy Implications of Lawsuit Lending and Its Effects on the Civil Justice System: Hearing Before the H. Comm. on Judiciary & Civil Jurisprudence*, 2012 Leg., 82d Sess. (Tex. 2012) (testimony of John H. Beisner, Skadden, Arps, Slate, Meagher & Flom LLP on behalf of the U.S. Chamber Institute for Legal Reform); see General Thurbert Baker, *Paying to Play: Inside The Ethics and Implications of Third-Party Litigation Funding*, 23 WIDENER L.J. 229, 232 (2013) (state attorney generals need to recognize “the anti-consumer nature of these financial products”); Martin J. Estevao, Note, *The Litigation Financing Industry: Regulation to Protect and Inform Consumers*, 84 U. COLO. L. REV. 467, 468-69 (2013); see also Jenna Wims Hashway, *Litigation Loansharks: A History of Litigation Lending and a Proposal to Bring*

argument is made almost exclusively against consumer litigation investment, and is really a form of paternalism. This argument is the same one that has been made to support state-imposed limitations on various self-regarding actions in the marketplace, such as minimum wage and maximum hour legislation, or limitations on subprime mortgages and payday lending.<sup>55</sup> Jeremy Bentham was one of the first to observe the family resemblance between the paternalistic laws prohibiting usury and champerty.<sup>56</sup> In the case of litigation investment, the paternalistic argument is worth considering only if unrestricted sale of litigation proceeds by competent and fully informed adults leads, as an empirical matter, to the destitution of the seller. Even then, as John Stuart Mill would point out, it is not clear why—unless the burden of the consequent destitution impacts the seller's family or society—the state should step in to interfere with the seller's freedom to make financially unsound deals.<sup>57</sup> Given that even the first stage of the paternalistic argument has not been established—other than by anecdote—it is like the first consequentialist argument, more often settled by appeals to other factors, such as those I will discuss below.

## 2. *The Perfectionist Critique*

The perfectionist argument endeavors to avoid making predictions about the economic effects of litigation investment. Instead, the argument takes the position that litigation investment must be prohibited because it is inconsistent with certain deontological principles, and that (to take but one variation of this argument)

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*Litigation Advances Within the Protection of Usury Laws*, 17 ROGER WILLIAMS U. L. REV. 750, 751 (2012).

55. At various times litigation investment has been compared to usury, subprime lending, and payday lending. See Richard L. Abel, *How the Plaintiffs' Bar Bars Plaintiffs*, 51 N.Y.L. SCH. L. REV. 345, 366 (2007) (describing payday lending); Susan Lorde Martin, *Litigation Financing: Another Subprime Industry That Has a Place in the United States Market*, 53 VILL. L. REV. 83, 83-85 (2008) (detailing subprime lending); Julia H. McLaughlin, *Litigation Funding: Charting a Legal and Ethical Course*, 31 VT. L. REV. 615, 637-38 (2007) (describing usury).

56. 3 JEREMY BENTHAM, LETTER XII (1787), reprinted in THE WORKS OF JEREMY BENTHAM 19-20 (John Bowring ed., 1843).

57. See JOHN STUART MILL, ON LIBERTY 148-49 (Gertrude Himmelfarb ed., Penguin Books 1982) (1859).

litigants should be prevented from debasing themselves by selling their proceeds, or (to take another variation) society should not be allowed to develop the view that legal rights are just another commodity that can be bought and sold.<sup>58</sup> As W. Bradley Wendel has noted, the most promising line of argument that does not rely on reference to the internal norms of law itself—which I will discuss below under the rubric of the rule-of-law argument—depends on the sort of anti-commodification arguments made by neo-Aristotelians like Elizabeth Anderson and Michael Sandel.<sup>59</sup>

Perfectionism can take different forms. “Human nature” perfectionism takes the development of human nature in its objective form to be a moral requirement.<sup>60</sup> It follows from this position that it is both right and good for the state to prevent individuals from acting in ways that are broadly speaking, irrational or, more narrowly, contradict their ideal rational selves. A problem with human nature perfectionism is that without a robust theory of human reason, it seems not only somewhat arbitrary (why should *human* nature matter so much?) but also question-begging (how can we distinguish right reason from mere appetite?).<sup>61</sup>

In the alternative, perfectionism can focus on a specified list of objective goods with the perfection of human nature being instrumental to their achievement.<sup>62</sup> “Objective goods” perfectionism finds widespread support when there is near universal consensus on the attractiveness of certain goods, such as art or health, and the patent irrationality of other goods, such as self-debasement or pain.<sup>63</sup> Outside a small set of clear cases, objective goods perfectionism trades a bit on a form of consequentialism. If people seem to prefer their own pleasure over items that others deem objectively good, why should the state prefer the latter over the former? Critics of

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58. See W. Bradley Wendel, *Alternative Litigation Finance and Anti-Commodification Norms*, 63 DEPAUL L. REV. 655, 656-57 (2014).

59. See, e.g., ELIZABETH ANDERSON, *VALUE IN ETHICS AND ECONOMICS* 195-216 (1993); MICHAEL SANDEL, *WHAT MONEY CAN'T BUY: THE MORAL LIMITS OF MARKETS* (2012); see also Cass R. Sunstein, *Incommensurability and Valuation in Law*, 92 MICH. L. REV. 779, 784 (1994) (“Different kinds of valuation cannot without significant loss be reduced to a single ‘superconcept,’ like happiness, utility, or pleasure.”).

60. See THOMAS HURKA, *PERFECTIONISM* 9-10 (1993).

61. See DEREK PARFIT, *REASONS AND PERSONS* 160-61 (1984).

62. See JOHN RAWLS, *A THEORY OF JUSTICE* 325 (1971).

63. See PARFIT, *supra* note 61, at 161-62; RAWLS, *supra* note 62, at 325.



perfectionism suspect that subjective tastes, which are just expressions of revulsion or disgust, do the work of sorting out which objective goods have priority over others.<sup>64</sup> The objective goods perfectionist response is that it is a category error to think that there is a simple priority or “master value” under which all human goods fall, and that Bentham was wrong to claim that pushpin is as valuable as poetry.<sup>65</sup>

Michael Walzer developed and supported his theory of “complex equality” on the various “blocked exchanges” he observed around him.<sup>66</sup> For example, he noted that almost all modern societies either prevented or would not honor contracts to purchase public office, public honors, children, et cetera.<sup>67</sup> Walzer makes a strong case that as a formal matter, there are incommensurable goods, *and that for this reason*, the state is justified in preventing people from using money to distribute those goods.<sup>68</sup> He does not provide much of a test for determining which goods, as he puts it, are the ones that “money can buy”; he relies to a certain degree on moral anthropology.<sup>69</sup>

Michael Sandel, who builds on Walzer’s argument, embraces the moral anthropology implicit in his version of perfectionism.<sup>70</sup> He, too, makes his argument by pointing out the many instances when society feels uncomfortable allowing the market to govern the distribution of goods.<sup>71</sup> His general point, while the same as Walzer’s main point, is built less by irrefutable example and more by accretion. Whereas Walzer held up certain goods that clearly should stay outside the market, Sandel’s goods are designed to induce some ambivalence. For example, is it really self-evident that people should not be allowed to purchase short-cuts through immigration

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64. See Jeremy Waldron, *Autonomy and Perfectionism in Raz’s Morality of Freedom*, 62 S. CAL. L. REV. 1097, 1145-46 (1989).

65. See JEREMY BENTHAM, *THE RATIONALE OF REWARD* (1825), *reprinted in* THE CLASSICAL UTILITARIANS: BENTHAM AND MILL 94, 94 (John Troyer ed., 2003); MICHAEL WALZER, *SPHERES OF JUSTICE* 8 (1983).

66. WALZER, *supra* note 65, at 95-103.

67. *Id.*

68. *See id.*

69. *Id.* at 103.

70. See Jeremy Waldron, *Where Money & Markets Don’t Belong*, 59 N.Y. REV. BOOKS 65, 65-66 (2012).

71. *Id.*

and customs lines in the airport or better access to health care through “concierge doctors”?<sup>72</sup> Sandel’s argument is not that any one of these market incursions into a previously nonmarket sphere of activity is wrong in itself, but rather that the accumulation of market incursions can destroy the vocabulary of nonmonetary value theory, which perfectionism both identifies and endorses.<sup>73</sup> Sandel argues that “markets change the character of the goods and social practices they govern.”<sup>74</sup> Sandel’s “crowding-out” argument provides an answer to the Millian who sees no basis in the “Harm Principle” for preventing activities which are apparently wholly self-regarding. Sandel argues that wholly self-regarding acts do not exist because our shared noneconomic value system is a public good, which if available to be enjoyed by one, is by necessity enjoyed by all, and vice-versa: its rejection even by a few of us limits its availability to everyone else.<sup>75</sup> Of course, it is incumbent on the advocate of perfectionism at the social level, like Sandel, to explain why certain private acts may be prevented in the name of the preservation of shared social attitudes, but others are not.

The perfectionist critique of litigation investment must be based on the claim that litigation is a sphere of activity in which commodification is especially dangerous. It would resemble in form, therefore, the claim that a market in *judicial outcomes* is wrong.<sup>76</sup> But the reason we intuitively understand the commodification of judging to be a synonym for “corruption” is not only because money is exchanged in its doing—that is too simplistic a test—but because in addition to money changing hands, we see that there is something amiss with a judge making a decision for a citizen that paid the most money. In other words, it is more like Walzer’s argument about separate spheres with their own metrics of value than Sandel’s argument that allowing markets in this one area might be the straw that breaks the camel’s back. Legal judgment is about the meaning of law and the weight of the facts. The amount of money

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72. SANDEL, *supra* note 59, at 3, 19.

73. *Id.* at 93-130 (discussing how markets crowd out morals).

74. *Id.* at 120.

75. *Id.* at 120-21, 23.

76. See, e.g., Ian Ayres, *The Twin Faces of Judicial Corruption: Extortion and Bribery*, 74 DENV. U. L. REV. 1231, 1232 (1997) (explaining how judicial corruption presents problems for the “convicted payor,” “acquitted payor,” and “convicted non-payor”).

offered by a party to the legal dispute is simply irrelevant to the question the judge is supposed to answer. Stated that way, the answer as to why an auction of judicial authority is unacceptable is relatively easy to state: a judicial judgment is supposed to be based on legal reasons *and nothing else*. To add a new reason—especially a supervening reason—based on financial self-interest, friendship, or loyalty to family is to make a mistake about the kind of reasons that should count in civil litigation.<sup>77</sup>

### 3. *The Rule-of-Law Critique*

By analogizing the perfectionist critique of litigation investment to the argument against selling judicial authority, we can see that a promising avenue of argument is that litigation investment introduces the wrong sort of reasons into the legal system. As a result, the parties' outcomes diverge from what the law should ideally produce. This is different from the perfectionist arguments put forward by Sandel and Walzer. It is an argument that law is a special kind of reasoning which litigation investment will disrupt. This Article calls this the "rule-of-law" argument against litigation investment. The idea that legal reasoning is different in kind from other forms of reasoning is not in itself radical.<sup>78</sup> The rule-of-law critique takes a further step to say that participants in litigation must be shielded from nonlawyer influence when there is litigation investment. According to the rule-of-law critique, clients must be shielded from nonlawyer influence in the formation of legal advice *even if they want it* and, by extension, the court must be protected from the effects that flow from the nonlawyer's influence on the client.

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77. The argument that judicial judgments should be based solely on legal reasons is equally forceful in arguments against judges basing their decisions on their political preferences or personal moral beliefs. For a version of this argument applied persuasively to support limitations on arbitration waivers in discrimination cases, see David Horton, *Arbitration and Inalienability: A Critique of the Vindication of Rights Doctrine*, 60 U. KAN. L. REV. 723, 745-65 (2012) (drawing on inalienability theory to "recalibrate the vindication of rights doctrine").

78. This is a version of the "core values" position in legal ethics. See Bruce A. Green, *The Disciplinary Restrictions on Multidisciplinary Practice: Their Derivation, Their Development, and Some Implications for the Core Values Debate*, 84 MINN. L. REV. 1115, 1145-48 (2000) (describing the six premises upon which the "core values rationale" relies).

The rule-of-law critique is different from any of the perfectionist arguments because although it is normative, it does not have to be rooted in the controversial metaethical naturalism that perfectionism (arguably) must assume.<sup>79</sup> One can make an argument about what “our” legal system requires and remain neutral not only on the question of what is good for all people, but even on the question of whether legality must be the same for all people. Rule-of-law arguments can be based on the kind of familiar scholarship produced by Blackstone and Holmes when they wrote about the common law—they claimed to be doing nothing more than describing the essential features of our legal system, conceding, at least implicitly, that at the most fundamental level these features were ultimately contingent.<sup>80</sup>

The basic structure of the rule-of-law argument is this: (1) the common law is characterized by features *a, b, c, d ... z*; (2) litigation investment tends to weaken one of those features (for example, *b*); (3) if a litigation investment transaction would weaken *b*, public policy requires that courts refuse to recognize the transaction. Barring that, legislatures should prohibit litigation investment transactions that would result in the loss of *b*, either through voluntary agreement or by operation of law. This Article suggests that for critics of litigation investment, transfer of control is like example *b*—an essential feature of litigation whose loss would change the very character of the practice.<sup>81</sup> As we will see, there are subsidiary rule-of-law arguments against litigation investment, such as the need for transparency before the court, or the rule of standing that requires the real party in interest to be before the court. These will be dealt with as elaborations on the original argument—that party control is an essential feature of the rule of law in common law adjudication.

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79. See generally Richard Rowland, *Moral Error Theory and the Argument from Epistemic Reasons*, 7 J. ETHICS & SOC. PHIL. 1 (2013) (discussing arguments against metaethical naturalism).

80. See generally BLACKSTONE, *supra* note 45; OLIVER WENDELL HOLMES, JR., *THE COMMON LAW* (1881).

81. JOHN H. BEISNER & GARY A. RUBIN, U.S. CHAMBER INST. FOR LEGAL REFORM, STOPPING THE SALE ON LAWSUITS: A PROPOSAL TO REGULATE THIRD-PARTY INVESTMENTS IN LITIGATION 1 (2012), available at <http://perma.cc/8KFQ-994M> (discussing how litigation investment “undercuts plaintiff and lawyer control over litigation”).

## II. THE RULE-OF-LAW CRITIQUE OF LITIGATION INVESTMENT

If taken at face value, the rule-of-law critique is a claim about the essential elements of common law adjudication.<sup>82</sup> According to those who embrace it, litigation investment “threatens to compromise the integrity of the U.S. judicial system.”<sup>83</sup> How exactly does litigation investment undermine the integrity of the judicial system? There are three subsidiary arguments that compose the party control argument. These are: (1) interference with the lawyer-client relationship; (2) interference with the plaintiff-defendant relationship; and (3) interference with the party-court relationship. Critics of litigation investment have claimed that the control granted to third parties in litigation investment either destroys or impermissibly complicates these relations, and that the cumulative effect of the episodes of interference that occur as a result distorts the legal system to the point where it no longer serves its fundamental rule-of-law function.<sup>84</sup> The purpose of this Part is to demonstrate that in each of these relations the common law has already permitted parties to alienate their control by contract. This Part will briefly explain why uncovering this contradiction matters. It matters because each of the following subsidiary rule-of-law arguments assumes that party control is necessary for the success of some aspect of tort or insurance law. This set of assumptions is false.

### *A. Interference with the Lawyer-Client Relationship*

The chief concern by those who raise rule-of-law objections to litigation investment is that it will interfere with the relationship between the party who has the claim and her lawyer. The Institute for Legal Reform has argued that litigation investment “undercuts plaintiff and lawyer control over litigation because the [litigation investment] company, as an investor in the plaintiff’s lawsuit,

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82. Rule-of-law arguments are, therefore, similar to what Fuller called “the internal morality of law.” See LON L. FULLER, *THE MORALITY OF LAW* 153 (2d ed. 1969).

83. Letter from U.S. Chamber Inst. for Legal Reform to ABA Comm’n on Ethics 20/20 (Feb. 15, 2011), in *Comments: Alternative Litigation Financing Working Group Issues Paper*, A.B.A., at 136, 139, available at <http://perma.cc/5C7V-K56T>.

84. See, e.g., Sebok, *supra* note 5, at 2949-52.

presumably will seek to protect its investment, and can therefore be expected to try to exert control over the plaintiff's and counsel's strategic decisions."<sup>85</sup> This concern is echoed by those who worry about whether an attorney can fulfill her ethical obligations in a case in which her client has signed a litigation investment contract.<sup>86</sup>

There are two very different arguments being made here. The first is that litigation investment contracts may require lawyers to violate ethical obligations to their clients. The second is that even if a lawyer can ethically represent a client who has contractual obligations to a litigation investor, the relationship between the lawyer and the client will be affected in a way that somehow interferes with the operation of the common law.<sup>87</sup> The first argument has been discussed most recently in a report published by the American Bar Association Commission on Ethics 20/20 and an opinion of the New York City Bar Association.<sup>88</sup> Both report that an attorney is not necessarily prohibited by the rules of professional responsibility from representing a client who wishes to make a contract with a litigation investment firm.<sup>89</sup> The second argument has received less attention.

As will be demonstrated in Part III of this Article, the common law permits parties to alienate control over litigation of their claims

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85. BEISNER & RUBIN, *supra* note 81, at 2.

86. *See, e.g.*, Me. Bd. of Overseers of the Bar Prof'l Ethics Comm'n, Op. 191 (2006), available at <http://perma.cc/VGA2-MCFH> ("[T]he lawyer must guard against any risk that the financing company will attempt to control the litigation or otherwise interfere with the lawyer's exercise of professional judgment."); State Bar of Mich. Standing Comm. on Prof'l & Judicial Ethics, Op. RI-321 (2000), available at 2000 WL 33716933 (concluding litigation investments contracts create an impermissible conflict of interest for the lawyer); *see also* McLaughlin, *supra* note 55, at 651 ("[Litigation investment contracts] threaten to undermine the duty of loyalty owed to a client by creating a contractual relationship with a third party.").

87. On this second argument, *see, for example*, BEISNER & RUBIN, *supra* note 81, at 15:

In order for American businesses to thrive, we need a reliable, predictable judicial system whose judgments all of us—plaintiffs, defendants, consumers, businesses—trust as impartial. [Third-party litigation financing] is antithetical to the free enterprise system because it allows private parties to subject businesses involuntarily to the coercive effects of our litigation system, all for the purpose of profit.

88. *See* ABA COMM'N ON ETHICS 20/20, INFORMATIONAL REPORT TO THE HOUSE OF DELEGATES (Dec. 27, 2011), available at <http://perma.cc/W6UL-F2YB>; Ass'n of the Bar of the City of N.Y. Comm. on Prof'l Ethics, *supra* note 1.

89. *See* Anthony J. Sebok, *Litigation Investment and Legal Ethics: What are the Real Issues?*, 55 CAN. BUS. L.J. 111, 123-26 (2014).

to third parties in numerous contexts: assignment, subrogation, and third-party liability contract. In the case of assignment, discussed in Part III.B, the original claimholder and her attorney (if there had been one) are fully substituted by another party with new representation; even if it is the same lawyer, the retainer is between the new party and the lawyer. So the common law's embrace of assignment (which, while not complete, is quite advanced) says nothing pro or con about the argument made against litigation investment with regard to its interference with the lawyer-client relationship. In subrogation and liability insurance, however, the relationship between the party and her lawyer is identical to that of the claimholder and her lawyer in the litigation investment contract.<sup>90</sup> Yet courts have upheld contracts in cases of subrogation and liability insurance, and rejected arguments that they are unenforceable because the insurer's control supplants the insured's power over her own case.

The concern that critics express about the relationship between the claimholder and her attorney in litigation investment reflects a similar confusion that insurance law scholars identified among those who once argued against allowing lawyers to represent insurers as well as insureds in the third-party liability insurance context.<sup>91</sup> The fear was that if a lawyer was permitted to jointly represent both the insurer and the insured in litigation and the insurer has the right to control under the insurance contract, the lawyer cannot in advance obtain adequate consent from the insured to prevent a conflict of interest if the insured and insurer come to disagree on the conduct of the insured's defense.<sup>92</sup> The reason this is not a real dilemma is twofold.

First, the insured can order the lawyer, as her agent, to accept instructions from other persons, including the insurer, and in fact, the insured may be obliged under the insurance contract to issue such instructions.<sup>93</sup> Second, if the insurer and the insured disagree

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90. See *infra* Part III.C-D.

91. See Stephen L. Pepper, *Applying the Fundamentals of Lawyers' Ethics to Insurance Defense Practice*, 4 CONN. INS. L.J. 27, 28 (1997).

92. *Id.* at 50.

93. Fischer, *supra* note 11, at 27 ("[T]he lawyer, in representing the policyholder, should, as the policy holder's designee accept direction from the insurer, for the claim's defense to the extent the insurer is responsible for the consequences, such as when the claim is likely to be

with each other about the best way to litigate the claim and whether the insured's instructions to the lawyer to obey the insurer are still in force, the lawyer's obligation is clear: the lawyer must either obtain a conflict waiver from both parties, or if that is impossible, withdraw from representation of one or both parties.<sup>94</sup> If the insured comes to regret her promise to the insurer, her remedy is in contract. She can always breach the contract and defend at her own expense using any attorney she chooses.<sup>95</sup> The insurer cannot use the insurance contract to order the lawyer to be disloyal to the insured. What the insurer *can* do (and this is perhaps what really upsets the critics of dual representation) is make it very expensive for the insured to regain the freedom to tell her attorney to do things to which the insurer is opposed.<sup>96</sup> The same is true in litigation investment: the same duty of loyalty that exists between the insured and her attorney exists between the claimholder and her attorney. If the claimholder breaks with the investor for any reason, her remedy is governed under the litigation investment contract. Her relationship with her attorney cannot be "interfered with" by the investor, even though the cost of regaining the freedom to tell one's attorney to do things to which the investor is opposed may be very high.<sup>97</sup> But that is an artifact of the terms of the contract between the client and the investor—and the ability of the investor to enforce the contract. It does not flow from the idea that party control is an essential feature of the common law.

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resolved within the policy's limits.").

94. See Ellen S. Pryor & Charles Silver, *Defense Lawyers' Professional Responsibilities: Part I—Excess Exposure Cases*, 78 TEX. L. REV. 599, 636 (2000) ("The proper understanding, then, is that a carrier possesses the right to control the defense, that a disagreement with an insured does not divest a carrier of this right, but that in a conflict situation a defense lawyer cannot follow a carrier's instructions without the informed consent of the insured.").

95. *Id.* at 639-40.

96. See *id.* at 638-39.

97. The price will vary according to the terms of the contract and the background contract doctrines that set the baseline duties and remedies between the claimholder and the funder. See generally Sebok & Wendel, *supra* note 13.



*B. Interference with the Plaintiff-Defendant Relationship*

Some critics have argued that litigation investment interferes with the relationship between the claimholder and the party she is suing. The Institute for Legal Reform has argued that

[t]he pernicious effect on defendants is clear: because [litigation investment] agreements are typically made under a “veil of secrecy,” a defendant facing a claim funded by [litigation investment] may not even realize who is guiding litigation strategy and decisions on the other side, making it unfairly difficult to mount an adequate defense.<sup>98</sup>

In *Weaver, Bennett & Bland v. Speedy Bucks, Inc.*, a plaintiff’s lawyer alleged that an investor, Speedy Bucks, intentionally induced the lawyer’s client to refuse a reasonable settlement offer, against her attorney’s advice, and worse, did so in secret because the lawyer did not know that the client had taken money from the investor.<sup>99</sup>

As we will see in the discussion of the law of subrogation in Part III.C, courts have enforced contracts that transfer party control in litigation to insurers and have concluded that the question of *who* is in control of the litigation may remain hidden from the factfinder and the court, unless some independent wrong is alleged, such as the promotion of perjury, the concealment of assets, or some form of tortious interference. I will argue that the same rule-of-law concerns are at stake in the transfer of party control in subrogation and litigation investment, and the rule in the former should be the rule in the latter.

In liability insurance, one of the risks that arises from transferring control is not, as is alleged in the case of litigation investment, that settlement will not happen, but that settlement will happen too easily and against the strong objections of the insured. The story of how courts dealt with this risk by imposing the duty to settle on

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98. BEISNER & RUBIN, *supra* note 81, at 14.

99. 162 F. Supp. 2d 448 (W.D.N.C. 2001); *see* McLaughlin, *supra* note 55, at 641 (stating that in *Weaver*, “the litigation-funding companies secretly and wrongfully advanced \$200,000” to the client); *see also* Tiger Joyce, *Shining a Light on the Lawsuit Loan Industry*, METROPOLITAN CORP. COUNS., July 2011, at 5, *available at* <http://perma.cc/HGF3-J27L> (citing *Weaver* as an example of how litigation finance distorts litigation).

insurers and expanding the duty to defend is one of remarkable responsiveness on the part of the law to the needs of society, but it is important to remember that courts did not eliminate *all* the risks faced by an insurance consumer who transfers party control in exchange for coverage.<sup>100</sup> This is the point of the discussion of the so-called “full coverage” cases in Part III.D. The fact that in third-party insurance the party who cedes control may have more faith in her *defense* than her insurer has, and that in litigation investment the party who cedes control may have more faith in her *claim* than her investor has, is a distinction without a difference from a rule-of-law point of view. In both cases, control over such things as whether to go to trial is being sold for a price to a stranger, albeit for different reasons.<sup>101</sup> The underlying rationale for adopting a liberal attitude in both cases—that the common law should allow such transactions barring strong countervailing public policy reasons—is the same.

### *C. Interference with the Party-Court Relationship*

Some critics have focused on the rule-of-law concern that litigation investment interferes with the relationship between the claimholder and the court. For example, in *American Optical Co. v. Curtiss*, a party who, for its own reasons, did not want to enforce a patent was approached by another party who wished to deprive the patent infringer of its market, and who offered to take an assignment of the patent and bring an infringement suit, which that party

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100. See Leo P. Martinez, *Classic Insurance Law in a Postmodern World*, 2 NEV. L.J. 403, 410-14 (2002) (discussing the expansion of the duty to defend); Kent D. Syverud, *The Duty to Settle*, 76 VA. L. REV. 1113, 1117 (1990) (discussing the expansion of the duty to settle). These pro-insured developments were clearly motivated by a number of factors, but it is important to acknowledge the influence of the idea that insurance contracts should be interpreted differently from other contracts. This was the legacy of Robert Keeton's argument for employing the doctrine of reasonable expectations in insurance contract interpretation. See Roger C. Henderson, *The Doctrine of Reasonable Expectations in Insurance Law After Two Decades*, 51 OHIO ST. L.J. 823, 823-26 (1990); Roger C. Henderson, *The Formulation of the Doctrine of Reasonable Expectations and the Influence of Forces Outside Insurance Law*, 5 CONN. INS. L.J. 69, 73-74 (1998). See generally Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961 (1970).

101. *But see* Boardman, *supra* note 11, at 682-83 (explaining that the difference between the insurer's and a funder's motivation to purchase control makes it impossible to draw useful parallels between the two).

would fund and control.<sup>102</sup> The court held that the contract violated New York's public policy because it was a "contrivance" designed to allow a stranger to profit by pretending to the court that it was the real party in interest.<sup>103</sup> Stephen Presser has argued that from the earliest years, the "Blackstonian hostility to third parties becoming involved in lawsuits," had to do with the sense that "the third-party funder is anonymous ... [using] secret influence" that "amounts to 'fraudulent interference.'"<sup>104</sup>

The argument that the rule of law is violated because litigation investment allows third parties to conceal their "real" interest from the court warrants two different answers. First, as the discussion of subrogation in Part III.C demonstrates, the common law has enforced contracts that are explicitly designed to conceal the true identity of the party in interest from the jury (although probably not the judge). Second, to the extent that this is a genuine concern, it is not obvious that litigation investment requires opacity at all. Unlike subrogation, in which the concealment of the identity of the benefitted party is a major benefit—if not the central goal—of the insurer, it is not clear that litigation investment funders need to keep their involvement secret from adverse parties, the courts, or even juries.<sup>105</sup>

### III. LOSS OF PARTY CONTROL IN TORT AND INSURANCE LAW

Part II presented the rule-of-law critique of litigation investment based on the centrality of party control. The central thesis of this Article is that the idea that party control is central to the common law is a myth. By knocking down this myth, I hope to show that

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102. 56 F.R.D. 26, 27-29 (S.D.N.Y. 1971).

103. *Id.* at 30.

104. Stephen B. Presser, A Tale of Two Models: Third Party Litigation in Historical and Ideological Perspective 9 (Sept. 2009) (unpublished manuscript) (on file with author).

105. In Australia, for example, IMF, the leading litigation investment firm in that market, advocates full, public, and mandatory disclosure of funding agreements. Kalajdzic et al., *supra* note 33, at 123. It is an open question in the United States whether the existence and content of funding agreements are discoverable and under what circumstances the agreements are discoverable. See *Miller UK Ltd. v. Caterpillar, Inc.*, 17 F. Supp. 3d 711, 721-24 (N.D. Ill. 2014) (expressing skepticism that "deal documents" are relevant under the Federal Rules of Evidence). For an argument that mandatory disclosure of the existence of funding may benefit plaintiffs and defendants, see Ronen Avraham & Abraham L. Wickelgren, *Third-Party Litigation Funding—A Signaling Model*, 63 DEPAUL L. REV. 233, 235 (2014).

there is no reason to fear that litigation investment will open the door to litigation led by nonlawyers lacking any commitment to the core values of the legal system. The following sections demonstrate that the alienation of party control is a common feature of tort and insurance law. The larger question that this Part will leave for the Conclusion is what we can learn from the variety of ways in which the courts have allowed control to be alienated, abandoned, and contracted away. But before this larger question can be adequately addressed, the degree to which control is much more fluid than the critics of litigation investment seem to realize must be demonstrated in detail.

#### *A. Introduction: How to Lose Control*

There are many ways that parties can transfer control in litigation. The most familiar is assignment, by which a party transfers the entire cause of action to a new party and, by extension, full control as well as a legal right in whatever is gained in the outcome, whether it is damages, property rights, or an injunction.<sup>106</sup> Related to assignment is contractual subrogation. A contractual subrogee is a stranger to a wrong who pays the victim for the victim's injury and then gains the right to receive repayment from the defendant based on the victim's rights, often by enforcing those rights.<sup>107</sup> However, as will be illustrated in greater detail below, there are significant differences between assignment and subrogation. Finally, a party can by simple contract agree to accept the instructions of the promisor with regard to litigation involving the promise.<sup>108</sup> The sorts of promises that could be made are limited only by the imagination of the contract drafters and the law. For

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106. 6 AM. JUR. 2D *Assignments* § 1 (2014). Jeffrey O'Connell noted that there was no logical reason why the doctrine of assignment did not include the possibility that a legal claim—even a claim for a personal injury—could be transferred to a complete stranger, such as a first-party insurer. See, e.g., Jeffrey O'Connell, *Harnessing the Liability Lottery: Elective First-Party No-Fault Insurance Financed by Third-Party Tort Claims*, 1978 WASH. U. L.Q. 693; Jeffrey O'Connell, *Transferring Injured Victims' Tort Rights to No-Fault Insurers: New "Sole Remedy" Approaches to Cure Liability Insurance Ills*, 1977 U. ILL. L. REV. 749, 775-93; see also Jeffrey O'Connell & Craig Brown, *A Canadian Proposal for No-Fault Benefits Financed by Assignment of Tort Rights*, 33 U. TORONTO L.J. 434 (1983).

107. See 59 AM. JUR. 2D *Parties* § 184 (2014).

108. See 17A AM. JUR. 2D *Contracts* § 1 (2014).

example, one could imagine an asbestos producer desperate for capital promising a bank that in exchange for a loan, the bank would have the right to instruct the asbestos producer on every detail of its mass tort litigation. Curiously, there seems to be very little evidence that covenants concerning control of litigation are explicitly built into commercial contracts *ex ante*.<sup>109</sup> That is, however, with one exception: almost every contract for liability insurance demands from the insured that it cede control of litigation in which it is a defendant to the insurer in exchange for a promise of coverage.<sup>110</sup>

### *B. Assignment*

#### *1. The History of Limitations on the Assignment of Choses of Action*

An assignment is the act of transferring all or part of one's property, interest, or rights to another.<sup>111</sup> The early common law prohibited all assignments of choses of action, regardless of whether they were based in contract, property, or tort.<sup>112</sup> This prohibition was relaxed until, as one court put it in 1947, "assignability of things [in action] is now the rule; non-assignability, the exception; and this exception is confined to wrongs done to the person, the reputation, or the feelings of the injured party."<sup>113</sup>

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109. This is not to say that lenders never take control over the management of an enterprise. Lenders can control decisions that affect ongoing or possible litigation, such as when creditors take control during bankruptcy proceedings. The same might be said of investors who receive special forms of equity that give them control over certain management decisions. See Selwyn Seidel, *Time to Pass the Baton*, COM. DISP. RESOL. 47, 48 (Nov.-Dec. 2012).

110. Charles Silver has argued that liability insurance and litigation funding "evolved independently but have similar structures and functions." Charles Silver, *Litigation Funding Versus Liability Insurance: What's the Difference?*, 63 DEPAUL L. REV. 617, 618-19; see also Michele DeStefano, *Nonlawyers Influencing Lawyers: Too Many Cooks in the Kitchen or Stone Soup?*, 80 FORDHAM L. REV. 2791, 2839 (2012) (comparing the control that liability insurers currently exercise over their policyholder's litigation with the control that critics of litigation investment fear funders demand by contract); Steinitz, *supra* note 25, at 1333 (making the same comparison as DeStefano, *supra*).

111. 6 AM. JUR. 2D *Assignments* § 1 (2014).

112. See *Webb v. Pillsbury*, 144 P.2d 1, 3 (Cal. 1943).

113. *Id.* (quoting 3 CAL. JUR. *Assignments* § 5 (1921)). In addition, most states will not permit the assignment of breach of contract claims that are "purely personal in nature," such

Today, the original common law rule of non-assignability has been almost fully abandoned.<sup>114</sup> However, exceptions do persist. Someone with a cause of action for a personal injury is barred in almost all parts of the United States from assigning it to a stranger.<sup>115</sup> This is based on the common law maxim *actio personalis moritur cum persona* (“a personal cause of action dies with the person”).<sup>116</sup> The original theory of *actio personalis* cannot be said to play much of a role in the common law since the advent of survivorship statutes in the nineteenth century; it goes without saying that tort claims now survive the death of the plaintiff and can be maintained by a set of persons named in the statute, usually members of the plaintiff’s family.<sup>117</sup>

Prior to the nineteenth century, common law courts embraced the “doctrine of the non-assignability of choses in action” and prohibited the assignment of *any* suit for damages in property, contract, or

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as promises of marriage. 6 AM. JUR. 2D *Assignments* § 52 (2010).

114. See, e.g., *Osuna v. Albertson*, 184 Cal. Rptr. 338, 345 (Ct. App. 1982) (“[T]he tendency of modern jurisprudence strongly favors the assignability and the survivability of things in action.”); *McKenna v. Oliver*, 159 P.3d 697, 699 (Colo. App. 2006) (discussing how Colorado law generally favors the assignability of claims, with the exception being causes of action for invasion of privacy); *Conrad Bros. v. John Deere Ins. Co.*, 640 N.W.2d 231, 236 (Iowa 2001) (“[T]he law now generally favors the assignability of choses in action, and courts have permitted the assignment of insurance policies under statutes providing for the assignment of contracts in exchange for a money payment.”); *Lemley v. Pizzica*, 36 Pa. D. & C.2d 327, 330 (Ct. Com. Pl. 1964) (“The trend of judicial decisions as to the assignability of certain causes of action is to enlarge, rather than to restrict the causes that may be assigned.”); *Wis. Bankers Ass’n v. Mut. Sav. & Loan Ass’n of Wis.*, 291 N.W.2d 869, 876 (Wis. 1980) (discussing how the principle of assignability exemplifies a trend of increasing commercial flexibility shared by the courts and legislature).

115. Marc J. Shukaitis, *A Market in Personal Injury Tort Claims*, 16 J. LEGAL STUD. 329, 330 (1987). Nine states allow the assignment of personal injury claims—Delaware, Iowa, Michigan, Mississippi, New Hampshire, South Carolina, Texas, Washington, and Wyoming. Terrance Cain, *Third Party Funding of Personal Injury Tort Claims: Keep the Baby and Change the Bathwater*, 89 CHI.-KENT L. REV. 11, 23 (2014).

116. JOHN C. P. GOLDBERG ET AL., *TORT LAW: RESPONSIBILITIES AND REDRESS* 385 (3d ed. 2012). *Actio personalis* worked in both directions—the death of the tortfeasor put an end to the plaintiff’s suit also. *Id.* As Blackstone put it, “neither the [heirs of the deceased] plaintiff have received, nor those of the defendant have committed, in their own personal capacity, any manner of wrong or injury.” 3 BLACKSTONE, *supra* note 45, at \*302.

117. In 1846 the English Parliament passed Lord Campbell’s Act, which created causes of action for wrongful death and allowed designated representatives of the deceased plaintiff to maintain the plaintiff’s causes of action for personal injury; that is, it abrogated *actio personalis*. Fatal Accidents Act, 1846, 9 & 10 Vict., c. 93 (Eng.). The various states of the United States soon followed. GOLDBERG ET AL., *supra* note 116, at 388; see, e.g., *Nelson v. Dolan*, 434 N.W.2d 25, 30 (Neb. 1989) (describing the operation of a state survival statute).

tort.<sup>118</sup> A chose in action was any “personal right[] ... which can only be claimed or enforced by action, and not by taking physical possession.”<sup>119</sup> These included, according to Holdsworth, “rights to debts of all kinds, and rights of action on a contract or a right to damages for its breach; rights arising by reason of the commission of tort or other wrong; and rights to recover the ownership or possession of property real or personal.”<sup>120</sup>

The doctrine of the non-assignability of choses in action must have proven an increasingly difficult hurdle to overcome in commercial litigation. Creative lawyers and courts used legal fictions to soften its bite, such as using equity to circumvent the prohibition of the assignment of contracts.<sup>121</sup> As Holdsworth dryly noted, the common law “was induced to connive at the introduction and extension of ... evasion[s] of its principle that a *chose* in action is not assignable.”<sup>122</sup> Eventually the exceptions swallowed the rule, and over the nineteenth century, the British Parliament legislatively removed almost all limitations on the assignment of choses in action for property and contract.<sup>123</sup>

After independence, the experience in the United States was similar to that of England, except that the Americans were even more eager than the British to allow the assignment of choses of action in as many areas of law as possible.<sup>124</sup> In *Comegys v. Vasse*,

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118. EDMOND H. BODKIN, *THE LAW OF MAINTENANCE AND CHAMPERTY* 6-7 (1935).

119. *Torkington v. Magee*, [1902] 2 K.B. 427, 430 (Eng.).

120. W.S. Holdsworth, *The History of the Treatment of Choses in Action by the Common Law*, 33 HARV. L. REV. 997, 997-98 (1920).

121. *Id.* at 1021; see also *Master v. Miller*, [1791] 100 Eng. Rep. 1042, 1052 (K.B.) (Buller, J.) (“Courts of Equity from the earliest times thought the doctrine too absurd for them to adopt, and therefore they always acted in direct contradiction to it.”); Lee Aitken, “*Litigation Lending*” After Fostif: *An Advance in Consumer Protection, or a License to “Bottomfeeders,”* 28 SYDNEY L. REV. 171, 174-75 (2006) (reviewing the same history of nonassignability in courts prior to the nineteenth century).

122. Holdsworth, *supra* note 120, at 1021-22.

123. Judicature Act of 1873, 36 & 37 Vict., c. 66, § 25(6) (Eng.) (removing limitations on assignment of choses in contract); Real Property Act, 1845, 8 & 9 Vict., c. 106, § 6 (Eng.) (removing limitations on assignment of choses for land). Note that special legislation was passed as early as 1330 allowing executors and administrators to sue for trespass committed to the personal property during the decedent’s lifetime. Harold R. Weinberg, *Tort Claims as Intangible Property: An Exploration from an Assignee’s Perspective*, 64 KY. L.J. 49, 52 (1975).

124. See Walter Wheeler Cook, *The Alienability of Choses in Action*, 29 HARV. L. REV. 816, 826-29 (1916) (describing American courts’ allowance of assignment of choses of action); Radin, *supra* note 40, at 68 (observing that although Coke had argued that the same reasons prohibiting champerty prohibited assignment, American courts were happy to distinguish the

the U.S. Supreme Court regarded the doctrine of the non-assignability of choses in action with skepticism and adopted a new theory of assignments in bankruptcy that did not rely on the legal fictions developed by the English courts.<sup>125</sup> State courts followed suit. In *Rice v. Stone*, the Massachusetts Supreme Judicial Court noted that

[the] ancient doctrine [against assignment] has been greatly relaxed. Commercial paper was first made assignable to meet the necessities of commerce and trade. Courts of equity also interfered to protect assignments of various choses in action.... And at the present day claims for property and for torts done to property are generally to be regarded as assignable.<sup>126</sup>

The *Rice* court noted “two principal reasons” for why assignments of choses of action were completely prohibited in the early common law.<sup>127</sup> The first was that “[i]n early times [an assignment] was regarded as an evil principally because it would enable the rich and powerful to oppress the poor.”<sup>128</sup> The second was that under common law theory, an assignment is impossible “unless the assignor has either actually or potentially the thing which he attempts to assign.”<sup>129</sup>

## 2. Modern Permissiveness in the Law of Assignment

The first reason offered by the *Rice* court is the historical argument made by Blackstone and others against litigation investment.<sup>130</sup> It is derived from the idea that, as Lord Abinger said in *Prosser v. Edmonds*, “no encouragement should be given to litigation by the introduction of parties *to enforce those rights, which others are not disposed to enforce.*”<sup>131</sup> The precise negative consequence to society is less important than the fundamental point that uniquely bad consequences flow from giving control over legal claims to

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conditions in England from their own).

125. 26 U.S. (1 Pet.) 193, 213 (1828); see Weinberg, *supra* note 123, at 61.

126. 83 Mass. (1 Allen) 566, 568 (1861).

127. *Id.* at 569.

128. *Id.*; see Holdsworth, *supra* note 120, at 1006.

129. *Rice*, 83 Mass. (1 Allen) at 569.

130. See, e.g., 4 BLACKSTONE, *supra* note 45, at \*134-36.

131. [1835] 160 Eng. Rep. 196 (K.B.) 204 (emphasis added).



strangers. The Supreme Court of Alabama only gestured towards the dangers that free assignment of inheritance rights would produce when it prohibited such an assignment in 1857:

Some of the recent cases do indeed relax the rules [of assignment] ... but ... when fully considered, they do not go the length of breaking down the barrier which the wisdom of ages has erected against *the perversion of the course of justice*, by opening a door for strangers to come in and interfere with suits in which they have no interest.<sup>132</sup>

This may seem like an anachronistic rationale given the relatively liberal attitude towards assignment in the modern common law today, but it persists in various isolated doctrines. For example, as noted above, New York prohibits the assignment of a “thing in action, or any claim or demand, *with the intent and for the purpose of bringing an action or proceeding thereon.*”<sup>133</sup> Maryland public policy will not recognize assignments which are part of a “scheme[ ] to promote litigation for the benefit of the promoter rather than for the benefit of the litigant or the public.”<sup>134</sup> The leading case interpreting Maryland law on this point illustrates the pitfalls of trying to limit assignment in modern times.<sup>135</sup> In *Accrued Financial Services v. Prime Retail, Inc.*, a company with expertise in forensic accounting took assignments of the legal claims of commercial tenants in over fifty shopping malls and promised to remit to the assignors between fifty and sixty percent of any discrepancies discovered and paid to the company by the assignors’ landlords, some of which were in Maryland.<sup>136</sup> The Fourth Circuit held that this practice violated Maryland public policy because it “improperly,

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132. *Poe v. Davis*, 29 Ala. 676, 683 (1857) (emphasis added).

133. N.Y. JUD. LAW § 489 (2014) (emphasis added). Courts have interpreted the law to prohibit the taking of an assignment in order to profit the legal costs of enforcing the cause of action acquired, as opposed to profiting from enforcing the rights at issue in the suit. For this reason, “New York courts have rarely encountered a case in which the challenged conduct was found, as a matter of law, to constitute a violation of the statute.” *Justinian Capital SPC v. WestLB AG, N.Y. Branch*, 952 N.Y.S.2d 725, 731 (Sup. Ct. 2012) (citing *Bluebird Partners, L.P. v. First Fidelity Bank, N.A.*, 731 N.E.2d 581 (N.Y. 2000)).

134. 298 F.3d 291, 299 (4th Cir. 2002) (quoting 7 WILLISTON ON CONTRACTS § 15:4 (4th ed. 2010)).

135. *See id.*

136. *Id.* at 294.

and for the purpose of stirring up litigation and strife, encourag[ed] others either to bring actions, or to make defenses which they have no right to make.”<sup>137</sup> Virginia, along with many other states, will not recognize the assignment of legal malpractice claims.<sup>138</sup> In its decision in *MNC Credit Corp. v. Sickels*, the Supreme Court of Virginia justified this outcome on a consequentialist argument concerning the “undue burden” such assignments would place on the legal profession and “the already overburdened judicial system.”<sup>139</sup>

The second reason offered by the *Rice* court, upon examination, can be linked up to variations of the rule-of-law arguments. To take but one example, when the *Rice* court referred to a “principle of law, applicable to all assignments,” it based its argument not on a prediction about the specific social consequences that might flow from the assignment of choses in action for personal injury, but on a claim about the status of inchoate claims in the common law, and how courts should treat their purported assignment:

A claim to damages for a personal tort, before it is established by agreement or adjudication, has no value that can be so estimated as to form a proper consideration for a sale. Until it is

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137. *Id.* at 299 (citations omitted). It is ambiguous whether the claims that are made without “right” are fraudulent, frivolous and/or spurious, or defective simply because they are the result of officious intermeddling by a stranger.

138. The states that prohibit assignment of legal malpractice claims include: Arizona, *Franko v. Mitchell*, 762 P.2d 1345, 1353-54 n.1 (Ariz. Ct. App. 1988), *abrogated on other grounds by* *Paradigm Ins. Co. v. Langerman Law Offices, P.A.*, 24 P.3d 593 (Ariz. 2001); California, *Goodley v. Wank & Wank, Inc.*, 133 Cal. Rptr. 83, 86 (Ct. App. 1976); Colorado, *Roberts v. Holland & Hart*, 857 P.2d 492, 495 (Colo. App. 1993); Connecticut, *Cont'l Cas. Co. v. Pullman*, 709 F. Supp. 44, 50 (D. Conn. 1989); Florida, *KPMG Peat Marwick v. Nat'l Union Fire Ins. Co.*, 765 So. 2d 36, 38 (Fla. 2000); *Forgione v. Dennis Pirtle Agency, Inc.*, 701 So. 2d 557, 559 (Fla. 1997); Illinois, *Brocato v. Prairie State Farmers Ins. Ass'n*, 520 N.E.2d 1200, 1201 (Ill. App. Ct. 1998); Indiana, *Picadilly, Inc. v. Raikos*, 582 N.E.2d 338, 341-42 (Ind. 1991); Kansas, *Bank IV Wichita, Nat'l Ass'n v. Arn*, 827 P.2d 758, 759 (Kan. 1992); Kentucky, *Coffey v. Jefferson Cnty. Bd. of Educ.*, 756 S.W.2d 155, 157 (Ky. Ct. App. 1988); Michigan, *Joos v. Drillock*, 338 N.W.2d 736, 739 (Mich. Ct. App. 1983); Minnesota, *Wagener v. McDonald*, 509 N.W.2d 188, 190 (Minn. Ct. App. 1993); Missouri, *Scarlett v. Barnes*, 121 B.R. 578, 581 (Bankr. W.D. Mo. 1990); Nebraska, *Earth Sci. Labs., Inc. v. Adkins & Wondra, P.C.*, 523 N.W.2d 254, 257 (Neb. 1994); Nevada, *Chaffee v. Smith*, 645 P.2d 966, 966 (Nev. 1982); New Jersey, *Alcman Servs. Corp. v. Bullock, P.C.*, 925 F. Supp. 252, 258 (D.N.J. 1996), *aff'd*, 124 F.3d 185 (3d Cir. 1997); Tennessee, *Can Do, Inc. v. Manier*, 922 S.W.2d 865, 869 (Tenn. 1996); Texas, *Britton v. Seale*, 81 F.3d 602, 604 (5th Cir. 1996); and Virginia, *MNC Credit Corp. v. Sickels*, 497 S.E.2d 331, 333 (Va. 1998).

139. *MNC Credit Corp.*, 497 S.E.2d at 334 (quoting *Goodley*, 133 Cal. Rptr. at 87).

thus established, *it has no elements of property* sufficient to make it the subject of a grant or assignment.<sup>140</sup>

The court was relying on a distinction between wrongs to *vested interests*, which included chattel, real property, and contractual expectations, in contrast to violations of *personal rights*, which included assault and battery, false imprisonment, malicious prosecution, and defamation.<sup>141</sup> According to the court, the former had an existence independent of the person who brought the claim (and, presumably, whether the claim was brought at all), while the latter did not exist until the party whose right had originally been injured obtained a final judgment from a court.<sup>142</sup> This skepticism about the legal status of causes of action based on personal rights persists in the Uniform Commercial Code, which at first held that tort claims could not be treated as collateral under Article 9.<sup>143</sup> Even after significant revisions, the revised Article 9 recognizes security interests in commercial torts but not torts “arising out of personal injury to or the death of an individual.”<sup>144</sup>

Rule-of-law concerns can be seen in nineteenth-century doctrine, which endeavored to distinguish between “naked” claims in fraud (which could not be assigned) and fraud claims clothed in an ownership interest (which could be assigned).<sup>145</sup> In *Gruber v. Baker*,

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140. *Rice v. Stone*, 83 Mass. (1 Allen) 569, 570 (1861) (emphasis added).

141. *Id.* at 569-70.

142. *Id.* (“The considerations which are urged to a jury in [sic] behalf of one whose reputation or domestic peace has been destroyed, whose feelings have been outraged, or who has suffered bodily pain and danger, are of a nature so strictly personal, that an assignee cannot urge them with any force.”).

143. U.C.C. § 9-104(k) (1972).

144. *Id.* § 9-102(a)(13)(B)(ii) (2000).

145. *See, e.g., Powe v. Payne*, 94 So. 587, 588 (Ala. 1922) (“[I]t appears that complainants are not entitled to immediate possession or enjoyment of any estate in the land and hence that they are not in a position to file a bill for partition.”); *Simmons v. Klemme*, 291 S.W.2d 801, 802 (Ark. 1956) (“A mere naked right to set aside a contract on the ground of fraud is not assignable.”); *McCord v. Martin*, 166 P. 1014, 1015 (Cal. Dist. Ct. App. 1917) (holding that the cause of action was assignable because it was “much more than a mere naked right of action for fraud and deceit”); *Marshall v. Means*, 12 Ga. 61, 67 (1852) (“Before such an interest can be assigned ... the party assigning such right, must have some substantial possession ... and not a mere naked right to maintain a suit.”); *Mulready v. Pheeny*, 148 N.E. 132, 133 (Mass. 1925) (“A mere naked right to set aside a contract on the ground of fraud is not assignable.”); *Cornell v. Upper Mich. Land Co.*, 155 N.W. 99, 102 (Minn. 1915) (affirming that “an assignment of a bare right to [bring suit] ... for a fraud ... is void as against public policy,” but holding the assignment at issue valid).

the assignment in question was essentially identical to the assignment in *Accrued Financial Services*.<sup>146</sup> The assignee sued to take possession of some mines whose title was held by a third party, Baker.<sup>147</sup> The assignee had received the assignment of the assignor's fraud claim against Baker, whom he believed—with evidence—had taken title from him by deceit.<sup>148</sup> It was proved that the assignee promised to transfer the title held by Baker to the assignor if the suit was successful; presumably the assignee would receive some reward or pro rata share of the value of the mines, for her trouble.<sup>149</sup> The court struck down the assignment, saying that “a bare right to file a bill in equity for a fraud committed upon the assignor” cannot be assigned.<sup>150</sup> The court cited *Prosser*, in which Lord Abinger said, “It is a rule, not of our law alone, but of that of all countries, that the mere right of purchase shall not give a man a right to legal remedies ... upon general principles, and by analogy ... a court of equity will discourage the practice.”<sup>151</sup> Even though it is tempting to dismiss this case as an anachronism—a result of a formalist style of reasoning that modern courts have abandoned—the argument used by the court to nullify the assignments in *Accrued Financial* was basically identical to the argument used by the court in *Poe*.<sup>152</sup>

Finally, rule-of-law concerns about treating inchoate rights as if they were real can explain another limitation on assignment that persists today—the distinction between the assignment of personal injury claims and the assignment of the *proceeds* of personal injury claims.<sup>153</sup> Because personal injury claims were considered inchoate,

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146. *Gruber v. Baker*, 23 P. 858 (Nev. 1890).

147. *Id.* at 858-59.

148. *Id.* at 859-60.

149. *Id.* at 863-64.

150. *Id.* at 862.

151. *Id.* at 862-63 (citations omitted).

152. This was Radin's ultimate point. See Radin, *supra* note 40, at 70-78.

153. See *Med. Lien Mgmt. Inc. v. Allstate Ins. Co.*, No. 12CA0691, 2013 WL 2450632, at \*4 (Colo. Ct. App. 2013) (reviewing jurisdictions that have allowed the assignment of the proceeds of a personal injury claim even if the claim itself could not be assigned). Other courts hold that there is no difference between the assignment of the action itself and the proceeds which may be recovered in such an action, and thus that such an assignment violates the rule prohibiting an assignment of a cause of action for personal injuries. See, e.g., *Karp v. Speizer*, 647 P.2d 1197, 1198 (Ariz. Ct. App. 1982) (“[A]bsent a statute to the contrary a cause of action for personal injuries is not assignable.”); *Town & Country Bank of Springfield v. Country Mut. Ins. Co.*, 459 N.E.2d 639, 640 (Ill. App. Ct. 1984) (“Illinois law has established that a cause of action for personal injuries may survive by virtue of the Survival Act, but it is nevertheless

the proceeds of a personal injury had to be, by implication, inchoate as well.<sup>154</sup> But courts accepted the argument that proceeds of personal injury claims could be the subject of an *equitable* assignment (which is capable of enforcement once the proceeds come into existence).<sup>155</sup> So, although New York prohibited by statute the assignment of any “claim or demand [when it is] to recover damages for personal injury,” by this maneuver New York courts permitted the assignment of the proceeds of personal injury claims, thus allowing parties to “do by indirection what the common law and the statute expressly [forbade].”<sup>156</sup>

Explicit rule-of-law arguments referencing control have been employed to provide a rationalization in favor of the assignment of the proceeds of personal injury claims, thus allowing courts to avoid legal fictions like the equitable assignment. Some courts, such as the Nevada Supreme Court in *Achrem v. Expressway Plaza Limited Partnership*, observed that because the assignor keeps control over the way a claim is litigated and settled when proceeds are assigned, the assignment of proceeds does not violate common law principles.<sup>157</sup> This argument exploits the practical reality that title over the proceeds of a claim has no special value to most assignors as long as they have ownership of other funds of equal or at least of negotiated value.<sup>158</sup> The court basically said that once party control is preserved, assignment in personal injury no longer violates the rule-of-law requirements of the common law. Of course, the court did not simply stipulate that party control in personal injury was a good in itself. The court justified its focus on party control by arguing that without it the legal system would be infected with

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not assignable, on public policy grounds.”)

154. See, e.g., *Costanzo v. Costanzo*, 590 A.2d 268, 271 (N.J. Super. Ct. Law Div. 1991) (“Any ‘specific thing,’ debt or chose in action may be the subject of an assignment. Obviously, that which is not in existence or cannot be identified cannot be assigned.” (citation omitted)).

155. *Williams v. Ingersoll*, 89 N.Y. 508, 518 (1882) (“Story, in his *Equity Jurisprudence*, in section 1040, says: ‘Courts of equity will support assignments, not only of choses in action, and of contingent interests and expectancies, but also of things which have no present, actual or potential existence, but rest in mere possibility.’”).

156. *Grossman v. Schlosser*, 244 N.Y.S.2d 749, 750-51 (App. Div. 1963).

157. 917 P.2d 447 (Nev. 1996); *Grossman*, N.Y.S. 2d at 448.

158. *Achrem*, 917 P.2d at 449 (“When the *proceeds* of a settlement are assigned, the injured party retains control of their lawsuit and the assignee cannot pursue the action independently ... [because the assignors] retained control of their lawsuit.”).

champerty.<sup>159</sup> But this argument still begged the question of why champerty was inconsistent with the rule of law.

### C. Subrogation

“Subrogation is broadly defined as the substitution of one person in the place of another with reference to a lawful claim or right.”<sup>160</sup> Subrogation is a doctrine that “originated in equity to give relief to a person or entity that pays a legal obligation that should have, in good conscience, been satisfied by another.”<sup>161</sup> Subrogation puts one to whom a particular right does not legally belong in the position of the legal owner of that right for the purpose of enforcing that right for their own benefit. The right of subrogation is purely derivative, because it permits a party to step into the shoes of the victim as it pursues recovery from the responsible wrongdoer.<sup>162</sup>

Subrogation may be conventional (arising from contract) or equitable (arising as a matter of law).<sup>163</sup> Most cases of equitable subrogation occur when a party pays a debt or an obligation of another in order to protect her own secondary rights, to fulfill a contractual obligation, or to comply with the request of the original debtor.<sup>164</sup> In order to enforce a right in equitable subrogation the subrogee does not necessarily have to communicate with the subrogor or have the opportunity to control any claim the subrogor is pursuing or could pursue. For example, when a master has been held liable for an injury caused by her servant under *respondet superior*, the master is subrogated to the plaintiff’s claim against the servant through operation of law, and yet the legal grounds of the claim cannot be altered by anything the master now does.<sup>165</sup>

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159. *Id.* at 448-49; *see also In re Duty*, 78 B.R. 111, 114 (Bankr. E.D. Va. 1987); *Charlotte-Mecklenburg Hosp. Auth. v. First of Ga. Ins. Co.*, 455 S.E.2d 655, 657 (N.C. 1995).

160. *See* 73 AM. JUR. 2D *Subrogation* § 1 (2012).

161. *Allied Mut. Ins. Co. v. Heiken*, 675 N.W.2d 820, 824 (Iowa 2004).

162. *Id.*

163. *See* Gregory R. Veal, *Subrogation: The Duties and Obligations of the Insured and Rights of the Insurer Revisited*, 28 TORT & INS. L.J. 69, 70 (1992).

164. *See, e.g., Shpritz v. District of Columbia*, 393 A.2d 68, 69 (D.C. 1978) (holding that shareholders who paid a corporation’s tax debt became subrogated to the federal government’s rights against customers of the corporation against whom it had tax liens).

165. *Losito v. Kruse*, 24 N.E.2d 705, 707 (Ohio 1940).

There is, however, a subset of subrogation rights that involve either the actual control or potential control of the subrogor's tort claims by the subrogee. These are subrogation rights that arise through first-party insurance contracts.<sup>166</sup> As in all other forms of subrogation, "an insurer who has paid a loss to an insured [becomes] 'subrogated in a corresponding amount to the insured's right of action against any other person responsible for the loss.'"<sup>167</sup> Insurers or other providers of assistance and medical care to the victim may recover from the person responsible for the loss only to the extent that their contracts subrogate them to the victim's rights.<sup>168</sup> This is conventional subrogation.<sup>169</sup> Conventional subrogation assumes that a valid claim can be asserted against the tortfeasor by the subrogor at least equal to the amount paid by the subrogee/insurer. The key point for our purposes is who controls that claim.<sup>170</sup> This is a question which should, in theory, be handled by the insurance contract.<sup>171</sup>

Questions of control arise because the tort victim's rights are the vehicle by which the insurer will get paid by the tortfeasor. In a loose sense, subrogation can be achieved by assignment, and certainly insurance contracts and courts sometimes treat assignment and subrogation as if they were interchangeable.<sup>172</sup> This is partly a result of the fact that many insurance contracts require the insured to assign their claim to the insurer as a means of subrogating the claim. But that does not mean that they are the same thing.<sup>173</sup> The differences between assignment and subrogation, while

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166. See 73 AM. JUR. 2D *Subrogation* § 31 (2014). First-party insurance subrogation rights usually arise by contract, but even when the insurance contract does not explicitly provide for them, the insurer's right to subrogation attaches by operation of law upon payment of the loss based on principles of equity. *Id.*

167. *Allied Mut. Ins. Co. v. Heiken*, 675 N.W.2d 820, 824 (Iowa 2004) (quoting 6A JOHN ALAN APPLEMAN & JEAN APPLEMAN, *INSURANCE LAW AND PRACTICE* § 4051, at 103 (rev. ed. 1972)).

168. 4 NEW APPLEMAN LAW OF LIABILITY INSURANCE § 42.01 (Matthew Bender ed., rev. ed. 2014).

169. 5 NEW APPLEMAN ON INSURANCE LAW LIBRARY EDITION § 49.02 (Jeffrey E. Thomas ed., 2014).

170. *Id.* § 49.08 (discussing how to enforce subrogation rights).

171. Thomas S. Brown & M. Jane Goode, *Conflict of Interest in Subrogation Actions*, 22 *TORT & INS. L.J.* 16, 26 (1986).

172. See, e.g., *Aetna Cas. & Sur. Co. v. Hensgen*, 258 N.E.2d 237, 242 (Ohio 1970).

173. 6A JOHN ALAN APPLEMAN & JEAN APPLEMAN, *INSURANCE LAW AND PRACTICE* § 4053 (rev. ed. 1972) ("[T]here is a difference between a subrogation and an assignment.").

rarely important in practice, reveal some interesting fault lines in the common law's view of the alienability of control.

Historically, insurance companies argued that there had to be a difference because the prohibition of the assignment of causes of action—which at one time extended to far more claims than today—would have made subrogation impossible if it were viewed as the same thing as assignment.<sup>174</sup> As late as 1975, the subrogation of insurance payments for medical expenses was challenged on the grounds that personal injury claims cannot be assigned.<sup>175</sup> Given the economic importance of first-party personal injury insurance (including automobile insurance, which rapidly became compulsory in most states), it is not surprising that courts found ways to distinguish assignment and subrogation when it was necessary to preserve insurers' subrogation rights.<sup>176</sup>

In *Imel v. Travelers Indemnity Co.*, the insured demanded that his insurer pay his medical expenses after a car accident but refused to sign documents ratifying the insurer's subrogation rights in exchange for the funds.<sup>177</sup> The insured's argument came down to this: the subrogation right sought by the insurer was an assignment of his cause of action for personal injury because it gave the insurer ownership of the claim, and that was not permissible under Indiana law (ironically, the insured cited *Rice v. Stone*, discussed above, to support his argument).<sup>178</sup> The court rejected the insured's argument, noting that despite a body of precedent favoring the insured, the court preferred a more modern approach supported by considerations of public policy.<sup>179</sup> The court noted the differences between assignment and subrogation:

We agree with the majority of the jurisdictions which make a distinction between an assignment of a claim for personal

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174. *Over v. Lake Erie & W. R.R.*, 63 F. 34, 35 (C.C.D. Ind. 1894); see, e.g., Brendan S. Maher & Radha A. Pathak, *Understanding and Problematizing Contractual Tort Subrogation*, 40 LOY. U. CHI. L.J. 49, 69-70 (2008).

175. See *Schuldt v. State Farm Mut. Auto. Ins. Co.*, 238 N.W.2d 270, 271 (S.D. 1975).

176. For a typical discussion by a court of the public policy concerns that justify drawing the distinction, see *Hosp. Serv. Corp. of R.I. v. Pa. Ins. Co.*, 227 A.2d 105, 110 (R.I. 1967) ("All of us are aware that today Blue Cross serves a most important beneficial, social, and economic purpose in our state.")

177. 281 N.E.2d 919 (Ind. Ct. App. 1972).

178. *Id.* at 920.

179. *Id.* at 921.



injuries and subrogation of one's rights arising from a personal injury. A few of the distinctions are: subrogation secures contribution and indemnity, whereas assignment transfers the entire claim; the consideration in subrogation moves from subrogor to subrogee, whereas in an assignment the consideration flows from assignee to assignor; assignment contemplates the assignee being a volunteer, whereas subrogation rests on a contractual duty to pay; assignment normally covers but a single claim, whereas subrogation may include a number of claims over a specific period of time; subrogation entails a substitution, whereas assignment is an outright transfer.<sup>180</sup>

The *Imel* court probably suspected that the insured's invocation of the prohibition of the assignment of personal injury claims was purely pretextual—the insured wanted to take the payments made by the insurer, keep them, and then sue the tortfeasor for the cost of the medical payments and keep these costs too.<sup>181</sup> The question of the insured's control over his lawsuit was probably never at issue in *Imel*; like many personal injury cases, the insurance payment was only for a portion of the damages suffered, and the insured had sufficient incentive to pursue his claim with his own lawyer. The insurer wanted the fruits of the insured's efforts and was more than happy to let the insured control the suit. That is the significance of the last item in the list quoted above: “subrogation entails a substitution, whereas assignment is an outright transfer.”<sup>182</sup> This meant that unless required by the court, the insurance company was not a party to the insured's suit, which meant that the insurer could not control the suit *as a party* (even if it wanted to).<sup>183</sup> From

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180. *Id.*

181. See 46A C.J.S. INSURANCE § 1993 (2014) (“Subrogation prevents ... unjust enrichment to the insured that would result from double recovery.”); 16 COUCH ON INSURANCE § 222:8 (3d. 2014) (“[I]t has been stated that subrogation has the objective of preventing the insured from recovering twice for one harm, as would be the case if he or she could recover from both the insurer and from a third person who caused the harm.”); ROBERT E. KEETON & ALAN I. WIDISS, INSURANCE LAW § 3.10(7) (1988) (“Recognition and enforcement of a right of subrogation for health insurers is primarily premised on precluding duplicative recoveries.”); see also *Standard Accident Ins. Co. v. Pellecchia*, 104 A.2d 288, 292 (N.J. 1954) (explaining that one of subrogation's goals is to protect against the possibility that the “insured would be unjustly enriched by virtue of a recovery from both the insurer and the third party”).

182. *Imel*, 281 N.E.2d at 921.

183. See *In re Garmhausen*, 262 B.R. 217, 221-22 (Bankr. E.D.N.Y. 2001) (discussing the meaning of substitution in the context of Federal Rule of Civil Procedure 25(c)).

the insurer's perspective this was the point. It did not want to be a party; it did not want to be in front of the jury.<sup>184</sup> Whatever the merits of this tactical consideration, it explains why insurers sought to maintain the possibility of subrogation without assignment.

In most cases, the interests of the insurer and the insured are in alignment against the tortfeasor, so it requires a little digging to see why control is ever an issue.<sup>185</sup> To be precise, what is at issue is not the problem of the *faithless* insured, although the insurer must worry about her too.<sup>186</sup> Faithless insureds usually try to settle their claim with the tortfeasor without telling the insurer; although they can also include insureds who, after receiving payments from the insurer, refuse to "cooperate" as the insurance contract requires, which might mean anything from refusing to file a complaint to refusing to participate in litigation initiated by the insurer in their name. Many doctrines have developed to deal with the faithless insured—ranging from holding the insured liable to the insurer for destroying the claim under which the insurer was subrogated, to allowing the insurer to sue the tortfeasor directly for the portion of the insured's claim under which the insurer was subrogated.<sup>187</sup> Neither of these remedies really go to the problem of control in subrogation because the insurer is not seeking to control how the insured litigates her own case. In the former, the insurer is simply

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184. "It is thought by insurers that a jury will be less sympathetic to a suit if it is brought in the name of the insurer, so it will bring the suit in the name of the subrogor/insured." NEW APPLEMAN LAW OF LIABILITY INSURANCE, *supra* note 168, § 42.03; *see, e.g.*, *Celanese Corp. of Am. v. John Clark Indus., Inc.*, 214 F.2d 551, 556-57 (5th Cir. 1954) (suggesting that the defendant's reason for attempting to join the plaintiff's insurance companies was to inform the jury that the plaintiff was insured and thereby potentially prejudice the plaintiff's case); *Acro Automation Sys. v. Iscont Shipping, Ltd.*, 706 F. Supp. 413, 421 (D. Md. 1989) ("[The defendants] would consider it a strategic advantage to have the jury know that a plaintiff has another source of recovery other than from them."); *Stouffer Corp. v. Dow Chem. Co.*, 88 F.R.D. 336, 338 (E.D. Pa. 1980) ("[T]here is a substantial risk of prejudice to an insurer which is forced to join as a plaintiff, as the presence of an insurer may affect a jury's decision on the merits."); *Kint v. Terrain King Corp.*, 79 F.R.D. 10, 12 n.4 (M.D. Pa. 1977) (citing prejudice to the plaintiff as one factor supporting a decision denying a motion under Federal Rule of Civil Procedure 19 to join the plaintiff's insurance companies).

185. *Brown & Goode*, *supra* note 171, at 26.

186. The faithless insured is someone who destroys her claim before receiving anything on behalf of the insurer's subrogated interest.

187. *City of N.Y. Ins. Co. v. Tice*, 152 P.2d 836, 842-43 (Kan. 1944). An insurer can sue the tortfeasor directly only if the tortfeasor was on notice of the potential subrogation claim destroyed by the insured's release. *See* ROBERT H. JERRY II & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW 669 (5th ed. 2012).

pursuing contract damages, whereas in the latter, the insurer is, in effect, taking an assignment.<sup>188</sup> Control is not at the center of the problem with the faithless insured, because her conflict with the insurer is not over the control of a suit she wants to pursue, but rather over her abandonment of the suit in toto.

The question of control arises, therefore, in cases of subrogation when the insured and the insurer both agree that the insured should make a claim. These cases can arise in one of two situations. If an insurer paid all of the insured's loss, both federal law and many states say that the insurer is the real party in interest and must bring the suit in its own name.<sup>189</sup> But some states say otherwise, as was illustrated above in *Imel*.<sup>190</sup> When the insurer wants to have the insured step forward as the plaintiff in the case and yet control it like a puppet, the defendant might attempt to expose this fact in the hope that it will turn the jury against the plaintiff. Most courts have rejected moves by defendants to expose the insurer as the puppeteer pulling the strings in the case. As the Supreme Court of Oklahoma said:

Defendant has the statutory right to have a cause of action prosecuted against him by the real party in interest .... The concern of the defendant ends, however, when a judgment for or against the nominal plaintiff would protect him from any action on the same demand by another, and when, as against the nominal plaintiff he may assert all defenses and counterclaims available to him the same as if the claim were enforced by the real owner .... The insured and insurer are free to enter into additional agreements or to set up a trust agreement in order to best handle the collection of the loss. The parties' fundamental right of liberty to contract, when done in a lawful manner in the absence of fraud is not to be dictated by the effect it might possibly have on defendant. This is a matter of business judgment to be determined by insured and insurer.<sup>191</sup>

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188. The latter option—the insurer seeking its subrogation without the cooperation of the insured—is possible in theory, but is highly impracticable unless the claim can be resolved entirely on the pleadings, as was the case in *City of New York Insurance Co. v. Tice*. 152 P.2d 836.

189. *United States v. Aetna Cas. & Sur. Co.*, 338 U.S. 366, 380-81 (1949) (citing 3 MOORE'S FEDERAL PRACTICE 1339 (2d ed.)).

190. *Imel v. Travelers Indem. Co.*, 281 N.E.2d 919, 921 (Ind. Ct. App. 1972).

191. *C & C Tile Co. v. Indep. Sch. Dist.*, 503 P.2d. 554, 561 (Okla. 1972) (citations omitted).

The court observed that the plaintiff clearly wished “to prevent disclosure of plaintiff’s insurance to the jury.”<sup>192</sup> Given that the plaintiff had nothing to gain in the litigation, it is clear that the plaintiff’s insurer in coordination with counsel that it was supplying was controlling the litigation.<sup>193</sup> In *Garcia v. Hall*, the Tenth Circuit took the same position.<sup>194</sup> In that case, the insured admitted that he had no interest in the outcome of the suit and was bringing it only for the benefit of the insurer—who did not want to be a party.<sup>195</sup>

If an insurer’s payment only partially compensated the policyholder, such as when the policyholder sustained losses in excess of policy limits or when there was a deductible that the insured, in theory, could personally recover, the insurer could seek to hide behind the insured’s residual interest, no matter how slight, so the insurer would not have to declare itself as a party to the suit against the tortfeasor.<sup>196</sup> Wise to this maneuver, tortfeasors have sought to have the insurer’s interest revealed, especially when it is substantial in comparison with that of its insured.<sup>197</sup> The federal courts have given their blessing to arrangements by which creative insurers conceal their interest in suits where they are the only party interested in suing the tortfeasor. In *Virginia Electric & Power Co. v. Westinghouse Electric Corp.*, the plaintiff suffered \$2,200,000 in damages due to the failure of a power generating station.<sup>198</sup> All but \$150,000 of the loss had been reimbursed by its insurer.<sup>199</sup> The

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192. *Id.* at 560 (pointing out that it would be inconsistent for the court to allow the jury to learn of the insurer’s interest in the suit if juries are prohibited from knowing whether the defendant has liability insurance); see NEW APPLEMAN LAW OF LIABILITY INSURANCE, *supra* note 168, § 42.03 (noting that it would be unfair if the “plaintiff-insurer must disclose its name under the ‘real party in interest’ doctrine, but the defendant-insurer does not”).

193. The practice of a subrogor being the party plaintiff in a case in which they had no interest and no control has been around for a while. See, e.g., Albert W. Jenner, Jr. & Phillip W. Tone, *Pleading, Parties and Trial Practice*, 50 NW. U. L. REV. 612, 612 (1955) (“An insured under an automobile collision policy who has collected for property damage under the policy ordinarily has no control over a subrogation action brought subsequently in his name by the insurer under the subrogation provision of the policy.”).

194. 624 F.2d 150, 152 (10th Cir. 1980).

195. *Id.*

196. See, e.g., *Trogub v. Robinson*, 853 N.E.2d 59, 63, 65-67 (Ill. App. Ct. 2006).

197. See June F. Entman, *More Reasons for Abolishing Federal Rule of Civil Procedure 17(a): The Problem of the Proper Plaintiff and Insurance Subrogation*, 68 N.C. L. REV. 893, 895-97, 911-31 (1990).

198. 485 F.2d 78, 81 (4th Cir. 1973).

199. *Id.* at 82.

insured and insurer agreed that the insured would file suit for the entire \$2,200,000 loss and that the insurer “would furnish counsel and have exclusive direction and control” of the claim.<sup>200</sup> The agreement further specified that if successful, the insured would receive its \$150,000 uninsured loss and it would not be obligated for the costs and expenses of the suit.<sup>201</sup> The court concluded that the tortfeasor could not force the insurer to join the suit; it noted that the fact that the insurer was in control of the suit counted *in favor* of allowing it to remain unnamed.<sup>202</sup>

Although the insured’s incentive to bring a claim that will benefit the insurer will vary based on many factors (including how much, if anything, she might keep after her lawsuit is resolved), the insurer’s incentive remains the same (recovery of the payment from the tortfeasor); the only thing that varies is the cost to it of the insured’s suit.<sup>203</sup> The cost might be close to zero if the insured is highly incentivized to sue and retains a contingency fee attorney who will advance all costs; or the cost might be high if the insured has no remaining financial interest in the claim and participates grudgingly.<sup>204</sup> There will be a separate but non-negligible cost to the insurer of monitoring the suit. There is also an additional cost of achieving an outcome which meets the insurer’s needs if there is a difference of opinion between the insured and the insurer as to settlement.<sup>205</sup>

For the purposes of this Article, it is important to note that the common law permits the insured *ex ante* to give up as much or as

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200. *Id.*

201. *Id.*

202. *Id.* at 85-86 (holding that one equitable factor against forcing joinder was that “because of [the insurer’s] control of the suit, it will be bound by any judgment in favor of the defendants”).

203. Maher & Pathak, *supra* note 174, at 86-87 (“The lower a plaintiff’s [that is, the insured’s] expected recovery, the less likely s/he is to expend effort prosecuting a suit .... The [insured] ... is the junior creditor on the dollars recovered: the first money in goes to the insurer; the next dollars go towards paying the plaintiff’s attorneys and costs of suit; and any remaining dollars go to the plaintiff.”).

204. *Id.* at 87-88.

205. Brown & Goode, *supra* note 171, at 26 (“In the event the litigation is successful or settlement offers are extended, the potential for conflict arises. While the parties are of a single mind with respect to the fact of recovery, there may be an enormous difference of opinions as to the allocation of the proceeds, fees, and costs, as well as who should have the power to accept or reject an offer of settlement.”).

little control over these questions as he sees fit before he knows the details of the suit that it will be bringing against the tortfeasor. Insurers have developed various mechanisms for taking control over claims brought by subrogors without having to join the litigation or take a complete assignment. The courts allow these strategies, as long as the basic requirements of contract law are observed. One federal court, when faced with a request to name an insurer as “a party in interest” in a suit brought by an insured whose interest was \$1000 of a \$228,127 claim, dismissed the defendant’s offer of proof that the insurer was controlling the litigation as irrelevant: “That argument is not persuasive. ‘As a practical matter, ... the insurance company will control the prosecution no matter in whose name it is brought.’”<sup>206</sup>

The mechanisms by which the insurer can control the litigation may be informal (based on the past and future transactions of the parties), or a threat of collateral litigation based on a breach of a duty to cooperate, or post-accident contracts that the insurer asks the insured to sign as a condition of receiving the payment under the insurance contract.<sup>207</sup> This last type of mechanism has various names, such as “subrogation receipts,” “loan receipts,” and “trust agreements.”<sup>208</sup> Each instrument can be drafted to fit the needs of the situation. The language in the agreement that was at issue in *C & C Tile Co. v. Independent School District* is illustrative, and perhaps typical:

THE UNDERSIGNED hereby acknowledge(s) receipt of \$84,764.00 from—INSURANCE COMPANY OF NORTH AMERICA— ... and the undersigned hereby irrevocably appoint(s) said Insurance Company as agent and attorney-in-fact of the undersigned *with full power to collect, enforce, compromise, release and dispose of such property, claims and recoveries*

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206. *Prosperity Realty v. Haco-Canon*, 724 F. Supp. 254, 258 (S.D.N.Y. 1989) (quoting C. WRIGHT & A. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1546, at 656).

207. *Veal*, *supra* note 163, at 89.

208. *Id.* at 77 (“A loan receipt is a device with which the insurer essentially settles by paying the insured and taking control of, but not title to, the insured’s claims.”); *see also* NEW APPLEMAN LAW OF LIABILITY INSURANCE, *supra* note 168, § 42.04 (2013) (providing examples of all three).

*through attorneys and representatives of the said Insurance Company's own selection, by legal proceedings or otherwise.*<sup>209</sup>

Under this instrument the insurer had full control of the insured's lawsuit. The insurer could select and instruct the attorneys. It was paying the attorneys (unless the insurer found an attorney willing to work for a contingent fee). It should be noted that the relationship between the attorneys selected by the insurer and the insured was the same triangular relationship that has been the subject of heated disputes about attorneys hired by liability insurers in the defense context.<sup>210</sup> The same question arises: Is the attorney the agent of both the insured and the insurer, or just the insured?<sup>211</sup> In the case of a conflict of opinion over litigation strategy and settlement, what should the attorney do?<sup>212</sup> In the liability insurance context (discussed in Part III.D), there has been disagreement among scholars and commentators about whether the insured can be represented by the same lawyer whom the insurer uses to control the litigation.<sup>213</sup> But in the liability insurance context, the risk is that an insurer acting in bad faith will instruct the attorney jointly representing the insurer and insured to expose the insured to excess liability. In the subrogation context, the risk goes entirely in the other direction—that having been made whole by the insurer, the insured will destroy the insurer's opportunity to be made whole by the tortfeasor.

The possibility that there may be a conflict between the insurer and the insured over the conduct of litigation against the insured's

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209. 503 P.2d 554, 557 (Okla. 1972) (emphasis added).

210. See, e.g., Charles Silver & Kent Syverud, *The Professional Responsibilities of Insurance Defense Lawyers*, 45 DUKE L.J. 255, 269-70 (1995).

211. *Id.* at 273.

212. *Id.* at 266-67.

213. See Robert J. Johnson, Comment, *In-House Counsel Employed by Insurance Companies: A Difficult Dilemma Confronting the Model Code of Professional Responsibility*, 57 OHIO ST. L.J. 945, 962-65 (1996). The consensus seems to be that it is ethical for attorneys employed by subrogers to represent subrogees. See, e.g., ABA Comm. on Ethics & Prof'l Responsibility, Informal Op. 1370 (1976). The committee further stated that such a representation was appropriate "provided you make the prescribed disclosure and remain sensitive to any subsequent divergence of interests of your clients." *Id.* All sides of this debate agree that the question is not whether the lawyer employed by the insurer can be an agent of the insurer and follow its instructions. Instead, the question is whether that person can also be an agent of the insured. *Id.*

tortfeasor is not large, but it exists. The insured's interests are protected to some extent by the "make-whole" rule, which says that an insured must have all of its losses paid before the insurer can take anything. This creates an incentive for the insurer, if it is controlling the litigation, to pursue a resolution to the insured's claim that leaves the insured whole.<sup>214</sup> But this only guarantees that the insured's interests are protected if there is a final judgment that produces funds which, in combination with insurer's payment to the insured, are equal or greater than the insured's loss. This may not happen if, for example, the insurer—who controls the case—refuses a settlement offer and chooses to go to trial on the insured's claim, and the tortfeasor prevails. The result could be that the insured, but not the insurer, is worse off than if there had been a settlement because the entire settlement may have gone to the insured. In addition, if the make-whole rule does not control—either because the jurisdiction does not accept the rule or because the insurance policy imposes a "first-dollar" rule that ensures that the first dollar of every settlement goes to the insurer—then the insured and the insurer may come into conflict if the settlement does not provide for the insured's uninsured losses.<sup>215</sup> The only difference is that now the insurer wants settlement more than the insured. Under either scenario, insurance law does not protect the insured: there is no duty on the part of an insurer—as subrogee—to settle its subrogor's claim in good faith.<sup>216</sup>

If a disagreement over litigation strategy and settlement between the insured and the insurer arises, the attorney's obligations are

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214. Elaine M. Rinaldi, *Apportionment of Recovery Between Insured and Insurer in a Subrogation Case*, 29 TORT & INS. L.J. 803, 805-07 (1994). This is the majority rule. See NEW APPLEMAN ON INSURANCE LAW LIBRARY EDITION, *supra* note 169, § 49.04 ("[A] minority of jurisdictions adhere to the 'insurer-whole' rule, whereby the insurer is made whole first out of a recovery from a third-party tortfeasor to the extent of the insurer's payment to the policyholder.").

215. Daniel Schwarcz, *Reevaluating Standardized Insurance Policies*, 78 U. CHI. L. REV. 1263, 1294 (2011).

216. See, e.g., *Lahti v. Finnish Mut. Fire Ins. Co.*, 256 N.W.2d 610, 611-12 (Mich. App. 1977) ("[W]e have searched in vain for any case holding an insurer liable to its insured for refusing to compromise its subrogation rights and enter into a settlement and release agreement with an alleged tortfeasor ... [and] in the absence of any such provision in the subrogation agreement, we are of the opinion that no such duty existed in this case."). This is quite the opposite from the protection offered to the insured under the duty to settle in good faith that has arisen in the parallel situation in liability insurance.



defined by the rules of professional responsibility for her jurisdiction—assuming the attorney represents both the insured and the insurer. When the attorney has been told by the insurer to reject a settlement offer that the insured thinks is reasonable, the attorney clearly can no longer represent both parties and must either withdraw completely or represent only one party.<sup>217</sup> But that does not really solve the insured's problem, which is that she wants to *maintain* control over the case. Through its new lawyer, the insurer can still effectively control the insured's litigation by refusing to accept settlement with the tortfeasor. The only way for the insured to settle separately with the tortfeasor is for him to breach his contractual obligations to the insurer, which would have significant consequences arising from the violation of his duty to cooperate with the insurer.<sup>218</sup>

The point of this discussion is not to conclusively answer the question of how the insured can maintain control over its claim if it is in conflict with the insurer over the handling of a subrogated claim. The point is simply to demonstrate that the law of subrogation does not privilege party control. Courts accept that control can be alienated without requiring the claims to be assigned. Further, courts do not directly limit alienation of control, but instead regulate the risks that may flow from alienation by providing a safety net of common law doctrines to ensure that parties who alienate control receive a minimum of their equitable interest in the claim, for example, the make-whole rule, which protects the insured.

Some have made rule-of-law arguments against insurers using subrogation contracts to hide their interest in a case from juries, but they are based on a very different set of concerns than the rule-of-law arguments for party control reviewed in this Part. June Entman

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217. Brown & Goode, *supra* note 171, at 28.

218. It is an open question whether the insurer could ask a court to issue an injunction against the insured sharing confidences and work product developed by attorneys who were in the employ of the insurer on behalf of the insured with third parties. At the very least, the insured would have to reimburse the insurer for all monies spent by the insurer to pursue the insured's claims not subrogated to the insured. It may also be liable for all or some portion of the insurer's subrogation interest if the insured's conflict with the insurer prejudices the insurer's remaining claim against the tortfeasor. *See, e.g.,* Home Ins. Co. v. Bernstein, 16 N.Y.S.2d 45, 47-49 (Mun. Ct. 1939) (holding that settlement for nonsubrogated portion of insured's claim could not insulate the insured from liability to insurer if the amount claimed by the insured was proven by insurer to be in excess of the insured's uncompensated injury).

argues that subrogation receipts and permissive joinder rules violate principles of federal and state common law.<sup>219</sup> Her argument has two parts. First, federal civil procedural values are violated when courts permit insurers to participate in federal litigation without revealing themselves as parties in interest, such as in *Virginia Electric & Power Co.*<sup>220</sup> Second, and related to the first, is that “one in control of litigation ... should bear the responsibilities of party status ... [i]f a subrogated insurer is in actual control of a lawsuit, but not named as a party ... its citizenship is ignored.”<sup>221</sup>

Entman’s arguments may be persuasive, but they are based solely in rule-of-law values that deal with ensuring that the courts and adverse parties are not misled about who the real party in interest is. Her arguments are not grounded in a concern over how the contract between the insurer and the insured interferes with the relationship between the insured and her lawyer, nor from a concern over interference with substantive choices made in the course of the litigation with the tortfeasor/defendant. All a critic like Entman wants is candor, which is not trivial given the tactical importance of establishing or destroying diversity jurisdiction in federal jurisdiction, but her concerns are very different from those of critics of litigation investment.

#### *D. Full Coverage Cases in Liability Insurance*

Usually, someone with an interest in the outcome of a lawsuit would prefer that the current claimholder control the litigation, so that instead of paying for control, the interested party “free-rides” on the effort of the original claimholder. However, as we saw in the previous section, when a subrogee has an equitable interest in the legal claim, it may often make sense for them to secure control over the conduct of litigation enforcing that claim through a contract. But what if the party seeking control has only a contingent (non-

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219. See June F. Entman, *Compulsory Joinder of Compensating Insurers: Federal Rule of Civil Procedure 19 and the Role of Substantive Law*, 45 CASE. W. RES. L. REV. 1, 12-14 (1994); Entman, *supra* note 197, at 899, 932.

220. See Entman, *supra* note 197, at 947-48 (“Thus, in the *Virginia Electric* case, a misapplication of rule 17(a) allowed the litigation in federal court of a two million dollar claim between nondiverse parties on the basis of the citizenship of a merely nominal representative.”).

221. Entman, *supra* note 219, at 66-68.

equitable) interest in the outcome of a legal claim against a stranger? As a practical matter, rights to control are rarely sought outside of the contexts already reviewed—assignment and subrogation. This may be for pragmatic reasons (the cost of obtaining the rights and enforcing them are too high) or legal reasons (courts will not enforce contracts seeking to enforce the right to control litigation by non-parties). There is, however, one significant exception to this generalization, and that is third-party liability insurance.

Before turning to liability insurance, I want to briefly review other contexts in which courts and legal scholars have noted the possibility of a party obtaining the right to control a stranger's defensive litigation. First, as Nathan Oman has observed, the theoretical possibility is present in every contract.<sup>222</sup> A widget manufacturer, in order to win the confidence of a counterparty (for example, lender or supplier) may make promises that limit her liberty with regard to control over her property or business.<sup>223</sup> Presumably, were it valuable to the counterparties, the covenants could extend to limiting control over future legal claims against it and litigation arising from those claims. One occasionally sees hints of this sort of exchange in, for example, real estate lending and construction finance.<sup>224</sup> In corporate finance, scholars have established that lenders secure control over the management of borrowers through covenants in debt instruments, which can rival the more naked power they exercise as creditors in bankruptcy.<sup>225</sup> The control, while significant, is limited to replacing personnel and

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222. Nathan Oman, *Corporations and Autonomy Theories of Contract: A Critique of the New Lex Mercatoria*, 83 DENV. U. L. REV. 101, 138 (2005).

223. These covenants “would significantly limit his former freedom to control ‘business’ property.” *Id.*

224. “[Lender] had the right to approve leases, set rental rates, input management contract decisions, control secondary financing ... and control the use of the Partnership’s Reserve Account .... It is uncontroverted that these terms are standard loan terms in the industry.” *Gray v. First Winthrop Corp.*, 776 F. Supp. 504, 511 (N.D. Cal. 1991). *But see* JOHN D. HASTIE, ALI-ABA, REAL ESTATE ACQUISITION, DEVELOPMENT, AND DISPOSITION FROM THE DEVELOPER’S PERSPECTIVE § 11.1.1 (2009) (observing that, although the construction lender attempts to “exert some element of control over the prosecution of the project” through “extensive and burdensome reporting requirements ... [t]he lender cannot exercise control of the project”).

225. *See* Douglas G. Baird & Robert K. Rasmussen, *Private Debt and the Missing Lever of Corporate Governance*, 154 U. PA. L. REV. 1209, 1226-28 (2006); Frederick Tung, *Leverage in the Board Room: The Unsung Influence of Private Lenders in Corporate Governance*, 57 UCLA L. REV. 115, 135-38 (2009).

controlling investment decisions. It has not extended to controlling defensive litigation, or at least if it has, the covenants that would grant that power have not been publicly revealed and discussed.<sup>226</sup> It is an interesting question why more lenders have not demanded control over litigation—either offensive or defensive—which might be critical to the borrower’s long term interests and hence to the lender’s long term interest in getting repaid.<sup>227</sup> Lenders and courts are not unfamiliar with the possibility nor do they lack a vocabulary with which to deal with conflicts that arise when lenders attempt to exercise control in their borrowers’ litigation.<sup>228</sup> Given the absence of the practice, it is impossible to tell whether its use is deterred by fear that contract conditions demanding control over a borrower’s litigation would not be enforced, or because there are more efficient mechanisms for lenders to reduce the risk of default.<sup>229</sup>

The one context in which contracts are used to control future defensive litigation by a counterparty is the third-party liability insurance contract.<sup>230</sup> As discussed in Part II, a liability insurance contract is really two forms of insurance, which in theory could be separated: the promise to pay liabilities that fall under the contract and the promise to pay for legal expenses connected with the defense of liability claims.<sup>231</sup> In the United States, the two are

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226. See, Robert M. Lloyd, *Financial Covenants in Commercial Loan Documentation: Uses and Limitations*, 58 TENN. L. REV. 335, 340-43 (1991).

227. This question is based on a suggestion by Jonathon Molot. See Jonathan T. Molot, *A Market in Litigation Risk*, 76 U. CHI. L. REV. 367, 403 (2009).

228. On a routine basis courts are asked to determine the boundary lines of control over plaintiff debtors’ litigation by creditors in bankruptcy. See, e.g., *In re Adelpia Commc’ns. Corp.*, 285 B.R. 848, 856 (Bankr. S.D.N.Y. 2002) (“[The creditor’s] rights to participate in an adversary proceeding [brought by the debtor], like any other lawsuit, may be thought of as falling along a continuum, with the right to file briefs and be heard in argument (rights similar to those of *amicus curiae*) at one end, and with the ownership or control of the underlying causes of action at the other.”); see also Seidel, *supra* note 109.

229. For a comprehensive review of the public policy limitations on contracts, see David A. Friedman, *Bringing Order to Contracts Against Public Policy*, 39 FLA. ST. L. REV. 563 (2012).

230. Standard general liability insurance contracts “are generally interpreted as granting the company plenary and exclusive control of the defense.” Silver, *supra* note 11, at 1596 (“Ordinarily, the company can select counsel to defend the insured, discharge appointed counsel and name a replacement without the insured’s consent, bargain with appointed counsel over fees, monitor counsel and direct litigation strategy, require counsel to inform the company of settlement demands and procedural developments, direct counsel to initiate settlement discussions, settle claims without an insured’s consent and decline to settle claims over an insured’s objection, and file appeals.” (footnotes omitted)).

231. See Boardman, *supra* note 11, at 682-83.

always sold together, but for the purposes of this Article, it is worth separating the two forms of insurance into *judgment costs insurance* (JCI) and *litigation costs insurance* (LCI).<sup>232</sup> They are sold together because the insurance contract must not only define who pays for the costs contained within each respective heading, but who controls the costs.<sup>233</sup> A JCI policy that does not allow the insurer to control settlement or the selection of counsel leaves a lot of leverage in the hands of the insured, even if she has to pay the litigation costs.<sup>234</sup> An LCI policy that only pays the bills sent in by the lawyers but does not control their expenses or the settlement decision, similarly leaves the insurer at the mercy of the insured, even if the insured has to pay the judgment costs.<sup>235</sup> So it is not a surprise that insurers, who often sell JCI and LCI in the same package, typically demand control over the selection of counsel and settlement, as well as other major incidents of control, when defending their insured.<sup>236</sup>

JCI and LCI are sold together because JCI insurers want to control the litigation that may result in a judgment they will have to pay.<sup>237</sup> The fact that they also offer to pay for the litigation expenses through LCI is an artifact of the insurer's demand of control over the litigation. In exchange, it is easy to see why the insureds would demand that the insurers pay for the litigation they seek to control. In other words, it is a matter of contract law. From this conclusion, once a default contract is established, alternatives, which vary the degree of control over litigation that may occur (or the selection of the counsel, how much they spend, et cetera), could be sold at prices that reflected the modification's value to each party. Directors and officers liability insurance, for example, is

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232. By "judgment" insurance, I mean settlements as well, which are negotiated in the shadow of the threat of adverse judgments which the insured and their insurer must pay. LCI is what insureds claim when they sue insurers for a breach of the "duty to defend." See, e.g., James M. Fischer, *Broadening the Insurer's Duty to Defend: How Gray v. Zurich Insurance Co. Transformed Liability Insurance into Litigation Insurance*, 25 U.C. DAVIS L. REV. 141, 144-45 (1991).

233. See Silver, *supra* note 11, at 1594.

234. See *id.* at 1394-96.

235. See *id.*

236. See *Davenport v. St. Paul Fire & Marine Ins. Co.*, 978 F.2d 927, 931-32 (5th Cir. 1992) (discussing the right of the insurer "to assume control of the defense of an action against the insured to the exclusion of the latter" and that "the same right that an insurer exercises in its settlement negotiations is exercisable by it in its choice of counsel").

237. See Silver & Syverud, *supra* note 210, at 264-65.

different from most other third-party liability insurance because although the insurer sells both JCI and LCI, the insurer does not take the same control over the litigation against its insureds.<sup>238</sup> The insurer keeps the right to settle within policy limits, which for the insured is a power they would happily give the insurer, but on all other matters the insured is in control.<sup>239</sup> Why boards allow managers to buy this kind of insurance is another question entirely, as is whether regulators should permit the insurance product to be sold.<sup>240</sup> Similarly, why claimholders want to sell party control and whether regulators should permit liability insurers to demand that claimholders sell their control are policy questions that are distinct from the relevant legal question: whether the common law currently permits such wide variations over party control.<sup>241</sup> Clearly, the common law permits such variations.

When courts have permitted insureds to alienate control over litigation, the courts understand exactly what they are permitting and the motives behind the parties' request. As the Supreme Court of Missouri observed in *In re Allstate Insurance Co.*, under the typical third-party liability insurance contract,

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238. See Tom Baker & Sean J. Griffith, *The Missing Monitor in Corporate Governance: The Directors' & Officers' Liability Insurer*, 95 GEO. L.J. 1795, 1814 (2007).

239. *Id.* ("D&O insurance contracts give policyholders the right to choose defense counsel and manage their own defense at the insurer's expense, subject only to the dollar limits of the policy and the requirement that defense costs be reasonable."). The fact that D&O (Directors and Officers) policies are purchased by corporate officers and directors with minimal monitoring by the parties who pay for it—the shareholder—may explain why this form of insurance is unlike any other. As Baker and Griffith point out, the incentives of the insurer and the agent/beneficiaries align towards an insurance contract that gives the agent/beneficiary control over litigation costs since the insurer is more than happy to sell such a policy (which is priced consequently higher) and the agent/beneficiary is happy to spend the principal's money to pay for it. *See id.* at 1832-33.

240. See Tom Baker & Sean J. Griffith, *Predicting Corporate Governance Risk: Evidence from the Directors' and Officers' Liability Insurance Market*, 74 U. CHI. L. REV. 487, 498, 502 (2007).

241. Certainly there are those who argue that in various circumstances, leaving this question to the market is not good policy. Insurer control over insured's claims may lead to undercompensation of deserving tort plaintiffs. *See, e.g.*, Jay M. Feinman, *Incentives for Litigation or Settlement in Large Tort Cases: Responding to Insurance Company Intransigence*, 13 ROGER WILLIAMS U. L. REV. 189, 193-94 (2008). Insured control over their own claims may lead to more tortious conduct. *See, e.g.*, TOM BAKER & SEAN J. GRIFFITH, ENSURING CORPORATE MISCONDUCT: HOW LIABILITY INSURANCE UNDERMINES SHAREHOLDER LITIGATION 135-36, 142-45 (2010).

[t]he insurer has the contract right to direct the litigation against [the] insured. It may evaluate claims and decide whether to settle.... It may make economic decisions without the assent of the insured. The insured may want a quick settlement to eliminate further demands on time and energy, but the insurer does not have to settle unless a satisfactory offer is forthcoming. Or the insurer may accept a settlement offer even though the insured wants to go to trial to establish freedom from fault. The insurer may decide what to spend in defense, what discovery is to be had, and what experts to hire. It also has the right to select counsel to defend its interests.<sup>242</sup>

Liability insurance involves a series of trade-offs between the contract parties, and as Charles Silver notes, “There is a downside to exclusive [insurance] company control.”<sup>243</sup> These downsides have been exemplified by several cases.<sup>244</sup> It is well understood that unless carefully monitored, insurance companies may take advantage of the control that comes with the coverage they sell. The insurer has an incentive to sacrifice the insured’s interests after litigation has begun (and after the bulk of the insurance premiums have been collected). Courts have developed various doctrines to protect the insured; the most significant is the duty to settle in good faith.<sup>245</sup>

The duty of good faith is entailed by the covenant of good faith and fair dealing, and the covenant of good faith and fair dealing has been read into insurance policies by modern courts.<sup>246</sup> The duty of good faith can come into play throughout the performance of the insurance contract by the insured, and it would include any conduct by the insurer during the insured’s litigation that damages “the very

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242. 722 S.W.2d 947, 952 (Mo. 1987) (en banc) (footnote omitted).

243. Silver, *supra* note 11, at 1597.

244. See, e.g., *Betts v. Allstate Ins. Co.*, 201 Cal. Rptr. 528, 546 (Ct. App. 1984) (noting that insurance company’s appointed defense attorney took advantage of the insured by “actively working to protect [the insurance company] ... and persisting in manipulating [the insured] ... against her own best interests”); *Rosenzweig v. Blinshteyn*, 544 N.Y.S.2d 865, 867 (App. Div. 1989) (defense counsel appointed by the insurance carrier adopted a defense to avoid the payment of any monies by the insurance company, regardless of the consequences to the insureds who were his “ostensible clients”).

245. See W. E. Shipley, *Duty of Liability Insurer to Settle or Compromise*, 40 A.L.R.2d 168, 178 (1988); Syverud, *supra* note 100, at 1116.

246. See, e.g., *Hall v. Svea Mut. Ins. Co.*, 493 N.E.2d 1102, 1104-05 (Ill. App. Ct. 1986).

protection or security which the insured sought to gain by buying insurance.”<sup>247</sup> Although in theory, under some set of facts, an insurer could harm the interests of an insured even where it settled a claim against the insured within policy limits (leaving the insured with no financial exposure), in practice, courts have rejected claims of the breach of the duty of good faith where the insurer settled within policy limits.<sup>248</sup> Following Charles Silver and Kent Syverud, I will call these “full coverage cases.” A claim of bad faith in a full coverage case turns on the insured’s uncompensated injuries that result from the insurer’s decision to settle the lawsuit (sometimes over the insured’s objection) and pay the entire amount of the settlement.<sup>249</sup> Full coverage cases are, therefore a useful place to test the limits, if any, which courts place on the alienation of control of litigation by insureds. In a full coverage case, an insured (or some other party) is asking a court to set aside a contract provision that gave the insurer control over the litigation, and the conflict is not over the amount of the settlement, but *how* the litigation is being conducted—that is, whether to settle at all.<sup>250</sup> In other words, the conflict is over the things that the insurer paid to have covered in the LCI, not the JCI—control over legal strategy and tactics, pure and simple.

In full coverage cases, insurance contracts are upheld as written, and without the slightest hesitation by the courts. The fact pattern that usually gives rise to challenges to insurer control of settlement involves doctors who object to their insurer settling medical malpractice claims within policy limits. Doctors often feel personally attacked when they are sued in medical malpractice and they believe, whether correctly or not, that settlements (if publicly known) injure their reputations.<sup>251</sup> Even if they are told that settlements arranged by their insurer will be sealed or protected from public access, doctors may try to insist on going to trial. They may feel that the allegations against them, unless categorically

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247. *Rawlings v. Apodaca*, 726 P.2d 565, 571 (Ariz. 1986) (en banc). The implied covenant of good faith and fair dealing can be traced back as far as the late nineteenth century. See *Brassil v. Md. Cas. Co.*, 104 N.E. 622, 624 (N.Y. 1914).

248. See Syverud, *supra* note 100, at 1159.

249. See Silver & Syverud, *supra* note 210, at 263.

250. See *id.* at 263-64.

251. See Eric Helland & Gia Lee, *Bargaining in the Shadow of the Website: Disclosure’s Impact on Medical Malpractice Litigation*, 12 AM. L. & ECON. REV. 462, 466 (2010).



rejected by a court, impugn their professional (and perhaps personal) character.<sup>252</sup> What doctors discover, once they are sued is that, “like auto liability policies, medical malpractice insurance policies for doctors typically give the insurer complete control over the defense and settlement of the claim.”<sup>253</sup> As one commentator stated, “These individuals have, of course, an option. They can defend at their own expense or they can bargain for ‘consent to settle’ provisions.”<sup>254</sup> The standard liability insurance contract does not require an insurer to go to trial or to pursue some other nonmonetary remedy (such as a public statement exonerating the doctor by the patient) if it settles within policy limits.<sup>255</sup>

The broad scope of control allowed under the standard liability insurance contract can be seen in *Hurvitz v. St. Paul Fire & Marine Insurance Co.*<sup>256</sup> The insureds (a physician and his wife) sued their former business partner (another physician) on various civil claims

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252. It is likely that the resistance by doctors to settlements in cases they feel are meritless—even if it costs them nothing financially—is something other people feel in other contexts. A driver might feel equally upset about a decision by her insurer to settle what, in the drivers’ mind, is a groundless claim in which she did nothing wrong.

The policyholder wishes to contest liability, perhaps to avoid the stigma of responsibility or the economic consequences of a finding of fault. A defense limited to the issue of damages may be perceived by the policyholder as an acknowledgment of legal responsibility. For some individuals such an admission may be difficult to make even in the face of clear evidence of fault. Some individuals can live with the vagaries of life. They will accept the decision to focus the litigation on minimizing the loss even though it means admitting, or being understood as admitting, responsibility for conduct they do not actually believe was legally wrongful. Other individuals will find such conduct morally and emotionally repugnant.

Fischer, *supra* note 11, at 40 (footnote omitted).

253. Tom Baker & Rick Swedloff, *Regulation by Liability Insurance: From Auto to Lawyers Professional Liability*, 60 UCLA L. REV. 1412, 1436 (2013).

254. Fischer, *supra* note 11, at 40. A “consent to settle” provision gives the insured control over whether to settle, but not the conduct of the litigation in other regards. Syverud, *supra* note 100, at 1175-76. Baker and Swedloff observe that consent to settle provisions, which insurers had freely offered (for a price) are disappearing as medical malpractice insurers seek new ways to “regulate” the conduct of physicians. See Baker & Swedloff, *supra* note 253, at 1436.

255. Syverud, *supra* note 100, at 1159; see *Webb v. Witt*, 876 A.2d 858, 867 (N.J. Super. Ct. App. Div. 2005) (absence of a consent to settle clause is not against public policy because “[p]resumably, the premium paid to the insurer reflects the presence or absence of a consent to settle clause”).

256. 135 Cal. Rptr. 2d 703, 705 (Ct. App. 2003). The analysis of *Hurvitz* and the accompanying footnotes are drawn substantially from my previous article, Sebok, *supra* note 5.

including defamation and intentional interference with contractual relationships.<sup>257</sup> The insureds were also subject to various counterclaims.<sup>258</sup> The insurer provided an attorney for all the claims except the intentional interference with contractual relationships (which it claimed was not within the scope of the policy's coverage).<sup>259</sup> The insurer agreed to a global settlement with the former partner dismissing all claims, including the intentional interference with contractual relationships and the counterclaims.<sup>260</sup> The settlement was secured by the insurer over the objections of the insureds.<sup>261</sup> The insureds sued the insurer, claiming that the settlement was favorable to the insurer and not favorable to the insureds.<sup>262</sup> The insureds also claimed that the insurer forced the insureds to accept the settlement by refusing to pay invoices of their independent defense counsel.<sup>263</sup> The trial court dismissed and the court of appeals upheld the dismissal.<sup>264</sup> The court conceded that the settlement imposed by the insurer harmed the insureds by exposing the insureds to unwanted media attention and cutting off their opportunity to pursue potentially valid counterclaims.<sup>265</sup> It held that these harms were the normal risks assumed by any insured who buys liability insurance.<sup>266</sup> The court said:

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257. *Hurvitz*, 135 Cal. Rptr. 2d at 705-06.

258. *Id.*

259. The insureds retained their own attorney to defend the intentional interference with contractual relationships claim. *Id.*

260. *Id.* at 707.

261. *Id.*

262. *Id.* at 708. According to the insureds, the settlement allegedly impaired the insureds' negotiating position, caused injury to their reputation, precluded them from filing a malicious prosecution action against their former partner, provided funds to the former partner to use to finance his defense of future lawsuits brought by the insureds, deprived the insureds of insurance financing for their future litigation against the former partner, and impacted the insureds' future insurability. *Id.*

263. *Id.*

264. *Id.*

265. *Id.* at 712.

266. *Id.* ("The decision to settle rather than continue litigation invariably involves a conflict between the desire to vindicate oneself and the desire to minimize the costs of litigation and avoid the risk of loss. Defendants who settle face an uphill battle in convincing others, including members of the interested public or the media, that they were completely innocent of the charges. Moreover, when a defendant pays money or gives up something of value to settle a claim, he or she loses the ability to later pursue a malicious prosecution claim.")

[T]hese are the ordinary consequences of settlement.... Liability insurance exists primarily to protect the insured's finances. The covenant of good faith and fair dealing requires the insurer to minimize the possibility of an award that exceeds the policy's limits—it does not require the insurer to fight a legal action until the bitter end when the costs of defense exceed the benefit to be achieved.<sup>267</sup>

The court noted the ironic twist in the insureds' complaint: the insureds "put[] a reverse spin" on the bad faith doctrine. Instead of arguing that the insurer breached the duty of good faith when it unreasonably *refused* to settle a case within policy limits, the insureds argued that the duty of good faith required the insurer to refuse any settlement which did not meet all of the insureds' legal interests—including a settlement which protected the insureds from an excess judgment.<sup>268</sup> The court reiterated the principle, which has been the focal point of this Article, that the law allows the complete alienation of an insured's party control as long as the insured is not exposed to an excess liability judgment.<sup>269</sup> The law does not require the insurer to take into account "the entire range of the insured's well-being;" it only requires the insurer to take into account the monetary judgment at risk in the claim against the insured.<sup>270</sup> The insurer, by contract, has unfettered discretion to handle that claim as long as policy limits are not in play.<sup>271</sup> Other cases have said the same thing.<sup>272</sup>

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267. *Id.* at 713.

268. *Id.* at 711 (citing *W. Polymer Tech., Inc. v. Reliance Ins. Co.*, 38 Cal. Rptr. 2d 78 (1995)).

269. *Id.* at 712.

270. *Id.*

271. *Id.*

272. *See, e.g.*, *Shuster v. S. Broward Hosp. Dist. Physicians' Prof'l Liab. Ins. Trust*, 591 So. 2d 174, 176-77 (Fla. 1992) ("[T]he insured was put on notice that the agreement granted the insurer the exclusive authority to control settlement and to be guided by its own self-interest when settling the claim for amounts within the policy limits."); Jon Epstein, *Liability of Insurer to Insured For Settling Third-Party Claim Within Policy Limits Resulting in Detriment to Insured*, 18 A.L.R. 5th 474, 507-08 (1994).

## CONCLUSION

The title of this Article needs some further explication. In truth, litigation investment does not raise control issues nearly as much as its critics claim.<sup>273</sup> The purpose of this Article has been to begin with the most extreme version of litigation investment painted by its critics and to ask, *even if that picture were accurate*, is there anything about it that offends the rule of law or the values of common law adjudication? In this Article, I have argued that the rule-of-law argument that is often used to such great rhetorical effect—that litigation investment allows strangers to take control of parties' lawsuits—would be underwhelming even if it were true. It turns out that in important parts of the common law, control over litigation is regularly alienated.<sup>274</sup> This fact alone should give us pause as to how seriously to take the rule-of-law arguments made by litigation investment's critics.

Two further lessons can be drawn from this Article. The first is that we should not ignore the very specific pattern of outcomes that emerges from a review of the common law's acceptance of the alienation of control over litigation. It is not my claim that the common law always had a liberal attitude toward the commodification of litigation. My claim is quite the opposite—the history of the common law reveals a clear evolution in the courts from a world informed by Blackstonian attitudes that were decidedly non-market

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273. Consumer litigation investment funders cannot exercise control over the cases in which they invest, since the contingent fee attorney—who in virtually all cases preexisted the funding—controls the case. Commercial litigation investment funding is a different story. In theory, funders could demand explicit control and entrench that control in their contracts. However, just like—and perhaps for the same reasons as—commercial lenders, commercial litigation investment funders do not seek enforceable contract rights to control major aspects of the litigation they fund. *See, e.g.*, Letter from Burford Group LLC to ABA Comm'n on Ethics 20/20 (Feb. 15, 2011), in *Comments: Issues Paper Concerning Lawyer's Involvement in Alternative Litigation Financing*, A.B.A., at 29, 33, available at <http://perma.cc/5C7V-K56T> ("Burford does not hire or fire the lawyers, direct strategy or make settlement decisions. Instead, Burford is a purely passive provider of non-recourse financing to a corporate party."); Letter from Juridica Capital Mgmt. (US) Inc. to ABA Comm'n on Ethics 20/20 (Feb. 17, 2011), in *Comments: Alternative Litigation Financing Working Group Issues Paper*, A.B.A., at 66, 72, available at <http://perma.cc/5C7V-K56T> ("We do not seek to control any of the decisions regarding the conduct of any litigation that we finance, nor are we aware of any other supplier in this market segment who does.").

274. *See supra* note 11 and accompanying text.

oriented to a world grounded in the Benthamite premise that litigation is nothing more than welfare maximization through the courts. We cannot ignore the fact that modern accident law and the insurance industry could not exist without the changes in the law of subrogation and third-party liability contract detailed above, and that those changes clearly illustrate how jurisprudential attitudes about law bend in the face of social necessity.<sup>275</sup>

In 1920, Holdsworth demonstrated how the prohibition on the assignment of choses of action was gradually hollowed out from within, until the exceptions swallowed the rule.<sup>276</sup> His explanation for the inexorable move towards the modern rule of free assignability was that “the common law was induced to connive at the introduction and extension of this evasion of its principle[s] ... by considerations of mercantile convenience or necessity.”<sup>277</sup> In 1936, Radin demonstrated how an exception to the prohibition of champerty was created out of whole cloth to allow for the contingency fee.<sup>278</sup> His explanation for the inexorable move towards the modern rule of allowing lawyers to take a share of the recovery in a lawsuit was that “the growth of contingent fees coincided with the rapid increase of actions for negligence which accompanied the multiplication of new forms of rapid transportation [as well as] the ... widespread feeling that the safety of passengers and ordinary pedestrians ought to be insured by transportation companies.”<sup>279</sup> In each of these developments, critics raised formal barriers of the

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275. The idea that changes in doctrine made the development of certain economically desirable features of modern society (such as insurance) possible, is not a controversial claim. All I am doing here is acknowledging law's instrumentalist relationship between itself and the larger society, especially economic institutions. See William J. Novak, *Law, Capitalism, and the Liberal State: The Historical Sociology of James Willard Hurst*, 18 *LAW & HIST. REV.* 97, 122 (2000) (discussing Hurst's legal instrumentalism). I am not taking a position on the more controversial question of whether changes in legal concepts in some way “cause” certain economic institutions to arise, or create the conditions for such institutions to arise, or were a result of social forces independent of the legal system. See John Fabian Witt, *Toward a New History of American Accident Law: Classical Tort Law and the Cooperative First-Party Insurance Movement*, 114 *HARV. L. REV.* 690, 693 n.7 (2001) (suggesting that, in contrast with his method, Morton Horwitz focused more on “intellectual currents in tort law theory rather than on the role of tort law in the great social struggles of the day”).

276. Holdsworth, *supra* note 120, at 997-98.

277. *Id.* at 1021-22.

278. Radin, *supra* note 40, at 71.

279. *Id.*

common law's established principles to block them, notwithstanding their social utility.<sup>280</sup>

Litigation investment stands in the same place now that the law of assignment and the law of lawyer champerty stood before. Objections based on abstract theories about how litigation must be structured are being raised in order to slow down or reverse the growth of litigation investment. Once claims about party control based on theoretical or formal concerns have been rejected, litigation investment's critics will have to frame their opposition entirely in terms of social costs and benefits. The argument that litigation finance will produce major social costs is a thinly-veiled repetition of claims already made against entrepreneurial plaintiff lawyering in general.<sup>281</sup> This Article is not intended to take up the social cost argument, but will touch on it briefly here.

In response to the argument that litigation investment will cost society dearly, one only needs to look to the publications by scholars and policymakers who have argued that litigation investment has the potential to increase social welfare, and conversely that there is little reason to believe that it will cause a loss in social welfare.<sup>282</sup> Scholarship in this vein ranges from law and economic analyses showing that litigation investment will generate efficient settlements by helping parties to price their claims accurately<sup>283</sup> to arguments that litigation investment will help underserved populations have more secure and adequate compensation for the wrongs they have suffered.<sup>284</sup>

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280. *Id.*

281. See, e.g., *Can We Sue Our Way to Prosperity?: Litigation's Effect on America's Global Competitiveness: Hearing Before the Subcomm. on the Constitution of the H. Comm. on the Judiciary*, 112th Cong. 49-51 (2011) (testimony of John H. Beisner, U.S. Chamber Institute for Legal Reform) (stating that in addition to the loss of party control, the other arguments against litigation investment are: (i) reducing plaintiff's recovery; (ii) increasing frivolous litigation; and (iii) unnecessarily prolonging litigation at the expense of the plaintiff).

282. See Michele DeStefano, *Claim Finders and Commercial Claim Holders: A Common Interest or a Common Problem?*, 63 DEPAUL L. REV. 305, 305-06 (2014); Keith Hylton, *Toward a Regulatory Framework for Third-Party Funding of Litigation*, 63 DEPAUL L. REV. 527, 537-39 (2014); Samuel Issacharoff, *Litigation Funding and the Problem of Agency Cost in Representative Actions*, 63 DEPAUL L. REV. 561, 582-85 (2014); Susan Lorde Martin, *The Litigation Financing Industry: The Wild West of Finance Should Be Tamed Not Outlawed*, 10 FORDHAM J. CORP. & FIN. L. 55, 67-72 (2004); Molot, *supra* note 227, at 407-11; Molot, *supra* note 7, at 107. See generally Steinitz, *supra* note 25.

283. See generally Hylton, *supra* note 282; Molot, *supra* note 227; Molot, *supra* note 7.

284. See generally Martin, *supra* note 282; Steinitz, *supra* note 25.

Recently the President of the Supreme Court of the United Kingdom, Lord Neuberger, reviewed the gradual shift in English law from prohibiting to encouraging litigation investment.<sup>285</sup> The common law's prohibition of litigation investment, Neuberger argues, was based on the circumstances of its times, which required the new court system and an economy that was emerging out of feudalism to be protected against the abuse of litigation by powerful aristocrats.<sup>286</sup> But as the circumstances of the judicial system and the economy changed, so did the need for prohibitions on litigation investment.<sup>287</sup> As the English Court of Appeals noted in 1895, the rules concerning litigation investment "do[] not appear to be founded so much on general principles of right and wrong or of natural justice as on considerations of public policy."<sup>288</sup> Neuberger notes that by the nineteenth century, the prohibitions on litigation investment themselves imposed costs on English society:

It is ... ironic. The original, medieval, rationale for the prohibitions was to protect the poor and weak from exploitation by the rich and powerful.... The later, 19th century, rationale was, in practice if not in theory, to the opposite effect: a person had to be independently wealthy to bring a case to court.... Their effect was, to borrow Bentham's conclusion, to give wealth the "*monopoly of justice against poverty*."<sup>289</sup>

As of 2013, Lord Neuberger observes that the argument concerning litigation investment "has come full circle": anyone concerned with the promotion of the rule of law should "positively ... support the development of litigation funding, as a means of securing effective access to justice."<sup>290</sup>

The second lesson to be drawn from this Article can be stated quite briefly. Just as the courts accommodated new attitudes toward

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285. Neuberger, *supra* note 12.

286. *Id.* at 9-10.

287. *Id.* at 10.

288. *Id.* at 13 (quoting *Alabaster v. Harness*, [1895] 1 Q.B. 339 at 342 (Eng.)).

289. *Id.* at 14 (emphasis added).

290. *Id.* at 20-21. Radin said the same thing eighty years earlier: "The shoe is really on the other foot. If in medieval England, powerful men oppressed their weaker fellow subjects by maintaining suits against them, in modern society powerful people are more likely to achieve their ends by daring their victims to maintain suits." Radin, *supra* note 40, at 77-78.

the alienation of control of litigation in insurance law, so should courts accommodate the alienation of control of litigation in litigation investment—assuming that some social benefit results. In response to the real risks caused by the transfer of party control to vulnerable parties, insurance law developed protective doctrines, such as the tort of bad faith and the make-whole doctrine, which in coordination with more liberal attitudes toward contract enforcement provide a balance that fits the needs of society. If such a balance could be achieved with insurance law, there is no reason to think that the same could not be achieved with third-party investment in litigation.

The fact that insurance law is the primary lens through which the argument of this Article has been made is not a coincidence. Like the litigation investment contract, the insurance contract is a social instrument.<sup>291</sup> Seeing insurance as a social instrument means that insurance law is not a two-step process in which the legal meaning of the contract is first determined using value-free legal tools, and then second, the contract's scope is either fully enforced or limited based on the court's non-legal, public policy preferences.<sup>292</sup> Instead, thinking about the types of social problems the insurance contract at issue was meant to solve provides an expanded menu of reasons with which to interpret the contract.<sup>293</sup> Although Jeff Stempel was not thinking specifically about the sale of party control when he applied his approach to various insurance contract disputes, we can see that his approach fits the judicial treatment of the contract terms examined above in disputes over control in subrogation—full coverage cases and litigation investment. In each of these, the reason for enforcing the contract was twofold. First, the main risks, which the contracts were designed to mitigate, were not increased or exacerbated by the sale of party control. Second, the sale of party control was arguably the least expensive way for the party providing funds (the insurer or the investor) to mitigate the risk that the other party (the insured or the claimant) would abandon the joint project that the contract created.

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291. See Stempel, *supra* note 12, at 1495-99.

292. *Id.* at 1582.

293. The "social instrument factor ... complements rather than supplants traditional contract analysis." *Id.*



So what do we say to critics who point out that litigation finance contracts might become a vehicle for socially wasteful litigation? The answer must be that absent evidence to the contrary, the risk of abuse must be permitted and dealt with in some other fashion. In reflecting on the persistence of the rules prohibiting litigation investment, Radin speculated that “[i]t is indubitably easier to reject all [champertous] agreements ... in bulk or to accept them in bulk.”<sup>294</sup> But, Radin noted, this is not an attitude toward law that we should encourage.<sup>295</sup> The appropriate response to the fact that some litigation investment contracts may be used for improper purposes or end up supporting groundless litigation is not to abolish litigation investment, but to develop, as we have in other useful areas of legal innovation, better processes of law.<sup>296</sup>

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294. Radin, *supra* note 40, at 78.

295. *Id.*

296. *Id.* at 72 (“If champertous contracts can serve any good purpose—and they apparently can—it is not foresight, but the infantile psychosis of ‘all-or-nothing’ which demands that we discard them altogether.”).

