

# LITIGATION FOR SALE

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## INTRODUCTION

In recent years, several litigation investment companies have appeared.<sup>1</sup> Typically, these companies acquire the rights to patent-infringement suits from private inventors who cannot finance their own lawsuits.<sup>2</sup> These investment companies may then syndicate the lawsuits, that is, sell shares in the lawsuits to raise money to finance the litigation.<sup>3</sup> The potential returns, although highly speculative, are enormous.<sup>4</sup> The syndication market is relatively new, but one company is considering plans to acquire a portfolio of lawsuits and sell shares in the fund to investors.<sup>5</sup>

Buying lawsuits is not a new concept. The ancient common law doctrine of champerty made illegal all agreements to share in the proceeds of another's lawsuit.<sup>6</sup> At common law, speculating in litigation was against public policy.<sup>7</sup> Although much of the common law on champerty has eroded to near obsolescence,<sup>8</sup> the core of the doctrine—the public policy against profiteering and speculating in litigation—still survives in most states.<sup>9</sup>

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<sup>1</sup> See Linda Himelstein, *Investors Wanted—For Lawsuits*, BUS. WK., Nov. 15, 1993, at 78, 78; see also Reynolds Holding, *Investing in Other People's Lawsuits*, S.F. CHRON., Jan. 12, 1996, at B1 (discussing Judgment Purchase, a company that buys shares in judgments on appeal).

<sup>2</sup> See Himelstein, *supra* note 1, at 78.

<sup>3</sup> See Cynthia L. Cooper, *Champerty, Anyone?*, CAL. LAW., Jan. 1991, at 19, 19.

<sup>4</sup> For example, in 1990, investors who financed a lawsuit won a verdict worth an estimated \$63 million. See Leslie Spencer, *Some Call It Champerty*, FORBES, Apr. 30, 1990, at 72, 72.

<sup>5</sup> See Telephone Interview with Roger Dillan, President, WBX Partners (Feb. 1994).

<sup>6</sup> See 14 AM. JUR. 2D *Champerty & Maintenance* § 7 (1964).

<sup>7</sup> See 14 C.J.S. *Champerty & Maintenance* § 2 (1991).

<sup>8</sup> See 14 AM. JUR. 2D *Champerty & Maintenance* § 1 (1964) (“In none of the states are the doctrines or laws of champerty and maintenance preserved in their original rigor. In many states they are declared to be obsolete and to have no existence at all.”).

<sup>9</sup> For a discussion of the modern status of champerty laws, see *infra* part III.B.

Despite these laws against investing in litigation, modern lawsuit investors have achieved some success in fending off legal challenges to their syndicated lawsuits. In 1978, in the first modern syndicated lawsuit, *Thee v. Parker Bros.*,<sup>10</sup> Carl E. Person, the plaintiff's attorney, was able to "cut through the . . . maze"<sup>11</sup> of legal technicalities and obtain clearance from the Securities and Exchange Commission, the New York Bureau of Securities, the American Bar Association, and a federal court to offer shares in an antitrust suit against a gamemaker who copied the plaintiff's game.<sup>12</sup> Although the plaintiff ultimately prevailed, the offering of shares in the lawsuit failed due to poor investor interest.<sup>13</sup> More than a decade later, in 1991, two California investors fended off a challenge to the legality of one of the most successful lawsuit syndications ever.<sup>14</sup> One company that invests in disputed intellectual property rights is publicly traded.<sup>15</sup> However, it has encountered judicial hostility to its business.<sup>16</sup>

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For a discussion of the policy against speculation in litigation, see *infra* part IV.D.1.

<sup>10</sup> [1978-1981 Transfer Binder] Copyright L. Dec. (CGH) ¶ 25,017 (E.D.N.Y. Mar. 9, 1978).

<sup>11</sup> INTELLECTUAL PROPERTIES, INC., OFFERING CIRCULAR UNDER SEC RULE 154A EXEMPTION 8 (1993) (available on the Internet (<http://www.lawmall.com>)) [hereinafter OFFERING CIRCULAR].

<sup>12</sup> See *id.*; see also *A Scheme to Sell Pieces of an Action*, BUS. WK., May 24, 1976, at 35, 35-36 (discussing a New York lawyer's scheme to finance a lawsuit by selling 100,000 shares through an unregistered stock offering).

<sup>13</sup> See Daniel C. Cox, Comment, *Lawsuit Syndication: An Investment Opportunity in Legal Grievances*, 35 ST. LOUIS U. L.J. 153, 154-56 & nn.9-25 (1990) (discussing the *Thee* case); see also OFFERING CIRCULAR, *supra* note 11, at 8 ("Because the *Thee* offering was self-underwritten and neither *Thee* nor *Person* was in the business of selling stock of any kind, the offering was discontinued for lack of any substantial dollar amount of subscriptions.").

<sup>14</sup> See *Killian v. Millard*, 228 Cal. App. 3d 1601, 1607 (Ct. App. 1991); Spencer, *supra* note 4, at 72.

<sup>15</sup> Refac Technology is engaged in international licensing and technology transfer and trades publicly on the American Stock Exchange. See *CEO Interview: Refac Technology Development Corporation*, WALL ST. TRANSCRIPT, Dec. 26, 1994, at \*1, available in Westlaw, Allnews Database. According to the company's CEO, "[o]ccasionally, we confront situations where the patent rights of a client seem to be infringed by third parties—and . . . we may consider it necessary to litigate." *Id.* at \*2.

<sup>16</sup> See *Refac Int'l, Ltd. v. Hitachi, Ltd.*, 921 F.2d 1247, 1256-57 (Fed. Cir. 1990) (affirming the district court's dismissal of a patent infringement suit, imposing sanctions in excess of \$200,000 for filing a frivolous appeal, reversing the lower court's denial of Rule 11 sanctions, and remanding for further Rule 11 sanction proceedings); *Refac Int'l, Ltd. v. Hitachi Ltd.*, 141 F.R.D. 281, 284 (C.D. Cal. 1991) (awarding, on remand, close to \$1.5 million in Rule 11 sanctions against Refac); *Refac Int'l, Ltd. v. Lotus Dev. Corp.*, 131 F.R.D. 56, 58 (S.D.N.Y. 1990) (invalidating Refac's purchase of patent infringement claims on the ground that the agreement was

This Comment discusses the legal impediments to investing in litigation and focuses on reaching concrete and specific conclusions on the viability of and limitations on such investment. To facilitate a more realistic assessment of the practical impact of these legal impediments to litigation investment, the legal analysis is conducted through a hypothetical litigation investment company, "Champerco."

Part I uses a law and economics approach to explore the basic premise underlying this Comment: There is a market for investor-financed litigation. Part I demonstrates some of the benefits of investor-financed lawsuits and, in the process, refutes some popular objections to the practice. Part II sets forth a blueprint for a company designed to meet the market demand for investor-financed litigation envisioned in Part I. Part III discusses the history, policies, and modern status of the law on champerty. Part IV examines the practicability of contracting around champerty laws in light of modern conflicts law and concludes that three steps can be taken to create enforceable champertous agreements.

## I. THE MARKET FOR LITIGATION FINANCING

Litigation is an investment process.<sup>17</sup> Traditionally, plaintiffs pay their litigation expenses as they arise during the progression of their lawsuits. These payments are "investments" by plaintiffs.<sup>18</sup> Often, however, plaintiffs will decide not to invest in their lawsuits. Litigation can drag on for years and the costs can add up tremendously<sup>19</sup> without any guarantee of a recovery. With prospects of any recovery uncertain and, in any event, months or years away, many plaintiffs may find it too risky to "invest." Even a plaintiff willing to make the risky investment in his lawsuit may not have the

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"nothing but a hunting license"); *Refac Int'l, Inc. v. IBM Corp.*, 710 F. Supp. 569, 572 & n.1 (D.N.J. 1989) (finding Refac's patent infringement suit frivolous and ordering Refac to pay defendants' attorneys fees, estimated to be \$2.5 million).

<sup>17</sup> See David M. Trubek et al., *The Costs of Ordinary Litigation*, 31 UCLA L. REV. 72, 76-77 (1983) (conceptualizing litigation as "the investment of scarce resources to achieve a future result").

<sup>18</sup> See *id.*

<sup>19</sup> See 1994 FEDERAL COURT MANAGEMENT STATISTICS 167 (reporting that in 1994 the median duration, from filing to trial, of all federal district court civil cases was 18 months, and that 6.2% of all cases on the courts' dockets were more than three years old); A. Leo Levin & Denise D. Colliers, *Containing the Cost of Litigation*, 37 RUTGERS L. REV. 219, 227-29 (1985) (discussing the continuing increases in the cost of civil litigation).

economic means to do so. These plaintiffs may abandon their claims unless there are alternative, less costly or less risky, methods of financing their lawsuits.

While borrowing against a claim is theoretically possible, in reality, banks and other lending institutions are unlikely to make such risky loans.<sup>20</sup> A better alternative might be to sell the lawsuit. Rather than abandoning a lawsuit because it is an unaffordable or risky "investment," a plaintiff can sell the lawsuit to an investor who believes that the lawsuit is a good investment. Alternatively, a plaintiff can sell shares in his lawsuit to raise money to finance the suit. This practice is actually widespread.<sup>21</sup> Theoretically, in contingent fee agreements, plaintiffs sell their lawsuits to entrepreneurial lawyers in exchange for a share of the profits. Viewed another way, contingent fee lawyers buy shares in lawsuits and pay with legal services instead of cash.<sup>22</sup>

Underlying the concept of buying and selling lawsuits is the assumption that a lawsuit might be worth more to one party (that is, the investor) than to another (that is, the plaintiff). Using law and economics analysis, this Part explores the factors that make lawsuits more valuable to one person than another. This analysis will reveal the efficiency and benefits of the free trade of claims.<sup>23</sup>

#### A. *Risk-Bearing and the Willingness to Litigate Claims*

The most significant factor that makes a claim more valuable to one party than another is the difference in the parties' relative risk-bearing abilities. There are several factors that affect a party's risk-bearing ability. One factor is a party's wealth. To illustrate the effect of a party's wealth on its risk-bearing ability and, thus, on the

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<sup>20</sup> See RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 567 (4th ed. 1992). The highly speculative proceeds of litigation are too risky for traditional lenders, many of whom are government regulated, to lend against, and the appropriate interest rates for loans with this risk grade may run afoul of usury laws. Also, the costs to lending institutions of valuing the borrower's claim may be prohibitively expensive. Furthermore, certain types of claims, such as tort claims, are generally unassignable. See *id.*

<sup>21</sup> See Roy D. Simon, Jr., *Lawsuit Syndication: Buying Stock in Justice*, 69 *BUS. & SOC'Y REV.* 10, 13 (1989) (arguing that contingent fee arrangements, factoring, and public interest litigation are existing examples of lawsuit syndication).

<sup>22</sup> See generally POSNER, *supra* note 20, at 567 (describing the contingent fee agreement as a contract where "[t]he lawyer lends his services against a share of the claim").

<sup>23</sup> *Id.* at 567-69.

value it places on a claim, consider the following two hypothetical scenarios.<sup>24</sup>

First, suppose someone holds the winning ticket to a \$150,000 lottery, but the lottery company refuses to honor the ticket because it claims that the ticket is a forgery. The ticket holder consults with a lawyer, who informs her that it will cost \$25,000 to sue the lottery company and that she will have a 50% chance of recovering the \$150,000 jackpot. The ticket holder, hereinafter the "blue collar plaintiff," has savings totalling only \$25,000. After weighing the 50% chance of recovering \$125,000 (after costs) against the 50% chance of losing \$25,000, her entire life savings, she decides that a \$25,000 loss would be too devastating to her financial position, and she simply "cannot afford" to take that risk. She feels that she has worked too hard to save the \$25,000 to just "gamble" it away on a lawsuit. She, therefore, abandons her claim.

Second, suppose the same facts as the first scenario, except that the ticket holder, hereinafter the "white collar plaintiff," is a wealthy investor. To the white collar plaintiff, the lawsuit is an excellent investment opportunity. With an average recovery of \$75,000 and a cost of only \$25,000, he can earn a hefty 200% return by "investing" in the lawsuit. He can afford the risk of a \$25,000 loss, as it would only marginally affect his total wealth. He, therefore, hires a lawyer and sues the lottery company.

As these two scenarios illustrate, the same claim that one party abandons without any recovery is pursued by another party for an average recovery of \$50,000 (after litigation costs). The difference between the two plaintiffs is their risk-bearing abilities. The white collar plaintiff is a better risk bearer simply because the claim constitutes a much smaller percentage of his wealth.<sup>25</sup> The risk is diversified with the rest of his wealth. This difference in risk-bearing abilities creates a difference in valuation between the blue

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<sup>24</sup> These hypotheticals are variations on a simpler hypothetical posed by Richard Posner. *See id.* at 567 (exploring a hypothetical in which a plaintiff has a claim of \$100,000 with a 50% probability of success).

<sup>25</sup> The theory of risk averseness is a corollary of the theory of the diminishing marginal utility of money. *See* ROBERT COOTER & THOMAS ULEN, *LAW AND ECONOMICS* 58 (1988). The rate of decrease in the marginal utility of money decreases with increases in wealth. Therefore, a party's degree of risk averseness decreases with increases in wealth. *See id.* In simple terms, \$25,000 is a much smaller percentage of the white collar plaintiff's wealth than it is of the blue collar plaintiff's wealth.

collar plaintiff, for whom the claim is worth nothing, and the white collar plaintiff, for whom the claim is worth close to \$50,000.<sup>26</sup>

The different values the two plaintiffs place upon the claim creates an opportunity for a mutually beneficial trade. Rather than abandoning her claim, the blue collar plaintiff can sell her claim to the white collar plaintiff. Suppose, for example, the blue collar plaintiff sells the lottery ticket for \$10,000 to the white collar plaintiff. To the white collar plaintiff, a \$40,000 average return on a \$35,000 investment far exceeds the market rate of return.<sup>27</sup> To the blue collar plaintiff, a guaranteed \$10,000 gain is preferable to abandoning her lawsuit and recovering nothing. The sale of the lottery ticket will, therefore, benefit both parties. The only loser in this sale is the lottery company, which might now be forced to honor the lottery ticket.<sup>28</sup> These two hypotheticals illustrate the potential gains from the free trade of claims from poor risk-bearing parties to better risk-bearing parties. These potential gains from trade create a market for litigation.<sup>29</sup> As with the free trade of other property, the gains are efficient and beneficial.<sup>30</sup>

Another factor that affects a party's risk-bearing ability is the party's risk diversification. A party owning many risky claims is better able to bear the risk of any particular claim and will, therefore, value the claim higher than another nondiversified

<sup>26</sup> The claim is worth nothing to the blue collar plaintiff because she will abandon the claim. The white collar plaintiff will pursue the claim with a 50% chance of winning \$150,000, for an average recovery of \$75,000. Because it will cost him \$25,000 in litigation costs to litigate the claim, his average return is \$50,000. This amount must be risk-discounted because even the white collar plaintiff would prefer a guaranteed \$50,000 to the lottery ticket.

<sup>27</sup> With a 50% chance of recovering \$150,000, the average expected recovery is \$75,000. The lawsuit costs \$35,000, \$10,000 to buy it and \$25,000 to litigate it, making the average expected profit \$40,000, an expected return of 114%.

<sup>28</sup> One of the most popular objections to the sale of lawsuits is that it foments litigation. For a discussion of this objection, see *infra* part IV.D.2. See also Simon, *supra* note 21, at 11-12 (discussing the argument that "syndication stirs up [frivolous] litigation"). This morally infused hypothetical exposes a fundamental flaw in this objection. When a lottery company takes advantage of the helplessness of a poor lottery winner, no one would argue that a lawsuit to vindicate her rights should be discouraged. Meritorious litigation should not be discouraged, and as demonstrated here, the fact that the blue collar plaintiff would not have brought this lawsuit does not reflect negatively on the merits of the claim. It is simply a consequence of the blue collar plaintiff's poor risk-bearing ability.

<sup>29</sup> See POSNER, *supra* note 20, at 10 ("[R]esources tend to gravitate toward their most valuable uses if voluntary exchange—a market—is permitted.")

<sup>30</sup> See generally *id.* at 12-16 (discussing the desirability of an economically efficient exchange).

party.<sup>31</sup> Returning again to the lottery ticket scenario, suppose that several other lottery companies, on rumors of rampant lottery ticket counterfeiting, have all refused to honor winning lottery tickets. The white collar plaintiff, pleased with his 114% expected return on the disputed winning lottery ticket he purchased, seeks out more blue collar plaintiffs who "cannot afford" to litigate their claims and purchases fifty more disputed winning lottery tickets for \$10,000 each. Assuming that the outcome of each lottery ticket lawsuit is independent of the others, the more claims the white collar plaintiff purchases, the more he will be willing to pay for them. The reason is that, by owning many claims, the white collar plaintiff diversifies out much of the riskiness of the claims so that the risk-discounted value of the claims to him is close to the full \$50,000 average expected recovery. Put another way, by eliminating the riskiness of his investment, he can afford to accept a lower rate of return.<sup>32</sup> Furthermore, because his portfolio of lottery tickets is diversified, he can obtain a loan against the lottery tickets, which allows him to leverage his investment even more. Taking diversification a step further, if the white collar plaintiff pools all his lottery tickets and syndicates them, he can afford to pay even more for each claim, since he has reduced the risk to a level that an ordinary investor can afford and, thus, has a much lower cost of capital.

### B. *Secondary Benefits of Superior Risk-Bearing*

Although it is generally in the best interests of litigants to settle their disputes,<sup>33</sup> litigants often do not settle, or settle only after spending huge sums on litigation. This failure is due in large part to the strategic bargaining behavior of the parties.<sup>34</sup> At least two

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<sup>31</sup> Contingent fee lawyers are an example of a diversified claim-holder. By virtue of their holding a stake in several claims, they are diversified and place a greater value on any particular claim than a nondiversified party, such as a private plaintiff. *See id.* at 567 (discussing the advantage of contingent fees: "Risk is reduced because the lawyer specializing in contingent fee matters can pool many claims and thereby minimize the variance of the returns").

<sup>32</sup> *See id.* (discussing how a contingent fee attorney pools many claims to reduce risk and minimize variance of the returns).

<sup>33</sup> Through settlement, both parties can save their respective costs of litigation. *See* Robert Cooter et al., *Bargaining in the Shadow of the Law: A Testable Model of Strategic Behavior*, 11 J. LEGAL STUD. 225, 225 (1982) (stating that a trial "represents a bargaining breakdown").

<sup>34</sup> *See* COOTER & ULEN, *supra* note 25, at 487-92 (describing strategic bargaining problems that occur in settlement negotiations). *But see* Russell Korobkin & Chris Guthrie, *Psychological Barriers to Litigation Settlement: An Experimental Approach*, 93

types of strategic bargaining problems can be cured by the free trade of claims to better risk-bearing parties: threat credibility and bilateral monopolies.

### 1. The Credibility of the Threat to Litigate

Returning once again to the first lottery ticket scenario, the lottery company, correctly assuming that the blue collar plaintiff will abandon her claim, will not offer her even a minimal settlement. If she threatens to sue the lottery company, the lottery company will call her bluff, rationally assuming that she is unwilling to gamble her life's savings on the lawsuit. Suppose, however, that the blue collar plaintiff decides to commence the lawsuit against the lottery company to bolster her threat of litigation in the hopes of inducing a settlement offer. She spends \$2000 on legal fees to file a complaint. At this point, the lottery company will take her threat to litigate a bit more seriously, although not seriously enough to make her a good faith settlement offer. On the outside chance that she is actually willing to gamble \$25,000 and litigate, the lottery company will offer her a \$5000 settlement. The theory is that, even if she is actually willing to gamble \$25,000; she will not be willing to gamble \$28,000.<sup>35</sup> The blue collar plaintiff, seeing the success of her bluff, might reject the \$5000 settlement offer and continue to bluff her willingness to gamble \$28,000 on the lawsuit, in the hopes that the lottery company will continue its behavior and offer a larger settlement. To bolster her threat to litigate, she might have to spend another \$3000 on legal fees to commence discovery. The lottery company, in turn, might counter with a \$10,000 settlement offer and, thus, increase the gamble to \$30,000.<sup>36</sup> This process will continue until either the plaintiff is satisfied with the lottery company's settlement offer or the lottery company calls her bluff and takes all settlement offers off the table.

The ability to bluff, a strategic bargaining tactic, helps the blue collar plaintiff who is not actually willing to gamble on her lawsuit, by allowing her to extract at least some settlement. If the blue collar plaintiff, however, is not bluffing but seriously intends to go forward with her lawsuit, the ability to bluff hurts her, because her

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MICH. L. REV. 107, 117 (1994) (describing psychological impediments to settlement).

<sup>35</sup> \$28,000 represents the foregone \$5000 settlement offer plus the additional \$23,000 necessary to prosecute the claim.

<sup>36</sup> \$30,000 represents the foregone \$10,000 settlement offer plus the additional \$20,000 necessary to prosecute the claim.



threat to litigate is not credible and, thus, will not bring the lottery company to the bargaining table with a good faith settlement offer. If the lottery company knew that the blue collar plaintiff's threat to litigate was serious, they would prefer to settle and save the costs of litigation. But the lottery company rationally assumes that she is bluffing. The problem is that the plaintiff cannot convince the lottery company to take her threats seriously until she spends substantial amounts of money on litigation, at which point much of the settlement gains have been spent.

In contrast, this problem would not occur with the white collar plaintiff.<sup>37</sup> The lottery company, knowing that it would be perfectly rational for the white collar plaintiff to "invest" \$25,000 in his lawsuit, will not be skeptical of the white collar plaintiff's threats to litigate. Therefore, the lottery company will make a good faith settlement offer immediately, and both parties will save the costs of litigation. The credibility of the threat to litigate is even stronger when the plaintiff is a litigation investment company, whose business is to invest in and conduct litigation. The moral of the story: When claims are traded from poorer risk-bearing parties to better risk-bearing parties, aside from the inherent efficiency gains, there are secondary gains from removing inefficient strategic bargaining problems that disrupt settlement.<sup>38</sup>

## 2. Bilateral Monopolies

In settlement negotiations between a plaintiff and a defendant, the defendant attempts to "buy" or settle the plaintiff's claim, and the plaintiff seeks to "sell" the claim to the defendant. The parties bargain over the price of this sale. Because the defendant is the only buyer interested in the plaintiff's claim, the defendant can threaten to walk away from the bargaining table (that is, force a trial) if the plaintiff asks too high a price. Simi-

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<sup>37</sup> See Simon, *supra* note 21, at 11 (noting that "by giving claim holders the financial power to litigate properly and the staying power to go to trial if necessary, [lawsuit] syndication helps claimants obtain more favorable settlements").

<sup>38</sup> Ironically, one of the policy arguments advanced against selling lawsuits is that it discourages settlement. See Killian v. Millard, 228 Cal. App. 3d 1601, 1604 (Ct. App. 1991) (citing the lower court's opinion that champertous agreements are against public policy because they "discourage[] settlements"). This argument confuses the ability to extract a higher settlement with the willingness to settle. See Simon, *supra* note 21, at 12-13 ("It is true that wealthy plaintiffs can afford trial better than poor plaintiffs, but that is likely to translate into more favorable settlements, not more trials.").

larly, because the plaintiff is the only one who can sell the claim to the defendant, the plaintiff can also threaten to walk away from the sale (that is, go to trial) if the defendant offers too little. This is a bilateral monopoly, a situation in which both parties have an incentive to hold out for a better deal.<sup>39</sup> This holdout problem causes the parties to litigate (either to bolster their holdout threats or because the settlement negotiations have reached an impasse) even though settling would be beneficial to both parties.<sup>40</sup>

The ability to sell claims destroys this bilateral monopoly and cures the holdout problem. From the plaintiff's point of view, the defendant's holdout threat is useless because there are other buyers who are competing to purchase the plaintiff's claim. From the defendant's point of view, holding out for a lower sale price might result in the sale of the claim to a third party who is more eager to go to trial and will not be forced into settlement by the defendant's holdout. The plaintiff has less of an incentive to hold out as well, because his high demands will drive other potential buyers away and he will lose his threat to sell the claim. In this manner, the sale of lawsuits eliminates another strategic bargaining obstacle to settlement.

In summary, there are potential gains from the sale of claims, which indicate the existence of a potential market for the trade of claims and argue for the encouragement of claim-trading. Furthermore, as the lottery ticket hypothetical illustrates, contrary to popular belief, the trade of claims may promote equity as well as efficiency.<sup>41</sup>

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<sup>39</sup> See generally EDWIN MANSFIELD, MICROECONOMICS: SELECTED READINGS 296-97 (3d ed. 1976) (discussing the bilateral monopoly problem).

<sup>40</sup> By settling, the parties gain, not only by eliminating the costs of litigation, but also by eliminating the risk of the uncertain outcome of the litigation.

<sup>41</sup> See generally Peter C. Choharis, *A Comprehensive Market Strategy for Tort Reform*, 12 YALE J. ON REG. 435, 435 (1995) (arguing that a market for selling, purchasing, and trading tort claims "will benefit tort victims with quicker, higher, and certain damage awards; offer defendants numerous ways to hedge their liability; reduce crowded court dockets and induce faster, fairer settlements; and help society by retaining appropriate safety incentives and allocating the costs of accidents to those most able to bear them"); Simon, *supra* note 21, at 11 ("Syndicating lawsuits has advantages for both individuals and the public at large.").

## II. CHAMPERCO

In light of the market for claim trading explored in the previous Part, this Part defines a hypothetical litigation investment company, appropriately named Champerco, that will be used throughout the rest of this Comment as a vehicle for analyzing the legal limitations to investing in litigation.

Champerco is a publicly traded New Jersey corporation that seeks to develop a market for claim trading. Champerco's operations are divided among three departments: Claim Procurement, Litigation, and Investor Services.

### A. Claim Procurement

Champerco advertises in law journals and other legal publications, offering a variety of financial services for litigants. These advertisements are targeted at lawyers whose clients are either in need of financial assistance to prosecute their claims, in need of cash while they wait for their expected recovery, seeking alternative billing arrangements, or simply looking to "cash out" of their lawsuits without further involvement.<sup>42</sup> As an incentive, referring lawyers receive a fee for their referrals. Champerco also targets lawyers who have taken cases on a contingent fee basis but need financial or other support for the prosecution of their clients' claims.

Champerco advertises in trade journals and other business publications, as well. These advertisements are targeted at potential plaintiffs, typically inventors, who have been discouraged from prosecuting their patent, copyright, or antitrust claims because they lack the funds or cannot afford the risks of litigation. On occasion, Champerco engages in more active solicitation of clients through mass mailings or direct contact with potential clients. Champerco also actively solicits trustees in bankruptcy and other receivers or administrators, whose duty it is to liquidate a business or estate, and offers them immediate cash for their claims.<sup>43</sup>

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<sup>42</sup> See Simon, *supra* note 21, at 11 ("Alternatively, claim holders who choose to sell their entire claims can obtain immediate cash in exchange for legal claims that may take years to resolve and ultimately yield no return. In effect, the claim holder receives the settlement value of the claim right away . . .").

<sup>43</sup> See *infra* note 88 (discussing New York's bankruptcy exception to its champerty statute).

When a plaintiff applies for financing, the claim procurement department interviews the client, investigates the facts, and researches the law to determine the merit, the risks, and the potential recovery of the plaintiff's claim. If the plaintiff is already represented by a lawyer, Champerco will interview the lawyer as well as the client and will require the plaintiff to waive the lawyer's duty of confidentiality.<sup>44</sup> Based on Champerco's evaluation of a plaintiff's claim, Champerco will offer the option of either assignment, partial sale, or loan to the plaintiff.

### 1. Assignment

Under this option, the plaintiff assigns his entire title and interest in his lawsuit to Champerco. Champerco pays the plaintiff with either cash or shares in the litigation proceeds, or some combination of the two. If the plaintiff's testimony or other cooperation is necessary, Champerco will generally insist that the plaintiff retain a sufficient interest in the proceeds in order to preserve an incentive for his cooperation. In any event, Champerco will generally require the plaintiff's consent to continue or bring the lawsuit in the plaintiff's name. This requirement serves two purposes. First, it preserves the secrecy of Champerco's identity as the real party in interest, which is necessary to prevent any prejudice to Champerco from the jury.<sup>45</sup> Second, bringing the suit in the plaintiff-assignor's name prevents the defendant from challenging Champerco's standing as a real party in interest.<sup>46</sup>

If the plaintiff is not yet represented by a lawyer, Champerco's litigation department will represent Champerco in the prosecution of the purchased claim. If the plaintiff has already retained a lawyer, Champerco will continue to retain that lawyer, with Champerco substituted as the client, unless the lawyer agrees to be bought out. This policy is necessary in order not to discourage lawyers from referring their clients to Champerco. If the plaintiff's

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<sup>44</sup> See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.6(a) (1994) ("A lawyer shall not reveal information relating to the representation of a client unless the client consents after consultation . . .").

<sup>45</sup> The sympathy factor of the plaintiff's claim will be diminished significantly if the jury is aware that any reward will go, not to the plaintiff, but to a corporation that purchased the claim at a price equal to a fraction of what the jury is prepared to award to the plaintiff.

<sup>46</sup> See FED. R. CIV. P. 17(a) ("Every action shall be prosecuted in the name of the real party in interest."). Champerco is only a real party in interest if it has established that it has a valid agreement with the plaintiff. See *infra* part III.C.

lawyer decides to remain on the case, Champerco's litigation department will provide support as is necessary. In all events, Champerco will acquire title to the claim, it will be the client, and it will exercise complete authority and control over the litigation, even if the plaintiff retains a significant share in the proceeds and the original lawyer remains. Because title to the claim will transfer to Champerco, there will be no lawyer-client relationship with the plaintiff and, thus, there will be no resulting attorney duties owed to the plaintiff-assignor.<sup>47</sup>

## 2. Partial Sale

Under this option, the plaintiff sells to Champerco shares in the litigation proceeds. Champerco pays the plaintiff either with cash or with an agreement to bear all the litigation expenses, or both. If the plaintiff is not yet represented, instead of paying the plaintiff's attorneys' fees, Champerco's litigation department may represent the plaintiff, much like an ordinary contingent fee arrangement. In any event, the plaintiff will remain the client and have total control over the litigation. This option is more palatable to plaintiffs that are simply seeking to finance their lawsuits, rather than "cash them out."

## 3. Loan

Under this final option, Champerco lends the plaintiff money, secured by the plaintiff's claim. The loan is a nonrecourse loan, meaning that repayment of the debt is either satisfied out of the proceeds of the lawsuit or not at all. Naturally, the loan is at a very high rate of interest because of the riskiness of the collateral. Champerco also offers to guarantee other lenders' loans to plaintiffs, which are secured by their lawsuits, for a substantial upfront guarantee fee.<sup>48</sup> Champerco generally only offers the loan option to plaintiffs with low-risk claims.

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<sup>47</sup> This transfer of identity may place the plaintiff's lawyer in an awkward position during Champerco's negotiations with the plaintiff, as she represents, at some point, each party to the negotiation and might even have an interest of her own. See MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.8(b) (1994) ("A lawyer shall not use information relating to representation of a client to the disadvantage of the client unless the client consents after consultation . . .").

<sup>48</sup> A guarantee fee is simply the fee charged for guaranteeing the loan. It is usually a percentage of the loan.

### B. *Litigation*

The litigation department serves several functions. First, it helps the claim procurement department evaluate claims. Second, it participates in all aspects of litigation. Under the assignment option, the litigation department manages the litigation, making all of the decisions that a client would normally make, and either litigates the claim itself or provides support and assistance for another lawyer to litigate the claim for Champerco. Under the partial sale option, the litigation department either represents plaintiffs, provides support to their lawyers, or helps plaintiffs find lawyers. Under the loan option, the litigation department only determines the appropriate interest rate to charge the plaintiff-borrower by evaluating the riskiness of the claim. At the plaintiff's request, however, Champerco may, in its discretion, offer, at no charge, the help of the litigation department's resources and expertise.<sup>49</sup>

### C. *Investor Services*

Champerco also offers investors several avenues for investing in litigation. Investors seeking the greatest possible returns can invest directly in specific lawsuits. These direct investments offer the greatest returns because these investments are undiluted, but also involve the highest risks because they are undiversified.<sup>50</sup> Direct investors may either buy shares in the lawsuits that Champerco already owns, or Champerco may act as a broker, matching up investors with plaintiffs and charging a brokerage fee.<sup>51</sup>

Most investors, however, will seek some degree of diversification. One way for investors to diversify is to become shareholders in Champerco, the corporation. However, there may not be a liquid market for Champerco's shares, and shareholders may want greater control over the distribution of Champerco's profits.

Champerco offers investors another diversified way to invest in litigation. Rather than buying individual litigation securities, investors can pool their monies by buying units of Champerco's mutual fund, Champerfund. The monies in Champerfund are used to buy shares in various lawsuits, thereby assembling a diversified

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<sup>49</sup> See MODEL RULES OF PROFESSIONAL CONDUCT Rule 5.4(a) (1994) ("A lawyer or law firm shall not share legal fees with a nonlawyer . . .").

<sup>50</sup> See *supra* notes 31-32 and accompanying text.

<sup>51</sup> See Simon, *supra* note 21, at 10-11.

portfolio of litigation securities.<sup>52</sup> Investors have the option of reinvesting their Champerfund dividends, receiving their dividends, or redeeming their units entirely on demand.

In addition to being financed by equity from shareholders and investors, Champerco is debt-financed. Investors can make loans to Champerco, secured by Champerco's portfolio of lawsuits. Investors receive premium interest rates because of the high-risk nature of these loans. If necessary, Champerco can also engage investors to guarantee the loans for a substantial guarantee fee. Alternatively, Champerco can guarantee an investor's direct loan to a plaintiff.

### III. CHAMPERTY

#### A. *History and Policy*

Champerty is defined as a "bargain between a stranger and a party to a lawsuit by which the stranger pursues the party's claim in consideration of receiving part of any judgment proceeds."<sup>53</sup> Champerty is one type of "maintenance," a term that "refers to maintaining, supporting, or promoting another person's litigation."<sup>54</sup> The doctrines of champerty and maintenance are ancient, reaching as far back as the ancient Greek and Roman law and the doctrines of *sykophanteia* and *calumnia*.<sup>55</sup>

Common law champerty doctrine developed as part of the resistance to the rise of capitalism that occurred around the Renaissance period.<sup>56</sup> Persons with capital would agree to bear the expenses and share the results of a lawsuit for the recovery of land.<sup>57</sup> This type of "transaction in medieval eyes was tainted with that speculation which was the essence of the abhorred sin of usu-

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<sup>52</sup> See *id.* at 11 ("Still other companies might assemble portfolios of litigation and sell equity interests in their portfolios to the public."). See generally Donald L. Abraham, Note, *Investor-Financed Lawsuits: A Proposal to Remove Two Barriers to an Alternative Form of Litigation Financing*, 43 SYRACUSE L. REV. 1297 (1992) (arguing that litigation securities should not be subject to securities regulation).

<sup>53</sup> BLACK'S LAW DICTIONARY 231 (6th ed. 1990) (citing *Alexander v. Unification Church*, 634 F.2d 673, 677 (2d Cir. 1980)).

<sup>54</sup> *Id.*

<sup>55</sup> See Max Radin, *Maintenance By Champerty*, 24 CAL. L. REV. 48, 49, 52-54 (1935). *Sykophanteia* and *calumnia* are doctrines against sycophants and calumniators, people who institute baseless litigation for their own gain. See *id.* at 49, 53.

<sup>56</sup> See *id.* at 65.

<sup>57</sup> See *id.* at 60.

ry."<sup>58</sup> In fact, the word "champerty" derives from *champart*, a type of feudal tenure in land that lent itself most easily to the evasion of laws against usury.<sup>59</sup>

Common law maintenance doctrine developed during feudal times in England in response to the practice of feudal magnates to maintain all of their retainers' lawsuits, whether justified or not, in order to aggrandize their estates.<sup>60</sup> These and other abuses of the judicial process abounded in the middle ages.<sup>61</sup> One particularly pernicious practice was the selling or assigning of a pretended right in land to persons of great power or influence, who would use their rank to further the prosecution of their lawsuits and oppress the possessors of the lands.<sup>62</sup> This problem was exacerbated where trial by combat prevailed and litigants assigned their claims to champion fighters.<sup>63</sup> Similar concerns led the *Talmud*, hundreds of years earlier, to frown upon the purchase of disputed titles in land.<sup>64</sup>

Another force that drove the development of ancient champerty and maintenance doctrine was the desire to discourage litigation, even if such litigation was meritorious.<sup>65</sup> The rise of Christianity infused into the law the Christian attitude that litigation was itself something to be discouraged, even if the claim was well-founded.<sup>66</sup> Forgiving debts was considered to be a fundamental Christian virtue, and recourse to secular law courts was discountenanced.<sup>67</sup> Trafficking in litigation was therefore naturally discouraged.

<sup>58</sup> *Id.* at 60-61.

<sup>59</sup> *See id.* at 61-63, 65-66.

<sup>60</sup> *See id.* at 64.

<sup>61</sup> *See Brown v. Bigne*, 28 P. 11, 12 (Or. 1891) ("So great was the evil of rich and powerful barons buying up claims, and, by means of their exalted and influential positions, overawing the courts, and thus securing unjust and unmerited judgments, . . . that it became necessary . . . to invoke in all its rigor the doctrine against champerty and maintenance.").

<sup>62</sup> *See id.* ("The doctrine [of champerty and maintenance] was established 'to repress the practices of many who, when they thought they had title or right to any land, for the furtherance of their pretended right conveyed their interest, or some part thereof, to great persons, and with their countenance did oppress the possessors.'" (citation omitted)).

<sup>63</sup> *See Radin*, *supra* note 55, at 58-59.

<sup>64</sup> *See BABYLONIAN TALMUD*, tractate Shevovoth 31a (stating that one who buys disputed titles in land, relying on his superior strength to take possession, is evil in the eyes of the law).

<sup>65</sup> *See Radin*, *supra* note 55, at 56.

<sup>66</sup> *See id.*

<sup>67</sup> *See id.*



There is also a hint of paternalism in some of the earliest examples of the rule against champerty. For example, under Roman law, the purchase of choses in action was allowed, unless *pendente lite*, until a famous constitution of the Emperor Anastasius forbade it in 506 A.D. on the grounds that the purchasers were “devour[ing] the property or fortunes of others” by inducing the plaintiffs to part with their claims for sums far below their actual value.<sup>68</sup> For similar reasons, the early common law prohibited a popular form of champerty in which the wealthier of two joint claimants bought out the other claimant.<sup>69</sup>

Over the last several centuries, the laws against champerty and maintenance have eroded considerably, leading many courts, as early as the nineteenth century, to pronounce the doctrine ancient and obsolete.<sup>70</sup> Nevertheless, common law champerty, at least in some form, continues to be either illegal, against public policy, or even criminal in most states.<sup>71</sup>

The contemporary justification for laws against champerty and maintenance is far from obvious.<sup>72</sup> Most of the policies that drove the development of common law champerty are now obsolete.<sup>73</sup> Feudalism died, as did the resistance to capitalism. The administration of justice is no longer so weak and corrupt that the judicial process can be used as an “engine of oppression.”<sup>74</sup> The view that even meritorious claims should be discouraged and, instead, forgiven, no longer prevails.<sup>75</sup>

<sup>68</sup> *Id.* at 55 (citation omitted).

<sup>69</sup> *See id.* at 60.

<sup>70</sup> *See, e.g.,* *Brown v. Bigne*, 28 P. 11, 13 (Or. 1891) (noting that champerty laws are narrowly applied “[t]o meet the changed condition of society”); *see also* 14 AM. JUR. 2D *Champerty & Maintenance* § 1 (1964) (“In many states [the doctrines of champerty and maintenance] are declared to be obsolete . . .”); 14 C.J.S. *Champerty & Maintenance* § 3 (1991) (noting that the “concept of champerty has been narrowed, tempered, and mellowed in modern times”).

<sup>71</sup> *See infra* part III.B (discussing the various modern approaches to champerty law).

<sup>72</sup> *See Radin, supra* note 55, at 71 (“If we dealt with this as a matter of abstract logic, it would be hard to justify the objection to champerty either in the case of lay champertors or lawyers.”).

<sup>73</sup> *See Bigne*, 28 P. at 12 (stating that the doctrine of “champerty and maintenance . . . arose from causes peculiar to the state of society in which it was established”); *Radin, supra* note 55, at 66 (“[T]he background against which the law of champerty and maintenance grew up . . . has disappeared.”).

<sup>74</sup> *Bigne*, 28 P. at 12 (citing 4 WILLIAM BLACKSTONE, COMMENTARIES \*135).

<sup>75</sup> *See Radin, supra* note 55, at 66 (“The condemnation of litigiousness . . . remains . . . a common element in the medieval and modern attitudes, but neither then nor now did it play a controlling role.”); *Simon, supra* note 21, at 11 (stating that “lawsuits

Almost a century ago, in *Peck v. Heurich*,<sup>76</sup> the Supreme Court stated that champertous agreements, at least between a plaintiff and an attorney, are "contrary to public policy, unlawful, and void, as tending to stir up baseless litigation."<sup>77</sup> Ironically, the one type of champertous agreement that has gained widespread acceptance is the contingent fee agreement between an attorney and a client.<sup>78</sup> Nevertheless, the most popular modern objection to champertous agreements between laymen and plaintiffs is that they tend to stir up frivolous litigation.<sup>79</sup>

Other policy justifications for the law against champerty have been offered as well.<sup>80</sup> The law might seek to encourage settlement,<sup>81</sup> to prevent unauthorized practice of law by corporations,<sup>82</sup> to prevent strife, discord, and harassment,<sup>83</sup> or to prevent trafficking and speculating in litigation.<sup>84</sup>

are considered one of the marks of a civilized society").

<sup>76</sup> 167 U.S. 624 (1897).

<sup>77</sup> *Id.* at 630.

<sup>78</sup> Contingent fee agreements, although technically champertous, are generally legal in the United States if they are reasonable. See 14 C.J.S. *Champerty & Maintenance* § 11 (1991).

<sup>79</sup> See 14 C.J.S. *Champerty & Maintenance* § 2 (1991) ("The laws against champerty . . . are aimed at the prevention of multitudinous and useless lawsuits . . ."); *infra* part IV.D.2 (discussing this objection as a basis for champerty laws).

<sup>80</sup> For a realist view of the modern justification for champerty laws, see Radin, *supra* note 55, at 66 (blaming the elitist members of the bar and their protectionist interests for the law against champerty).

<sup>81</sup> See Simon, *supra* note 21, at 11 (stating that champerty "may impede settlements, since well-heeled investors may be more willing than individuals to gamble at trial").

<sup>82</sup> See *Knobel v. Estate of Eugene A. Hoffman Inc.*, 432 N.Y.S.2d 66, 67 (App. Div. 1980) (noting that the purpose of Judiciary Law § 489 is to prevent champertous agreements and the unauthorized practice of law by corporations).

<sup>83</sup> See *Fairchild Hiller Corp. v. McDonnell Douglas Corp.*, 270 N.E.2d 691, 693 (N.Y. 1971) (noting that the "legislative concern [behind Judiciary Law § 489] is . . . [the] prevent[ion of] . . . strife, discord and harassment which could result from permitting attorneys and corporations to purchase claims for the purpose of bringing actions thereon").

<sup>84</sup> See, e.g., *Pritzker v. Yari*, 42 F.3d 53, 66 (1st Cir. 1994) (declaring that the "single serious purpose" of the Puerto Rico champerty statute is "to discourage financial speculation in litigation" (quoting *Pritzker v. Yari*, No. CIV.92-2825, 1993 WL 71760, at \*5 (D.P.R. Mar. 5, 1993))); *Koro Co. v. Bristol-Myers Co.*, 568 F. Supp. 280, 288 (D.D.C. 1983) (finding that New York's champerty statute was "designed to prevent trafficking and speculation in lawsuits"); see also 14 C.J.S. *Champerty & Maintenance* § 2 (1991) ("The laws against champerty . . . are aimed at . . . the prevention of speculation in litigation.").

### B. *Modern Champerty Law*

Although states take different approaches to champerty, champerty runs contrary to public policy in almost every state. In some states, champerty is prohibited by statute, in others by common law, and in others by rule of public policy. This Part explores a sampling of several states' champerty laws, grouped by their different approaches.

#### 1. Statute: New York<sup>85</sup>

The New York legislature has expressed its strong public policy against champerty in section 489 of the Judiciary Law.<sup>86</sup> The statute makes no reference to "champerty," but it clearly spells out a broad prohibition against it:

No person or co-partnership . . . and no corporation or association . . . shall solicit, buy or take an assignment of, or be in any manner interested in buying or taking an assignment of a bond, promissory note, bill of exchange, book debt, or other thing in action, or any claim or demand, with the intent and for the purpose of bringing an action or proceeding thereon. . . . [A]ny person . . . violating the provisions of this section . . . is guilty of a misdemeanor.<sup>87</sup>

The intent of the New York Legislature to thwart investment in litigation is clear from the sheer breadth of the statute's prohibition,<sup>88</sup> and its policy against speculating in litigation is clear from

<sup>85</sup> Mississippi has also adopted a statutory approach to regulating champerty. *See* MISS. CODE ANN. § 97-9-11 (1994).

<sup>86</sup> *See* N.Y. JUD. LAW § 489 (McKinney 1983).

<sup>87</sup> *Id.*

<sup>88</sup> The statute, however, carves out one very significant exception to its prohibition of investing in litigation:

[B]ills receivable, notes receivable, bills of exchange, judgments or other things in action may be solicited, bought, or assignment thereof taken, from any executor, administrator, assignee for the benefit of creditors, trustee or receiver in bankruptcy, or any other person or persons in charge of the administration, settlement or compromise of any estate, through court actions, proceedings or otherwise.

*Id.* This exception freely allows the purchase of claims from trustees and the like who are in charge of winding up an estate. The purpose of the exception is to facilitate expeditious liquidation and final settlement of certain estates. *See* *People v. Berlin*, 317 N.Y.S.2d 191, 194 (Nassau County Ct. 1971). Although this exception is narrow, it provides a significant market for investing in litigation because such plaintiffs are likely to be very eager to cash out and liquidate their claims, which is precisely the purpose of the exception. *See, e.g., In re Resorts Int'l, Inc.*, 145 B.R. 412, 474 (D.N.J.

the statute's focus on intent.

Because investing in litigation is illegal, champertous agreements are void.<sup>89</sup> A lawsuit brought by a champertous assignee will be dismissed.<sup>90</sup> Even when an agreement does not actually violate the New York champerty statute because another state's laws apply, New York will refuse to entertain a lawsuit based on the agreement if the agreement is illegal under New York law.<sup>91</sup> Nevertheless, New York will not go so far as to dismiss a lawsuit brought by a bona fide plaintiff who happened to enter into an illegal champertous agreement with a third party.<sup>92</sup>

1990) (upholding, under the bankruptcy exception of § 489, the validity of a Litigation Trust to which a bankrupt debtor assigned its claims and then distributed shares in the trust to its creditors); *Investment Opportunities*, NAT'L L.J., Dec. 4, 1995, at B19 (advertising the sale, by a bankruptcy estate, of a 51% interest in a \$28.8 million judgment on writ of appeal). Interestingly, the statute's exception is a candid admission by the New York Legislature that speculating in litigation is not necessarily undesirable or harmful.

<sup>89</sup> See *Lee v. Community Capital Corp.*, 324 N.Y.S.2d 583, 585 (Sup. Ct. 1971) ("[A] party to an illegal . . . act or transaction cannot base a cause of action on such act or transaction."). Generally, champertous agreements will violate the letter of the statute. But where an agreement does not violate the letter of the statute, it will be valid and enforceable even though it is against New York's public policy against champerty. See *Lost Lots Assocs. v. Bruyn*, 415 N.Y.S.2d 99, 100 (App. Div. 1979) (holding that champerty is only viable as a defense as provided by statute).

<sup>90</sup> See *Refac Int'l, Ltd. v. Lotus Dev. Corp.*, 131 F.R.D. 56, 58 (S.D.N.Y. 1990) (holding that the champertous assignee could not maintain a patent-infringement claim because it was "not the real party in interest," but was only a "surrogate plaintiff").

<sup>91</sup> See *American Optical Co. v. Curtiss*, 56 F.R.D. 26, 30 (S.D.N.Y. 1971) (stating that a plaintiff "should not be permitted to sue in [New York] on a[n] . . . action . . . which would not be enforced by New York Courts"). For a further discussion of this case, see *infra* notes 250-59 and accompanying text.

<sup>92</sup> Compare *Knobel v. Estate of Eugene A. Hoffman Inc.*, 432 N.Y.S.2d 66 (Sup. Ct. 1980) with *American Optical Co. v. Curtiss*, 59 F.R.D. 644 (S.D.N.Y. 1973) and *American Optical Co. v. Curtiss*, 56 F.R.D. 26 (S.D.N.Y. 1971). *Knobel* held that the statute prohibits taking assignment of a claim with the intent to sue whether the claim is structured to appear to belong to the assignee or to the assignor. See *Knobel*, 432 N.Y.S.2d at 68. *American Optical* indirectly held that the court could refuse to entertain a lawsuit brought by a champertous assignee, although it could not refuse to entertain the same lawsuit brought in the assignor's name, regardless of the existence of a champertous assignment. See *American Optical*, 56 F.R.D. at 32 (dismissing the complaint unless the University, the real plaintiff, was joined or substituted as party plaintiff within 10 days).

Neither *Knobel* nor *American Optical*, however, is directly on point. *Knobel* dealt only with the reach of the statute's prohibition, not with its viability as a defense. *American Optical* did not directly deal with a violation of the champerty statute; the court simply refused to entertain the lawsuit because it was contrary to New York's policy embodied in the statute. The court, nevertheless, allowed the champertous assignee to bring the claim if it joined the assignor as a plaintiff. In any event, there

## 2. Legal Champerty: New Jersey

New Jersey has neither adopted the English champerty statutes and common law nor otherwise maintained the public policy against champerty.<sup>93</sup> In one of the earliest lawsuit syndication cases,<sup>94</sup> the New Jersey Court of Chancery held that speculation in lawsuits violates neither the law nor the public policy of New Jersey.<sup>95</sup> Agreements to buy lawsuits or shares of the proceeds thereof are, therefore, valid and enforceable like any other contract. In fact, a New Jersey statute explicitly makes all lawsuits arising out of contracts assignable.<sup>96</sup>

## 3. Common Law: Pennsylvania

Pennsylvania is one of several jurisdictions that maintains the vintage common law doctrine against champerty.<sup>97</sup> In the leading

is almost no precedent holding that an action by a bona fide plaintiff can be dismissed by virtue of a bona fide plaintiff's champertous agreement with a third party. See L.S. Tellier, Annotation, *Assertion of Defense of Champerty in Action By Champertous Assignee*, 22 A.L.R.2d 1000, § 3, at 1011 (1952).

<sup>93</sup> See *J ex rel. A v. D*, 482 A.2d 531, 534 (N.J. Super. Ct. Law Div. 1984) ("The doctrine[] of . . . champerty do[es] not prevail in New Jersey . . ."); *Sweeney v. Veneziano*, 175 A.2d 241, 245 (N.J. Sup. Ct. 1961) (holding that a suit for legal services by a partnership composed of defendant and another was permissive considering New Jersey's policy favoring champerty); *Bouvier v. Baltimore & N.Y. Ry.*, 51 A. 781, 784 (N.J. 1902) (departing from English common law in holding that champerty and maintenance doctrines are inapplicable). *But see Stanford v. Werder*, 20 N.J. L.J. 56, 59 (Dist. Ct. 1897) (finding one particular champertous agreement contrary to public policy).

<sup>94</sup> See *Bigelow v. Old Dominion Copper Mining & Smelting Co.*, 71 A. 153 (N.J. Ch. 1908).

<sup>95</sup> The court unequivocally enunciated New Jersey's permissive attitude toward trading in litigation:

Neither the law nor the policy of New Jersey prohibits what complainant is pleased to call a speculation in a lawsuit. In this state we have not adopted the English statutes of champerty and maintenance. . . . And with us the assignment of choses in action has from an early day been encouraged.

*Id.* at 167.

<sup>96</sup> See N.J. STAT. ANN. § 2A:25-1 (West 1985) ("[A]ll choses in action arising on contract shall be assignable . . .").

<sup>97</sup> See, e.g., *Kenrich Corp. v. Miller*, 377 F.2d 312, 314 (3d Cir. 1967) ("Under the common law of Pennsylvania, an arrangement offends public policy against champerty and is illegal if it provides for the institution of litigation by and at the expense of a person who, but for that agreement, has no interest in it, with the understanding that his reward is to be a share of whatever proceeds the litigation may yield."); *Keiper v. Miller*, 68 F. 627, 630 (E.D. Pa. 1895) (dismissing a patent-infringement suit and holding that an agreement between the patentee and an attorney, which assigned the patent to the attorney so that the attorney could prosecute infringement suits in his

case on champerty,<sup>98</sup> a corporation assigned its rights in a derivative suit against its former directors in exchange for a share of the proceeds.<sup>99</sup> The assignee, Jerome Kline, was the former president, director, and principal shareholder of the company.<sup>100</sup> The assignment agreement called for Kline to present to the company the factual basis for the derivative suit.<sup>101</sup> The company would then have a choice either to sue in its own name, with Kline receiving 25% of the proceeds, or to assign the claim to Kline, who would then sue in his own name and retain 66% of the proceeds.<sup>102</sup> The company elected not to sue in its own name and assigned its rights in the suit to Kline, who brought suit in his own

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name and share the recoveries with the patentee, was champertous and, therefore, void); *Ames v. Hillside Coal & Iron Co.*, 171 A. 610, 610 (Pa. 1934) ("While there has been some relaxation in the application of the common-law doctrines of champerty and maintenance in this . . . jurisdiction[,], champerty, repugnant to public policy, is still ground for denying the aid of the court.").

For cases in other jurisdictions that retain the common law rule against champerty, see *Parks v. American Warrior, Inc.*, 44 F.3d 889, 893 (10th Cir. 1995) (recognizing that the doctrine of champerty exists in Oklahoma, although it cannot be used as a defense against a bona fide plaintiff); *Design for Business Interiors v. Herson's, Inc.*, 659 F. Supp. 1103, 1108 (D.D.C. 1987) ("If a contract is determined to be champertous, District of Columbia courts will not enforce it." (quoting *Marshall v. Bickel*, 445 A.2d 606, 609 (D.C. 1982))); *Hall v. State*, 655 A.2d 827, 830 (Del. Super. Ct. 1994) (stating that "the doctrine [of champerty and maintenance] continues to have vitality in this State"); *Boettcher v. Criscione*, 299 P.2d 806, 811 (Kan. 1956) (stating that "[w]hether champerty . . . is in violation of public policy . . . turns largely on the facts and circumstances of each case"); *McCullar v. Credit Bureau Sys.*, 832 S.W.2d 886, 887 (Ky. 1992) (holding that the "champerty doctrine remains viable [but] only as a defense in a contract action"); *Curry v. Dahlberg*, 110 S.W.2d 742, 748 (Mo. 1937) ("The law of champerty and maintenance is in force in this state."); *McKellips v. Macintosh*, 475 N.W.2d 926, 929 (S.D. 1991) ("[T]he doctrines of champerty and maintenance currently apply in South Dakota.").

Other jurisdictions retain the common law against champerty but limit its application to champertous agreements that are against public policy. See, e.g., *American Hotel Management Assoc. v. Jones*, 768 F.2d 562, 571 (4th Cir. 1985) ("Champerty and maintenance will not be found 'unless the interference is clearly officious and for the purpose of stirring up strife and continuing litigation.'" (quoting *Smith v. Hartsell*, 63 S.E. 172, 174 (N.C. 1908)) (citations omitted)); *Lott v. Kees*, 165 So. 2d 106, 110 (Ala. 1964) ("[W]hen such contracts are made for the purpose of stirring up strife and litigation, harassing others, inducing suits to be begun which otherwise would not be commenced, or for speculation they come within the analogy and principles of [the] doctrine [of champerty], and should not be enforced." (quoting *Brown v. Bigne*, 28 P. 11, 13 (Or. 1891))).

<sup>98</sup> See *Kenrich Corp. v. Miller*, 377 F.2d 312 (3d Cir. 1967).

<sup>99</sup> See *id.* at 313-14.

<sup>100</sup> See *id.* at 313.

<sup>101</sup> See *id.* at 313-14.

<sup>102</sup> See *id.* at 314.

name.<sup>103</sup> The district court held that the assignment agreement was champertous and illegal under Pennsylvania law and dismissed the suit with prejudice as to Kline but without prejudice as to the company.<sup>104</sup> The Third Circuit affirmed.<sup>105</sup>

This case shapes many of the contours of Pennsylvania's champerty doctrine. By dismissing the suit with prejudice only as to Kline, the champertous assignee, the Third Circuit held that a defendant has standing to raise the defense of champerty against an assignee suing in its own name, but that an assignor does not forfeit its rights in the action by virtue of its champertous agreement. Thus, a defendant has no standing to assert the plaintiff's champertous contract with a third party as a defense against the plaintiff-assignor.<sup>106</sup> However, because the agreement would nonetheless be illegal and invalid, the assignee also could not enforce the agreement against the plaintiff-assignor.

#### 4. Public Policy: California

California has never adopted the common law doctrine of champerty.<sup>107</sup> Nevertheless, champertous agreements may be void as contrary to California public policy,<sup>108</sup> although there is a dearth of California precedent finding champertous agreements void as against public policy.

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<sup>103</sup> See *id.* at 313-14.

<sup>104</sup> See *id.* at 314.

<sup>105</sup> See *id.*

<sup>106</sup> In *Augenti v. Cappellini*, 499 F. Supp. 50 (M.D. Pa. 1980), the court held that a "[d]efendant cannot avail himself of the champertous agreement as a defense to the action." *Id.* at 51 (citing *Burnes v. Scott*, 117 U.S. 582, 589 (1886); *Bedell v. Oliver H. Bair Co.*, 158 A. 651, 653 (Pa. Super. Ct. 1932)).

<sup>107</sup> See *In re Cohen's Estate*, 152 P.2d 485, 489 (Cal. Ct. App. 1944) ("California is one of the many states that has never adopted the common law doctrines of champerty and maintenance."); *Mathewson v. Fitch*, 22 Cal. 86, 95 (1863) ("[T]he offense of maintenance is unknown to the laws of this State.").

A California statute does prohibit attorneys from buying claims with the intent to sue thereon, but the statute applies only to attorneys. See CAL. BUS. & PROF. CODE § 6129 (West 1990). The statute applies only to members of the California Bar, as the law is based on the Supreme Court of California's power to control its officers. See *id.* § 6087.

<sup>108</sup> Connecticut takes a similar approach to California. Connecticut has not adopted the common law rule against champerty, but rather applies a public policy test to determine whether such agreements are valid. See *Rice v. Farrell*, 28 A.2d 7, 8 (Conn. 1942) ("[T]he common law doctrines of champerty and maintenance as applied to civil actions have never been adopted in this state, and the only test is whether a particular transaction is against public policy.").

In a case that sheds some light on California's champerty law, *Killian v. Millard*,<sup>109</sup> William Millard, the president of Computerland, issued a note to a venture capital firm to finance the start-up of the company.<sup>110</sup> The note was convertible after a specified time into a 20% equity share in Computerland.<sup>111</sup> The plaintiffs purchased the note from the venture capital company and, after Millard refused to honor the note, sued to enforce it.<sup>112</sup> Unable to finance the litigation out of personal funds, the plaintiffs turned to outside investors.<sup>113</sup> They offered fifty shares in the proceeds of the litigation at \$10,000 a share.<sup>114</sup> The trial court, however, granted the defendant's motion to compel the plaintiffs to sever all ties with the investors and return their money.<sup>115</sup> The court held that the investment scheme violated public policy and was, therefore, void.<sup>116</sup> On appeal, the California Court of Appeal reversed, holding that the defendant lacked standing to challenge the validity of contracts between the plaintiff and its investors, contracts to which the defendant was not a party.<sup>117</sup> The California Court of Appeal did not, however, overturn the lower court's holding that the lawsuit-syndication scheme violated California public policy, a holding that may still be the law in California.

##### 5. Civil Law: Puerto Rico and Louisiana

The civil law deals with champerty in a unique fashion.<sup>118</sup> Under civil law, if a plaintiff sells all or part of his claim, the defendant may extinguish the claim by redeeming it from the purchaser for the price he paid plus interest and costs.<sup>119</sup>

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<sup>109</sup> 228 Cal. App. 3d 1601 (Ct. App. 1991); *see also* Spencer, *supra* note 4, at 72 (discussing "the most successful investor-financed lawsuit in U.S. history").

<sup>110</sup> *See* Cox, *supra* note 13, at 157.

<sup>111</sup> *See id.*

<sup>112</sup> *See id.*

<sup>113</sup> *See id.*

<sup>114</sup> *See Killian*, 228 Cal. App. 3d at 1604.

<sup>115</sup> *See id.* at 1606.

<sup>116</sup> *See id.*

<sup>117</sup> *See id.* at 1607. After the California Supreme Court upheld the jury's verdict, the investors stood to receive an incredible 1600% return on their investments. *See* Spencer, *supra* note 4, at 72.

<sup>118</sup> *See generally* Mervin H. Riseman, *The Sale of a Litigious Right*, 13 TUL. L. REV. 448 (1939) (discussing Louisiana law on the purchase of litigious rights). Riseman, in consonance with almost every other commentator on the subject of champerty, states that "[i]n spite of the policy restraining the purchase of litigious rights by public officers, there seems to be nothing actually odious in the purchase of such rights by other parties." *Id.* at 451.

<sup>119</sup> *See* LA. CIV. CODE ANN. art. 2652 (West 1991); P.R. LAWS ANN. tit. 31, § 3950



In the recent Puerto Rico case of *Pritzker v. Yari*,<sup>120</sup> the plaintiff, in a breach of contract action, packaged and sold various rights in the proceeds of his claim in order to finance his fiercely contested lawsuit.<sup>121</sup> When the defendant learned of the agreements through discovery, he immediately tendered payment to the three investors to redeem their interests in the lawsuit pursuant to Article 1425, the Puerto Rico champerty statute.<sup>122</sup> Article 1425 gives a debtor the right to redeem and extinguish a "litigated credit" that is sold.<sup>123</sup> After the investors refused to acknowledge the existence of the defendant's right of redemption, the defendant brought a collateral suit to enforce his redemption right.<sup>124</sup> The district court rendered judgment in favor of the defendant (that is, the party exercising the right of redemption), and the Court of Appeals for the First Circuit affirmed, holding that the case fell squarely within the language of the statute.<sup>125</sup>

In one sense, the civil law approach to champerty favors defendants because it grants them an independent, enforceable right of redemption, whereas under the common law of champerty, the defendant often lacks standing to challenge a champertous agreement.<sup>126</sup> Yet, under the common law, a champertous agreement may be held invalid, and the investor may lose all of his money,<sup>127</sup> whereas under the civil law, the investor will at least get his money back, plus interest and costs.

Despite its clear purpose to frustrate "litigious profiteering,"<sup>128</sup> the civil law approach to champerty poses only minor

(1991) (also referred to as "Article 1425").

<sup>120</sup> 42 F.3d 53 (1st Cir. 1994).

<sup>121</sup> See *id.* at 58.

<sup>122</sup> See P.R. LAWS ANN. tit. 31, § 3950 (1991). Article 1425 states:

When a litigated credit is sold, the debtor shall have the right to extinguish the same by reimbursing the assignee for the price the later [sic] paid for it, the judicial costs incurred by him, and the interest on the price from the day on which the same was paid. . . . The debtor may make use of his right within nine (9) days, counted from the day the assignee should demand payment of him.

*Id.*

<sup>123</sup> See *id.*

<sup>124</sup> See *Pritzker*, 42 F.3d at 58-59.

<sup>125</sup> See *id.* at 68.

<sup>126</sup> See *infra* part III.C.

<sup>127</sup> The investor may be able to recover in restitution.

<sup>128</sup> See *Pritzker*, 42 F.3d at 68. According to the First Circuit, "the district court hit the bull's-eye when it declared that the 'single, serious purpose' of article 1425 is 'to discourage financial speculation in litigation.'" *Id.* at 65-66 (quoting *Pritzker v. Yari*,

obstacles to investing in litigation. The reason for this ineffectiveness is that the defendant must exercise his right of redemption promptly. Both Puerto Rico and Louisiana make it clear that the defendant cannot continue to contest the lawsuit, wait and see whether he succeeds, and then exercise his right of redemption if he loses.<sup>129</sup>

The limitation period for exercising a right of redemption puts litigation investors in a very secure position. In Puerto Rico, for example, the limitation period is nine days, beginning from the time the purchaser of the claim demands that the defendant exercise his right.<sup>130</sup> The defendant must irrevocably tender payment within that time or lose the right of redemption. Since the course of litigation, and thus the value of the plaintiff's claim, is unlikely to change much in the nine-day period, the defendant essentially has little more than a right of first refusal to buy the plaintiff's claim. From an investor's perspective, this is an acceptable restriction. When the investor purchases shares in a lawsuit, he can immediately notify the defendant and demand the exercise of the right within nine days.<sup>131</sup> If the defendant does not exercise his right promptly, then the investor's investment is secure, and the defendant has no recourse. If the defendant does exercise his right promptly, then the investor gets all of his money back plus interest and costs<sup>132</sup>—very nearly a no-lose situation.

Furthermore, the likelihood of the defendant exercising his right is theoretically low. If the plaintiff was willing to sell her claim to a third party for X dollars, she would have been willing to settle with the defendant for X dollars.<sup>133</sup> Since the defendant obviously was not willing to buy the claim from the plaintiff for X dollars, the

No. CIV.92-2825, 1993 WL 71760, at \*5 (D.P.R. Mar. 5, 1993)).

<sup>129</sup> See P.R. LAWS ANN. tit. 31, § 3950 (limiting the right of a debtor to extinguish litigated credit to nine days from the day the assignee demands payment of him); *A.M. & J. Solari, Ltd. v. Fitzgerald*, 150 So. 2d 896, 901 (La. Ct. App. 1963) (“[A] party seeking to redeem a litigious right must be prompt in making known his intention . . .”); *Riseman*, *supra* note 118, at 453 (“If, on learning of the transfer, [a party] continues to contest the suit, he may not, when he realizes that the judgment is about to become final or that he is going to lose the suit, avail himself of the provisions which the law has established in his favor for the purpose of litigation.”).

<sup>130</sup> See P.R. LAWS ANN. tit. 31, § 3950.

<sup>131</sup> See *id.*

<sup>132</sup> See *id.*

<sup>133</sup> There are, of course, psychological factors such as hostility, vindication, and revenge that may have prevented a settlement even though the amount was right. Also, strategic bargaining might have prevented the parties from settling regardless of the amount of the settlement. See *supra* part I.B.

defendant would presumably be unwilling to buy it from the third-party purchaser for X dollars. Logically, therefore, the defendant will not exercise its right of redemption promptly, and the right will terminate.<sup>134</sup>

### C. *The Practical Impact of Champerty Laws*

As this Part has revealed, champerty is generally illegal in most states. Nevertheless, where champerty and maintenance are not criminally prohibited, the only effect of champerty laws is to make champertous agreements unenforceable. In many states, however, the lack of an enforceable agreement poses a serious obstacle to buying lawsuits. Since a champertous agreement between a plaintiff and an investor is invalid, the assignment of the claim is invalid as well. The investor-assignee, therefore, has no standing as a real party in interest, and his claim will be dismissed.<sup>135</sup>

Some states do not allow defendants to raise champerty as a defense against a champertous assignee, on the ground that the defendant has no standing to challenge an agreement to which he is not a party.<sup>136</sup> Most states, however, allow the defense on the ground that the assignee's standing and entitlement to a judgment are predicated on the assignment.<sup>137</sup> The validity of the assignment, therefore, is a necessary element of the investor-assignee's case, which the defendant can challenge on the ground that the assignment is champertous and invalid.<sup>138</sup> If the court finds the assignment void for champerty, the assignee's claim will be dismissed for lack of standing as a real party in interest.

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<sup>134</sup> The situation, however, is different when the plaintiff sells only a portion of the claim. Since the plaintiff could not have sold (that is, settled) only a part of his claim to the defendant, there is less reason to believe that the defendant will not exercise its right of redemption.

<sup>135</sup> See FED. R. CIV. P. 17(a) ("Every action shall be prosecuted in the name of the real party in interest."); 6A CHARLES A. WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 1545, at 350 (1990) (stating that "the court must assure itself that a *valid* assignment has been made" (emphasis added)); see also *Refac Int'l, Ltd. v. Lotus Dev. Corp.*, 131 F.R.D. 56, 58 (S.D.N.Y. 1990) (holding that the champertous assignee could not maintain a latent-infringement claim because it was "not the real party in interest," but only a "surrogate plaintiff").

<sup>136</sup> See *Killian v. Millard*, 228 Cal. App. 3d 1601, 1605 (Ct. App. 1991) (noting that Millard lacked standing because he "had no substantive right in the contract between Syndicators and Investors"); *Tellier*, *supra* note 92, at 1006 ("[A]lthough an assignment may be champertous, such champerty is not available as a defense . . .").

<sup>137</sup> See *Tellier*, *supra* note 92, at 1003.

<sup>138</sup> See 14 AM. JUR. 2D *Champerty & Maintenance* § 15 (1964).

To avoid the risk of dismissal and to take away the defendant's champerty defense against an investor-assignee, the investor should either join the plaintiff-assignor as a party or bring the lawsuit in the plaintiff's name.<sup>139</sup> This, of course, is never a problem when the investor purchases less than the plaintiff's full interest in the lawsuit,<sup>140</sup> but even when the investor purchases the plaintiff's entire claim, the investor can bring the lawsuit in the plaintiff's name. Since, legally, the agreement is invalid, the claim was never validly assigned, and the plaintiff remains the real party in interest. Once the plaintiff-assignor is joined or named as the plaintiff, champerty is no longer available as a defense.<sup>141</sup>

Bringing suit in the plaintiff-assignor's name, however, poses another serious risk to investors. If the plaintiff-assignor is named as the plaintiff in the lawsuit, any judgment or settlement will be paid to him. There is a significant risk that the plaintiff will keep the money and repudiate his agreement with the investor.<sup>142</sup> After a substantial judgment or settlement, the value of the investor's shares may be three or four times greater than the price the plaintiff received for them, and, since the agreement is unenforceable, the plaintiff will have a strong incentive to renege. In practical terms, then, investing in litigation is not feasible unless champertous agreements are enforceable. No prudent investor can assume the risks of doing business without an enforceable agreement. Litigation investment companies, such as Champerco, must

<sup>139</sup> See, e.g., *McCullar v. Credit Bureau Sys.*, 832 S.W.2d 886, 887 (Ky. 1992) (affirming the lower court's denial of the debtor's motion to dismiss against the champertous assignee after the assignee joined the real creditors as plaintiffs following the lower courts dismissal, on champerty grounds, of the assignee's action brought in its own name); see also *American Optical v. Curtiss*, 59 F.R.D. 644 (S.D.N.Y. 1973), discussed *supra* note 92.

<sup>140</sup> See *WRIGHT & MILLER, supra* note 135, § 1545, at 351-53 ("[W]hen there has been only a partial assignment the assignor and the assignee each retain an interest in the claim and are both real parties in interest.")

<sup>141</sup> See 14 AM. JUR. 2D *Champerty & Maintenance* § 15 (1964); see also *Parks v. American Warrior, Inc.*, 44 F.3d 889, 893 (10th Cir. 1995) (finding that a champertous cost-sharing contract between the plaintiffs and a third party did not operate to decrease the liability of the defendants to the plaintiffs); *American Hotel Management Assoc. v. Jones*, 768 F.2d 562, 570-71 (4th Cir. 1985) (holding that "the champerty and maintenance doctrine remains viable only as a defense in contract actions"); *Killian v. Millard*, 228 Cal. App. 3d 1601, 1607 (Ct. App. 1991) (holding that the defendant, Millard, lacked standing to challenge the contract for sale of shares in the litigation proceeds). See generally *Tellier, supra* note 92 (discussing the use of champerty as a defense).

<sup>142</sup> See, e.g., *McKellips v. MacIntosh*, 475 N.W.2d 926, 929 (S.D. 1991) (finding the agreement champertous and therefore void as against public policy).

develop a means to enforce their agreements if their business is to be viable.

#### IV. CONFLICT OF LAWS

Part III revealed that champerty laws, as ancient and obsolete as they are, continue to invalidate agreements to divide the proceeds of litigation. Consequently, almost no state will enforce a champertous agreement. Furthermore, many states will deny standing to a champertous assignee. This latter consequence is less significant because a champertous assignee can always sue in the assignor's name and thereby avoid any champerty challenge to the assignee's standing. The unenforceability of champertous agreements, however, makes investing in litigation impracticable. Investors, such as Champerco, would not be wise to invest in litigation without the security of an enforceable agreement.

Despite the unenforceability of champertous agreements in almost every state, champerty laws may not be fatal to investing in litigation. The contractual nature of champerty laws<sup>143</sup> opens up the possibility of creating enforceable champertous agreements by "contracting around" champerty laws.<sup>144</sup> If Champerco can somehow choose the law that governs its agreements, then all that is needed is one state, here New Jersey, to open its doors just a crack to litigation investment. With the door open, litigation investment in all other states can get in through that crack. This Part explores the possibility of contracting around champerty laws by choosing New Jersey law to govern a champertous agreement.

There are three ways Champerco can "choose" New Jersey law to govern its agreements: (1) negotiate and execute its agreements in New Jersey; (2) provide in its agreements that New Jersey law governs the agreement (that is, a New Jersey choice-of-law clause); and (3) designate New Jersey as the sole and exclusive forum for any

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<sup>143</sup> See RESTATEMENT (FIRST) OF CONTRACTS § 540(2) (1932) (defining "champerty" as "the division of the proceeds of litigation between the owner of the litigated claim and a party supporting or enforcing the litigation"); SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1711, at 857 (Walter H.E. Jaeger ed., 3d ed. 1972) ("Champerty is a bargain to divide the proceeds of a litigation between the owner of the litigated claim and the party supporting or enforcing the litigation.").

<sup>144</sup> See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 cmt. e (1971) (stating that the prime objectives of contract law—ensuring certainty and predictability—can best be obtained by permitting parties to a contract to choose the applicable law governing the validity of their contract, even though they would be able to escape prohibitions such as champerty that would otherwise invalidate their agreement).

litigation arising out of the agreement (that is, a New Jersey forum-selection clause). Obviously, "choosing" the applicable law is not that simple: the unfettered ability to contract around a rule of illegality is an inherently paradoxical concept.<sup>145</sup> Not surprisingly, there are limitations on the ability to contract around a rule of illegality.<sup>146</sup>

In each state, choice-of-law rules determine which state's laws govern the validity of an agreement and whether the parties' choice of law will be honored or ignored. Unfortunately, although predictability and uniformity are two of the key policy goals underlying the conflict-of-laws field,<sup>147</sup> conflict of laws may very well be the least predictable and uniform area of the law.<sup>148</sup> Nevertheless, it is fair to say that three basic approaches to conflict of laws have emerged: the traditional approach (that is, *lex loci contractus* in contracts cases), the Restatement (Second) of Conflict of Laws, and "interest analysis."<sup>149</sup> Courts, however, frequently combine these approaches,<sup>150</sup> and the approaches themselves overlap somewhat. This Part cumulatively analyzes Champerco's

<sup>145</sup> If parties could freely contract around a rule invalidating their agreement, the rule would be transformed from a rule of validity to a rule of interpretation. See *id.* § 187 (distinguishing between the parties' ability to choose the law to govern the interpretation of their agreement and their ability to choose the law governing the validity of the agreement).

<sup>146</sup> See *id.* (allowing a forum to refuse to follow the parties' choice of law when the chosen law would contravene a fundamental policy of a state that has a materially greater interest than the state of the chosen law in the determination of the particular issue).

<sup>147</sup> See *id.* § 6(2)(f) & cmt. d ("Adoption of the same choice-of-law rules by many states will further the . . . values of certainty, predictability and uniformity of result.").

<sup>148</sup> See ROBERT A. SEDLER, *ACROSS STATE LINES* 1 (1989) (quoting Professor Prosser's reference to the conflict-of-laws jurisprudence as a "dismal swamp").

<sup>149</sup> Interest analysis was developed by Brainerd Currie. See generally BRAINERD CURRIE, *SELECTED ESSAYS ON THE CONFLICT OF LAWS* 183-84 (1963) (arguing that if a court "finds that the forum state has an interest in the application of [the] policy [expressed in its laws], it should apply the law of the forum, even though the foreign state also has an interest in the application of its contrary policy," but that, if the forum state finds that it has no interest in the application of its policy and that the foreign state has such an interest, the court should apply the law of the foreign state). Another modern approach to conflict of laws is the *choice-influencing considerations* approach developed by Robert A. Leflar. See generally Robert A. Leflar, *Conflicts Law: More on Choice-Influencing Considerations*, 54 CAL. L. REV. 1584, 1586 (1966) (outlining and elaborating the major choice-of-law considerations: (1) predictability of results, (2) maintenance of interstate and international order, (3) simplification of the judicial task, (4) advancement of forum's governmental interests, and (5) application of the better rule of law).

<sup>150</sup> See SEDLER, *supra* note 148, at 28.

agreements under each of the three conflicts approaches and demonstrates that Champerco can ensure the enforceability of its agreements by contracting in New Jersey and including New Jersey choice-of-law and forum-selection clauses in its agreements.

### A. *Lex Loci Contractus*

The traditional approach to determining the law governing the validity of a contract, which is also the simplest and most predictable approach, applies the *lex loci contractus*, the law of the place of contracting.<sup>151</sup> The “place of contracting” is the place where the principal event necessary to form the contract takes place.<sup>152</sup> If all states followed the traditional approach, then, through the simple expediency of executing all its contracts in New Jersey, Champerco could choose New Jersey law to govern its agreements, ensuring their enforceability and making litigation investment possible in any state. Few jurisdictions, however, apply the *lex loci contractus* rule.<sup>153</sup> In fact, New Jersey generally follows the Restatement approach.<sup>154</sup> Thus, a champertous agreement executed in New Jersey would not necessarily be enforced, even by a New Jersey court.

### B. *The Restatement and Choice-of-Law Clauses*

#### 1. The Restatement’s “Contacts” Analysis

The most popular approach to conflict of laws is the Restatement (Second) of Conflict of Laws. Under the Restatement, the place of contracting is not itself controlling, but is instead one of several “contacts” evaluated to determine the center of gravity of the transaction or, as the Restatement calls it, the place with “the most significant relationship” to the transaction and the parties.<sup>155</sup> The Restatement lists five “contacts” used to determine the place with the most significant relationship: “(a) the place of contracting,

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<sup>151</sup> See *id.* at 30.

<sup>152</sup> See RESTATEMENT (FIRST) OF CONFLICT OF LAWS §§ 311-331 (1934).

<sup>153</sup> Florida is one jurisdiction that does apply the *lex loci contractus* rule. See *Sturiano v. Brooks*, 523 So. 2d 1126, 1128-30 (Fla. 1988).

<sup>154</sup> See *State Farm Mut. Auto. Ins. Co. v. Estate of Simmons*, 417 A.2d 488, 491-92 (N.J. 1980) (adopting the Restatement’s approach, albeit in slightly modified form, in insurance contract cases). *But see Pfau v. Trent Aluminum Co.*, 263 A.2d 129, 130-31 (N.J. 1970) (applying the interest analysis approach in a tort case).

<sup>155</sup> RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 188 (1971).

(b) the place of negotiation of the contract, (c) the place of performance, (d) the location of the subject matter of the contract, and (e) the domicile, residence, nationality, place of incorporation and place of business of the parties."<sup>156</sup> Ostensibly, these contacts are counted up, and the state where the contacts are predominantly concentrated, if any, is the place with the most significant relationship, or center of gravity.

Under this approach, Champerco can incorporate and establish its principal place of business in New Jersey, and it can negotiate and execute all its contracts in New Jersey. Unless the location of the contract's subject matter, the place of performance, and the residence of the plaintiff are all in another single state, New Jersey will be the state with the most significant relationship, and, presumably, New Jersey law will apply. This solution, however, falls short in two respects.

First, the probability that the location of the subject matter of the contract, the place of performance, and the residence of the plaintiff are all in one state is not entirely unlikely. The subject matter of the champertous agreement is the plaintiff's claim, which is located in the state where it accrues,<sup>157</sup> very likely the state of the plaintiff's residence. Furthermore, the forum of the litigation, which may also be the place of performance of the champertous agreement,<sup>158</sup> is also likely to be in the state where the claim accrues and, thus, also the state of the plaintiff's residence.

Second, although, at first glance, the Restatement appears to take a relatively simplistic contacts-counting approach, close examination reveals that the Restatement is quite a bit more sophisticated. For instance, the Restatement provides that the contacts should be evaluated according to their relative importance to the issue.<sup>159</sup> The Restatement also provides a list of choice-of-law principles in light of which the contacts are to be evaluated.<sup>160</sup> These principles include, among others, the relevant policies of the forum, the relevant policies of other interested states and the relative interest of those states in the determination of the particu-

<sup>156</sup> *Id.*

<sup>157</sup> See *Koro Co. v. Bristol-Myers Co.*, 568 F. Supp. 280, 286 (D.D.C. 1983).

<sup>158</sup> If the contract designates a particular forum for the underlying action, and Champerco is required to make some performance in the forum (for example, carry on the litigation), then the forum is the place of performance.

<sup>159</sup> See *RESTATEMENT (SECOND) OF CONFLICT OF LAWS* § 188(2) (1971).

<sup>160</sup> See *id.* § 6 (listing factors relevant to the choice of the applicable rule of law pursuant to § 188).



lar issue, and the basic policies underlying the particular field of law.<sup>161</sup> These principles inject too much uncertainty into the Restatement's approach for Champerco to rely on its aggregation of New Jersey contacts to ensure the application of New Jersey law to its agreements.

## 2. Choice-of-Law Clauses

A much simpler and more obvious solution, provided for in the Restatement, is for Champerco to designate in its champertous agreements that New Jersey law governs the agreement. The Restatement directs the court to follow the parties' choice of law unless:

application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which, under the rule of § 188, would be the state of the applicable law in the absence of an effective choice of law by the parties.<sup>162</sup>

Although choice-of-law clauses essentially give parties the ability to opt out of a contractual rule of illegality and override the law, the Restatement contemplates and condones this result within the prescribed limits.<sup>163</sup> Theoretically, then, Champerco can create valid champertous agreements, enforceable in every state,<sup>164</sup> simply by designating New Jersey law as the law governing the agreement. The only requirement is that the application of New Jersey law will not be contrary to a "fundamental policy" of a state with a "materially greater interest" in the application of its law to the determination of the validity of the champertous agreement.<sup>165</sup>

The Restatement's "fundamental policy" and "materially greater interest" test is essentially a modified version of the "interest analysis" approach, an approach that has not yet been considered. Therefore, the analysis and discussion of choice-of-law clauses under

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<sup>161</sup> See *id.*

<sup>162</sup> *Id.* § 187(2)(b).

<sup>163</sup> See *id.* § 187 cmt. e (rejecting traditional ideas that giving the parties to a contract the power to choose the law governing their agreement is tantamount to delegating legislative power to them).

<sup>164</sup> Although not every state follows the Restatement, the Restatement's approach to choice-of-law clauses is essentially the only approach. The approach is very flexible, however, and may be applied with different results by different states. See *infra* part IV.F.1.

<sup>165</sup> See *supra* note 162 and accompanying text.

the Restatement will be partially subsumed under and partially deferred until after the following discussion and application of the "interest analysis" approach to Champerco's agreements.

### C. Interest Analysis

The interest analysis approach resolves choice-of-law problems by analyzing the interests of the relevant states in the application of their laws.<sup>166</sup> Determining the applicable law under interest analysis is of great practical significance because, regardless of whether a court purports to follow the interest analysis approach or purports to follow some other approach,<sup>167</sup> the interest analysis approach most accurately predicts which state's law a court will actually apply.<sup>168</sup> Furthermore, as previously noted, the Restatement's approach to choice-of-law clauses is a modified interest analysis. Consequently, a thorough application of interest analysis to Champerco's agreements is necessary to predict whether courts will enforce such agreements. Additionally, the policy-oriented nature of interest analysis lends itself as an excellent vehicle for exploring and critiquing the policies underlying champerty laws.

The fundamental interest analysis rule is that the law of the forum governs any particular issue unless it is displaced by the law of another state with a greater interest in the application of its law to that issue.<sup>169</sup> The interest of a state in the application of its law is determined by the policies reflected in the content of its law, in light of the state's contacts to the issue.<sup>170</sup> In relation to the contacts-centered approaches, interest analysis differs in that contacts are significant, not in and of themselves, but only to the extent that a particular state's policy is affected through that contact.<sup>171</sup>

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<sup>166</sup> See SEDLER, *supra* note 148, at 38 ("In considering whether the forum should displace its own law, the court should first look to the *content* of the differing laws of the forum and the other involved state or states. The content of a state's law will reflect a *policy*, and the court must determine whether, in light of that policy, one or more states has an *interest* in having its law applied . . .").

<sup>167</sup> See *id.*

<sup>168</sup> See *id.* at 40 ("[T]he results that the courts reach in the cases coming before them for decision are generally consistent with the interest analysis approach.").

<sup>169</sup> See *id.* at 38.

<sup>170</sup> See *id.*

<sup>171</sup> See *id.* at 37-38.

The most salient feature of interest analysis is that it eliminates "false conflicts."<sup>172</sup> False conflicts arise when a state has contacts to a particular issue but has no real interest in the application of its law to the determination of that issue.<sup>173</sup> A state has an "interest" if and only if the application of that state's law will actually further the purposes and policies of the law.<sup>174</sup> If it will not, then that state's law creates a false conflict, and it will not be applied. The classic example of a false conflict is the application of a forum's guest statute to bar a passenger's recovery against a driver for injuries incurred in an accident in the forum state.<sup>175</sup> Where both the driver and passenger are residents of another state, the forum has no interest in the application of its guest statute, even though the accident occurred in the forum state. The reason is that the purposes of the forum's guest statute—to protect its drivers from ungrateful guests—will not be furthered by the application of the guest statute to this case, since both the driver and the passenger are residents of another state.<sup>176</sup>

#### D. *Interest Analysis and Champerty*

Since there is an apparent conflict between New Jersey law, under which Champerty's agreements are valid, and the laws of all other potentially interested states, where such agreements are invalid, the policies underlying each of these potentially interested states' laws must be identified and evaluated to determine whether they create real interests or merely false conflicts. Part III identified some of the early policies that drove the development of ancient champerty doctrine. These policies, however, are obsolete,<sup>177</sup> as some courts have explicitly recognized.<sup>178</sup> Nevertheless, many

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<sup>172</sup> *Id.*

<sup>173</sup> *See id.*

<sup>174</sup> *See id.*; see also Bruce Posnak, *Choice of Law—Interest Analysis: They Still Don't Get It*, 40 WAYNE L. REV. 1121, 1137 (1994) ("Whether a state has an 'interest' depends solely upon whether it is reasonable to conclude that a policy behind that state's competing law would be advanced if that law were applied.").

<sup>175</sup> For an example of what some have considered to be the paradigm "false conflict" case, see *Babcock v. Jackson*, 191 N.E.2d 279, 283 (N.Y. 1963).

<sup>176</sup> *See* SEDLER, *supra* note 148, at 38.

<sup>177</sup> For a discussion of why the policies are obsolete, see *supra* notes 72-75 and accompanying text; *infra* notes 189-91 and accompanying text. *See also* Radin, *supra* note 55, at 66-68 (noting that "the background against which the law of champerty and maintenance grew up . . . has disappeared," and "a new basis ha[s] to be found").

<sup>178</sup> *See, e.g., Brown v. Bigne*, 28 P. 11, 12 (Or. 1891) ("The doctrine of champerty . . . arose from causes peculiar to the state of society in which it was established.").

courts continue to invoke the common law doctrine against champerty, offering no insight into its modern policy justifications and hiding behind conclusory statements that such agreements are contrary to public policy.<sup>179</sup>

Although a court applying interest analysis must give deference to another state's policy decisions and has no license to discount another state's policy simply because the court does not approve of the policy,<sup>180</sup> a competing law based on clearly obsolete policies would be deemed a false conflict because a state has no interest in the application of its law to further policies it no longer maintains.<sup>181</sup> The challenge to courts applying interest analysis in the champerty context is to cut through the cobwebs of ancient champerty doctrine and find the contemporary policies that drove another state's courts or legislature to preserve the doctrine. The dearth of authority expounding on the modern policies underlying champerty laws makes it extremely difficult to conduct an interest analysis with any integrity.<sup>182</sup> However, from the scant sources that do discuss the modern policy justifications against champerty, the following policies emerge: the prevention of speculation in litigation,<sup>183</sup> the discouragement of frivolous claims,<sup>184</sup> and the

<sup>179</sup> See *Barrelli v. Levin*, 247 N.E.2d 847, 850 (Ind. Ct. App. 1969) ("The public policy reason for making . . . champertous contracts void is not always mentioned in the early cases.").

<sup>180</sup> *But see* RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 cmt. g (1971) ("The forum will apply its own legal principles in determining whether a given policy is a fundamental one . . . and whether the other state has a materially greater interest than the state of the chosen law in the determination of the particular issue.").

<sup>181</sup> See *id.* (stating that a rule "tending to become obsolete" probably does not embody a "fundamental policy").

<sup>182</sup> See *Barrelli*, 247 N.E.2d at 850.

<sup>183</sup> See *Pritzker v. Yari*, 42 F.3d 53, 65-66 (1st Cir. 1994) (declaring that "the district court hit the bull's-eye when it declared that the 'single, serious purpose' of [Puerto Rico's champerty statute] is 'to discourage financial speculation in litigation'" (quoting *Pritzker v. Yari*, No. CIV.92-2825, 1993 WL 7160, at \*5 (D.P.R. Mar. 5, 1993))); *Koro Co. v. Bristol-Myers Co.*, 568 F. Supp. 280, 288 (D.D.C. 1983) (declaring that the purpose of the New York champerty law is "to prevent trafficking and speculation in lawsuits."); 14 C.J.S. *Champerty & Maintenance* § 2 (1991) ("The laws against champerty . . . are aimed at the prevention of . . . speculation in lawsuits.").

<sup>184</sup> See *Peck v. Heurich*, 167 U.S. 624, 630 (1897) (finding that champerty encourages "baseless litigation"); *Barrelli*, 247 N.E.2d at 850 ("When the public policy behind the rule is stated, however, it is usually said that [champertous] contracts tend to promote litigation and to multiply lawsuits."); *Killian v. Millard*, 228 Cal. App. 3d 1601, 1604 (Ct. App. 1991) (citing the lower court's finding that champertous agreements are against public policy because they foment litigation); 14 C.J.S. *Champerty & Maintenance* § 2 ("The laws against champerty . . . are aimed at the prevention of multitudinous and useless lawsuits.").

prevention of harassment, strife, and discord.<sup>185</sup> Each of these policies must be evaluated to determine whether and when it creates a state interest in the application of its law against champerty or whether it creates only false conflicts.<sup>186</sup>

It is important to bear in mind the context in which a court will apply interest analysis. The issue of the validity of Champerco's champertous agreements does not arise in the underlying champertous lawsuit, because Champerco will bring that action in the name of the real plaintiff-assignor.<sup>187</sup> The issue will only arise after the plaintiff, acting for or with the help of Champerco, has obtained a substantial judgment or settlement and then repudiates its agreement with Champerco. When Champerco sues the plaintiff to enforce the champertous agreement, the plaintiff will raise champerty as an affirmative defense, claiming that the forum's law, or some law other than New Jersey's, governs the agreement and that the agreement is void and unenforceable as illegal or against public policy under that state's laws. Champerco will counter with the argument that New Jersey law governs the agreement and that the agreement is therefore valid and enforceable. The forum will then look to the policies underlying the potentially applicable champerty laws to determine whether those laws create false conflicts or whether the application of those champerty laws would further their underlying purposes or policies.

### 1. Speculation in Litigation

The most frequently cited policy underlying champerty laws is the policy against speculation in litigation.<sup>188</sup> The goals and purposes of this policy are far from clear. Under the ancient common law, speculation in litigation was discouraged as tending to

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<sup>185</sup> See *Fairchild Hiller Corp. v. McDonnell Douglas Corp.*, 270 N.E.2d 691, 693 (N.Y. 1971) (noting that the policy underlying New York's champerty statute is the prevention of "strife, discord and harassment which could result from permitting [the] purchase [of] claims for the purpose of bringing actions thereon"); *Brown v. Bigne*, 28 P. 11, 13 (Or. 1891) (stating that modern champerty "is confined to cases where a man, for the purpose of stirring up strife and litigation, encourages others . . . to bring actions").

<sup>186</sup> When dealing with choice-of-law clauses under the Restatement, there is actually another requirement—that the policy be a fundamental one. See *RESTATEMENT (SECOND) OF CONFLICT OF LAWS* § 187 (1971).

<sup>187</sup> See *supra* part III.C.

<sup>188</sup> See, e.g., *Pritzker v. Yari*, 42 F.3d 53, 65-66 (1st Cir. 1994); *Koro Co. v. Bristol-Myers Co.*, 568 F. Supp. 280, 288 (D.D.C. 1983).

lead to "the abhorred sin of usury."<sup>189</sup> This was part of the common law's effort at frustrating capitalism.<sup>190</sup> Usury (that is, loans on interest) is no longer an "abhorred sin"; in fact, along with speculation, it is the cornerstone of our modern capitalist economy.<sup>191</sup>

Perhaps the modern application of the policy against speculation in litigation is the paternalistic policy against gambling, an extreme form of speculation. Although investing in litigation is distinguishable from gambling,<sup>192</sup> there is support for the proposition, that the policy is directed against "gambling" on lawsuits.<sup>193</sup> If preventing gambling is the policy underlying modern champerty laws, then, in the context of Champerco, champerty laws only create false conflicts. Since the gambler, Champerco, is a New Jersey corporation, New Jersey would be only the state<sup>194</sup> with a real paternalistic interest in the application of its law to prevent Champerco from gambling. The problem, of course, is that New Jersey has no law or policy against champerty. Since none of the other involved states' paternalistic policies against gambling would be furthered by the application of their champerty law to Champerco's agreement, their champerty laws create only false conflicts.

More likely, however, rather than embodying a paternalistic desire to protect gamblers from their own improvidence, the policy against speculation in litigation represents a policy against doubtful and *speculative* (that is, frivolous) actions for the purpose of harassing others and stirring up strife.<sup>195</sup> The most thorough

<sup>189</sup> Radin, *supra* note 55, at 61; *see also id.* at 69 ("To acquire a share in [] a claim is essentially a speculation and in the Middle Ages is tainted with the discredit which attached to every form of speculation.")

<sup>190</sup> *See id.* at 65 ("Champerty . . . had its source in the resistance to the slowly growing capitalism that followed the Renaissance of the eleventh and twelfth centuries.")

<sup>191</sup> *See id.* at 70.

<sup>192</sup> Whereas gamblers simply pool their monies and then redistribute the monies to the winners, the winnings from speculation in litigation are not drawn from the speculators' monies, but from the proceeds of a successful claim. Therefore, theoretically, there can be an expected net positive gain from investing in litigation, unlike in gambling, where there is an expected net positive loss.

<sup>193</sup> *See, e.g.,* Brown v. Bigne, 28 P. 11, 13 (Or. 1891) ("The doctrine of champerty is directed against speculation in lawsuits, and to repress the gambling propensity of buying up doubtful claims."); OFFERING CIRCULAR, *supra* note 11, at 8 (identifying gambling establishments as potential competitors to investing in litigation).

<sup>194</sup> Champerco's shareholders and investors are in a sense also gamblers, but they are not directly a party to Champerco's agreements and their impact is too diluted to create an interest in the application of the state law of the shareholders.

<sup>195</sup> *See* 14 C.J.S. *Champerty and Maintenance* § 3 (1991).

judicial discussion of the contemporary evils against which champerty laws are directed is found in the oft-cited case of *Brown v. Bigne*.<sup>196</sup> In *Bigne*, the court enforced a champertous agreement, distinguishing between “the *bona fide* acquisition of an interest in the subject of litigation [and] an unfair or illegitimate transaction, gotten up for the purpose merely of spoil or speculation.”<sup>197</sup>

The line is not entirely clear, but the court’s opinion seems to indicate that an illegitimate transaction is one entered into for the purpose of stirring up strife or litigation or harassing others.<sup>198</sup> Some courts have expressly stated that the underlying basis of the law against champerty and the policy against speculation in litigation is the tendency of champerty to encourage harassment, strife, and discord.<sup>199</sup> The policy against speculation in litigation, then, is a policy against frivolous claims, and is based on the concern that speculation in litigation has a tendency to encourage others “to bring actions . . . which they have no right to” bring, “for the mere purpose or desire of perpetuating strife and litigation.”<sup>200</sup>

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<sup>196</sup> 28 P. 11 (Or. 1891).

<sup>197</sup> *Id.* at 13.

<sup>198</sup> In at least six different places, the court refers to the illegitimate purposes that may justify the application of champerty laws to invalidate an agreement. The case is not entirely clear and consistent and, at some points, seems to include speculation in litigation as an illegitimate purpose distinct from the problems of stirring up strife and litigation or harassing others. On the whole, the latter two purposes seem to dominate the court’s understanding of the modern policy justifications against champerty.

<sup>199</sup> See, e.g., *Fairchild Hiller Corp. v. McDonnell Douglas Corp.*, 270 N.E.2d 691, 693 (N.Y. 1971) (“The legislative concern is . . . [t]o prevent the . . . strife, discord and harassment which could result from permitting attorneys and corporations to purchase claims for the purpose of bringing actions thereon.”); see also *Koro Co. v. Bristol-Myers Co.*, 568 F. Supp. 280, 288 (D.D.C. 1983) (citing *Fairchild* and interpreting New York’s policy of preventing strife, discord, and harassment as a policy against trafficking and speculating in litigation). Although *Brown v. Bigne* held that champertous agreements are invalid only when made for an “illegitimate” purpose (such as stirring up strife), other states that invalidate *all* champertous agreements presumably are concerned with the tendency or potential for champerty to foster these illegitimate purposes. Thus, although the holding in *Brown v. Bigne* is directly contrary to the champerty laws of many other states, and, indeed, is often cited as support for enforcing a champertous agreement, the case nevertheless is an accurate expression of the modern policies underlying champerty laws. Other states simply find that these policies justify broader laws against champerty, not limited to circumstances in which the potential evils of champerty are directly involved.

<sup>200</sup> *Bigne*, 28 P. at 13.

## 2. Frivolous Claims

Champerty's tendency to encourage frivolous claims is frequently cited as the modern justification for its prohibition.<sup>201</sup> The basis for assuming that champerty tends to encourage frivolous claims has never been examined. *Brown v. Bigne*<sup>202</sup> suggests that the law is concerned that champerty encourages people to bring claims that they would not otherwise have brought.<sup>203</sup> This would mean that the law draws two inferences. First, the law assumes that, if a plaintiff sells part or all of his claim, he would not otherwise have brought the claim himself. Second, the law assumes that, if a plaintiff would not have brought a claim, then the claim is frivolous. In other words, the two inferences are first, if a claim is meritorious, the claimant will bring the claim, and second, if a plaintiff is willing to bring a claim, the plaintiff will not sell all or part of that claim.

Admittedly, the two inferences are weak and have never been empirically supported. Based on this line of reasoning, however, many states, by indiscriminantly invalidating all champertous agreements, maintain an irrebuttable presumption that the claims underlying these agreements are frivolous.<sup>204</sup> Assuming that there is a rational connection between champerty and frivolous claims, three states may have an "interest" in the application of their champerty laws to Champerco's agreements in furtherance of their policies against frivolous claims: the forum of the enforcement action (the "enforcement forum"), the forum of the underlying champertous lawsuit (the "underlying forum"), and the state of the defendant's residence (the "defendant state").

### a. *The Enforcement Forum*

At first glance, it might appear that when Champerco brings an action to enforce its champertous agreements, the enforcement forum has an "interest" in applying its champerty laws to invalidate the agreement and to dismiss the "champertous" lawsuit. Under its

<sup>201</sup> See *Peck v. Heurich*, 167 U.S. 624, 630 (1897).

<sup>202</sup> 28 P. 11 (Or. 1891).

<sup>203</sup> See *id.* at 13 (stating that the doctrine of champerty "is confined to cases where a man . . . encourages others . . . to bring actions [which they] otherwise would not" bring); see also *Simon*, *supra* note 21, at 11 ("The major arguments against syndicated lawsuits are [that] syndication stirs up litigation . . . that otherwise would never be brought . . .").

<sup>204</sup> But see *Bigne*, 28 P. at 13 (holding that champertous agreements should not be held per se void, as they "may sometimes be in furtherance of justice").



champerty law, the forum presumes that "champertous" lawsuits are frivolous, and frivolous claims waste courts' time and resources, clogging their dockets. Under interest analysis, however, assuming that the enforcement forum was not also the underlying forum, the enforcement forum's champerty laws create only a false conflict because the forum has no "interest" in the application of its champerty laws to invalidate Champerco's agreements. More specifically, the application of the enforcement forum's champerty law to invalidate Champerco's agreement will not advance the law's underlying policy against frivolous claims.

Although the enforcement forum may presume that "champertous lawsuits" are frivolous, Champerco's enforcement action is not a "champertous lawsuit." To the enforcement forum, Champerco's enforcement action is no different than any other contract enforcement action. The fact that this contract would be illegal and void under the enforcement forum's champerty laws is irrelevant, because the enforcement forum's interest in deterring frivolous claims is not implicated by this contract. Although the law may presume that a claim supported by or subject to a champertous agreement is frivolous, there is no reason to assume that a contract enforcement action is frivolous simply because the contract relates to a frivolous claim.

To understand the point a bit more clearly, the line of inferences, delineated earlier, that connects champerty and the policy against frivolous claims must be applied. The law usually assumes that a plaintiff who is willing to bring a claim will not sell all or part of the claim. Therefore, if a plaintiff does, in fact, sell part of the claim, we can infer that, but for the champertous agreement, the plaintiff would not have brought the claim, and that the claim is therefore frivolous. This same logic becomes circular when it is applied to an action to enforce a champertous agreement: The enforcement action is frivolous because, but for the champertous agreement, no action to enforce the champertous agreement would have been brought. If we accept this argument, then all contract-enforcement actions are frivolous because, but for the making of the contract, there would be no enforcement action. The fact that champertous agreements, unlike other contracts, are illegal does not change the fact that invalidating the agreement, which presumably promoted a frivolous claim in the *underlying forum*, will not further the *enforcement forum's* policy against frivolous claims. If any state has an "interest," it is the underlying forum.

b. *The Underlying Forum*

Unlike the policies of the enforcement forum, the underlying forum's policy against frivolous claims is affected by the underlying champertous, and presumably frivolous, lawsuit that takes place in its courts. Frivolous lawsuits waste limited judicial resources and clog the courts' dockets, preventing or delaying access to justice to other plaintiffs with meritorious claims. Apparently, then, the underlying forum has an interest in the application of its law by the enforcement forum to invalidate Champerco's champertous agreement in order to protect its courts from frivolous claims.<sup>205</sup> Nevertheless, the underlying forum's policy against frivolous claims creates only a doubtful, or at most marginal, "interest" in the application of its champerty law by the enforcement forum.

i. An "Interest" Based on a Legal Fiction

One problem with the underlying forum's purported "interest" is that, although the underlying forum may have presumed that the underlying champertous lawsuit was frivolous, the enforcement forum—which has the benefit of hindsight—can see that the underlying lawsuit was not in fact frivolous. When a plaintiff obtains a recovery that is substantial enough for the plaintiff to repudiate its champertous agreement and substantial enough for Champerco to bring an enforcement action, the facts militate strongly against the legal presumption that the claim was frivolous. Furthermore, if the underlying claim was frivolous, then the underlying forum itself should have vindicated its own policy against frivolous claims through dismissal, sanctions, or summary judgment.<sup>206</sup> Certainly, if the underlying forum actually rendered judgment in favor of the plaintiff, the presumption of frivolousness is rebutted. Legal fictions do not create real "interests." The underlying forum's "interest" in weeding out frivolous claims will not be advanced by invalidating an agreement that promoted a manifestly meritorious

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<sup>205</sup> See *Pritzker v. Yari*, 42 F.3d 53, 62-64 (1st Cir. 1994) (emphasizing, in the context of a "minimum contacts" analysis, the underlying forum's interest).

<sup>206</sup> See *Brame v. Ray Bills Fin. Corp.*, 85 F.R.D. 568, 578 n.6 (N.D.N.Y. 1979) (stating that "[i]t is questionable whether [the fear that champerty will result in a greater number of vexatious or frivolous lawsuits] . . . is a sufficient justification for the prohibition on [champerty], in view of the existence of other safeguards against frivolous litigation, such as summary judgment").

claim, regardless of the underlying forum's presumption that the claim was frivolous. The underlying forum's "interest," therefore, is highly questionable.

## ii. Deterrence and Open Courts

Despite the fact that it might be apparent, with the benefit of hindsight, that Champerco's underlying lawsuit was not frivolous, the underlying forum may nevertheless have a general deterrence interest in the application of its champerty law to invalidate Champerco's agreement in order to discourage future champertous lawsuits, which the underlying forum presumes are frivolous. Finding that the underlying forum has a deterrence "interest" in the application of its champerty law assumes that invalidating a champertous agreement that promoted a meritorious claim will further the policies of the underlying forum's champerty law. This assumption, however, is seriously flawed.

Some measure of deterrence against frivolous claims will likely be achieved by invalidating a champertous agreement that promotes a meritorious claim. However, when the true nature of the policy against frivolous claims and champerty is considered, the small measure of deterrence achieved appears insignificant in light of the countervailing adverse effects on the underlying forum's "open courts" policy.

### (a) *Dual Policies*

Rules against frivolous claims represent a balance between two competing policies: (1) providing all meritorious claimants their day in court (the "open courts" policy) and (2) eliminating all claims that have no merit (that is, frivolous claims).<sup>207</sup> In designing sanctions rules against frivolous claims, legislatures and courts seek to balance these two policies.<sup>208</sup>

Because frivolous claims must be eliminated, if at all, at an early stage of litigation, these rules must establish a threshold which claims must meet before they are heard.<sup>209</sup> Inevitably, because

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<sup>207</sup> See Byron C. Keeling, *Toward a Balanced Approach to "Frivolous" Litigation: A Critical Review of Federal Rule 11 and State Sanctions Provisions*, 21 PEPP. L. REV. 1067, 1152 (1994) (stating that "a sanctions scheme must respect both the interest in preserving free access to the courts and the interest in redressing litigation abuse").

<sup>208</sup> See *id.*

<sup>209</sup> See *id.* at 1094-1125 (discussing three approaches to drawing the line between frivolous and nonfrivolous claims in sanctions provisions).

claims will be evaluated before they are fully heard, some meritorious claims will fall short of the threshold and will be denied their day in court, and some meritless claims will nevertheless meet the threshold and will be fully heard. The point is that the line, wherever drawn, does not separate the meritorious claims from the meritless claims, but represents a dividing point on a slippery slope. On the average, claims falling below the line will be frivolous.<sup>210</sup> With regard to these claims, the open courts policy is subordinated to the policy against frivolous claims, and these claims will be dismissed and discouraged. Claims rising above the line, on the average, will be meritorious. With regard to these claims, the policy against frivolous claims is subordinated to the open courts policy, and these claims are permitted and encouraged.

Champerty laws represent a line that states draw in the implementation of their policies against frivolous claims. These laws do not presume that *all* champertous agreements promote frivolous claims and are therefore against public policy. The law recognizes, as illustrated in Part I, that champertous agreements often promote access to the courts by meritorious claimants who cannot otherwise afford to bring their claims or who prefer to avoid the risk, hassle, and delay of litigation.<sup>211</sup> Champerty laws simply presume that, on the average, champertous agreements promote frivolous claims. The open courts policy is therefore subordinated to the policy against frivolous claims, and champertous agreements are prohibited.

The pertinent point is that the open courts policy is *subordinated* by champerty laws, but not eliminated.<sup>212</sup> The fact that it is the

<sup>210</sup> This does not mean that a majority of the claims falling below the threshold will be frivolous, but rather that the benefit of the frivolous claims excluded outweighs the harm of the meritorious claims excluded.

<sup>211</sup> See *Brown v. Bigne*, 28 P. 11, 13 (Or. 1891) ("Indeed, it may sometimes be in furtherance of justice and right that a suitor who has a just title to property, and no means except the property itself, should be assisted [by a] fair *bona fide* agreement . . . to supply funds to carry on [the] pending suit, in consideration of having a share in the property if recovered . . ."); 14 AM. JUR. 2D *Champerty & Maintenance* § 1 (1964) ("[T]o transfer a right of action or to maintain the suit of another . . . will by no means necessarily produce mischief or oppression. . . . [S]uch . . . maintenance will have a tendency to secure rights and promote the ends of justice.").

<sup>212</sup> This is evidenced by the fact that in some states champerty laws invalidate champertous agreements only when the agreements are against "public policy" or entered into for "illegitimate" purposes. Connecticut, for example, has taken a public policy approach. See *Rice v. Farrell*, 28 A.2d 7, 8 (Conn. 1942) ("[T]he only test is whether a particular transaction is against public policy."). Alabama and Oregon have taken a "legitimate purpose" approach. See *Bigne*, 28 P. at 13 (holding that

policy against frivolous claims that is evinced by the champerty law should not mask the existence of a subordinate policy which may become dominant in particular cases. When it is clear that the underlying claim was not frivolous, then the underlying forum's policy against frivolous claims is subordinated to its open courts policy, and the underlying forum has no "interest" in the application of its champerty law by the enforcement forum to invalidate the agreement. The fact that Champerco's champertous agreement would be illegal under the underlying forum's champerty law does not necessarily translate into an "interest" by the underlying state in the application of its law. The beauty of interest analysis is that, although the underlying forum would apply its law indiscriminately, regardless of which policy dominates in a particular case, the enforcement forum is not constrained by the underlying forum's law, and need only apply the underlying forum's champerty law when the underlying forum has an "interest" in its application, that

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champertous agreements must be carefully scrutinized to determine whether they were made with the "*bona fide* object of assisting a claim believed to be just [or] for the [illegitimate] purpose of injury and oppressing others by aiding unrighteous suits"); *Lott v. Kees*, 165 So. 2d 106, 108-11 (Ala. 1964) (adopting the *Bigne* approach).

New York has drawn a bright-line rule against champerty, but has carved out an exception for one class of plaintiffs whose legitimate purpose in selling their claims is readily apparent. See N.Y. JUD. LAW § 489 (McKinney 1983) (allowing the purchase of claims from bankruptcy trustees and other receivers who are in charge of winding up estates so as to "facilitate" the expeditious liquidation of these estates); *People v. Berlin*, 317 N.Y.S.2d 191, 193 (Nassau County Ct. 1971) (discussing the facilitation of expeditious liquidation and final settlement of certain estates); see also *supra* note 88 (elaborating on this exception). New York's exception further illustrates that in champerty laws, the "open courts" policy is merely subordinated to the policy against frivolous claims. In fact, every state, by permitting contingent fee agreements, which are a form of champerty, has decided that in some circumstances the open courts policy should prevail over the policy against frivolous claims. See *Richette v. Solomon* 187 A.2d 910, 918 (Pa. 1963) ("Contingent fees . . . enable some just claims to be recovered which the circumstances of the parties would otherwise defeat, while on the other hand they certainly tend to encourage litigation of a speculative and unfounded character, which is against the true interests of society. But wisely or unwisely, a point on which opinions may fairly differ, the law has long been settled that contracts 'for such fees are lawful and enforceable by the courts and something more than the mere contingency of the compensation is necessary to make them [illegal].'" (quoting *Williams v. Philadelphia*, 57 A. 578, 579 (Pa. 1904))).

Conversely, New Jersey, in which the "open courts" policy has prevailed and champerty is legal, has a strong public policy against frivolous claims. See N.J. STAT. ANN. § 2A:15-59.1(a), (b) (West Supp. 1995) (defining a "frivolous" claim as a claim that "was commenced, used or continued in bad faith, solely for the purpose of harassment, delay or malicious injury").

is, when the policy against frivolous claims is dominant and the open courts policy is subordinate.

(b) *The Ultimate Policy*

More than just a subordinate policy, the open courts policy is actually the ultimate policy underlying champerty laws and the policy against frivolous claims. From the underlying forum's perspective, frivolous claims waste limited judicial resources, clog the courts' dockets, and prevent or delay meritorious claimants from having their day in court.<sup>213</sup> The ultimate harm, then, of frivolous claims is that they impede the forum's open courts policy. Thus, eliminating frivolous claims is actually a means of effectuating the underlying forum's open courts policy of promoting free access to the courts for the just, speedy, and inexpensive resolution of legitimate claims,<sup>214</sup> and the ultimate policy goal of champerty laws is to promote free access to courts.

Therefore, when a champertous agreement furthers the underlying forum's open courts policy and enables the underlying plaintiff to bring her meritorious claim, the underlying forum can hardly have an "interest" in the application of its champerty law to invalidate the agreement. Invalidating the agreement will not further the underlying forum's ultimate champerty policy of promoting access to its courts. On the contrary, enforcing Champerco's agreement will encourage other similar agreements that will promote access to the courts for "blue collar plaintiffs" and enable other plaintiffs to receive prompt and certain recoveries.

Ultimately, then, the small additional deterrence against frivolous claims achieved by invalidating meritorious champertous agreements, such as Champerco's, will not further the policy against frivolous claims and ensure free access as much as enforcing such agreements will. Therefore, the underlying forum has no "interest" in the application of its champerty law to invalidate meritorious champertous agreements, such as Champerco's. The underlying forum's champerty law creates only a false conflict, or at best a weak interest, that is not "materially greater" than the interest of New Jersey in the application of its law.<sup>215</sup>

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<sup>213</sup> See Keeling, *supra* note 207, at 1069 (stating that "[frivolous] litigation that serves no function other than to consume court time" must be eliminated).

<sup>214</sup> See FED. R. CIV. P. 1 (instructing that the Federal Rules, which in large part seek to eliminate frivolous claims, should "be construed and administered to secure the just, speedy, and inexpensive determination of every action").

<sup>215</sup> For a discussion of New Jersey's interest, see *infra* part IV.D.3. For a discussion

### iii. Is Hindsight 20/20?

Hindsight is the factor that allows the enforcement forum to promote the interests of the underlying forum and yet reach a different result than the underlying forum would have reached. Since frivolous claims must be weeded out, if at all, before they consume the court's time, the underlying forum is forced to adopt a bright-line rule invalidating all champertous agreements, without seeking to determine whether a particular champertous agreement in fact promotes a frivolous claim. The enforcement forum, on the other hand, passes on the validity of the champertous agreement after the underlying claim has been fully heard and disposed of. It has the opportunity to see, with hindsight, whether or not the champertous agreement actually promoted a frivolous claim and, therefore, whether or not to apply the underlying forum's champerty law.

Another problem, however, presents itself at this point. If the mere existence of an enforcement action is enough to rebut the underlying forum's presumption that the claim was frivolous, then champertous agreements will always be enforced. Only meritorious claims result in enforcement actions, since frivolous claims, by definition, yield no recovery and, therefore, no opportunity for the plaintiff to breach a champertous agreement. The problem, then, is that narrowing the application of the underlying forum's champerty law to truly frivolous claims will fail to effectuate the law's underlying policy of deterring frivolous claims. Champertors will be in a no-lose situation: If the underlying claim results in no recovery, the champertor will have no need to enforce his champertous agreement, and if the underlying claim does result in a recovery, the fact of recovery will be enough to rebut the presumption of frivolousness and enforce the agreement.<sup>216</sup>

To resolve the foregoing problem, it is necessary to examine more thoroughly the interaction between frivolous claims and

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of the Restatement's "materially greater interest" test, see *infra* part IV.E.

<sup>216</sup> Because narrowing the application of the underlying forum's champerty law to frivolous claims will not effectuate the law's purposes, the underlying forum will have an "interest" in the application of its champerty law even to meritorious claims. The underlying forum, by virtue of its law against champerty, has implicitly decided that, in an all-or-nothing situation, enforcing no champertous agreements will further its policies more than enforcing all champertous agreements because the law presumes that, on the average, champertous agreements tend to promote frivolous claims. See *supra* notes 208-11 and accompanying text.

champerty laws. In reality, the foregoing problem presents itself irrespective of any of the arguments set forth in this Comment. Champerty laws seek to deter frivolous claims by eliminating the economic incentives to promote frivolous claims, that is, by denying champertors their share of the litigation proceeds. But, if frivolous claims never yield any proceeds, how can frivolous claims ever be deterred by denying champertors their share in the proceeds? More pointedly, why would a champertor ever invest in a frivolous claim? And why would the law presume that a claim is frivolous because someone contracted for a share of the proceeds?

Obviously, the assumption that frivolous claims never yield any recovery is false. Frivolous claims often yield nuisance settlements, which represent nothing more than the nuisance value of the suit—the expense, harassment, and embarrassment that the defendant may endure in defending the suit. These nuisance settlements provide enough of an incentive for plaintiffs to pursue them<sup>217</sup> and, therefore, for investors to invest in them.

Champerty laws deter such investors by invalidating champertous agreements, eliminating the economic incentive to promote these frivolous claims for their nuisance value. To be effective, then, champerty laws need not invalidate *all* agreements, but only those that promote frivolous claims brought solely for their nuisance value. This narrow application of the underlying forum's champerty law will effectively deter frivolous claims by eliminating the economic incentive—the nuisance settlement—to invest in and promote such claims.

One question remains: How will the enforcement forum determine whether the plaintiff's recovery is a nuisance settlement and the claim is frivolous, or whether the recovery is real and the claim meritorious? To this point, the analysis has proceeded on the assumption that the mere existence of an enforcement action is sufficient to rebut the presumption that

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<sup>217</sup> See COOTER & ULEN, *supra* note 25, at 486 (stating that “nuisance suits are possible between rational plaintiffs and defendants only when a trial is more costly to the latter than the former”); Lucian A. Bebchuk, *Suing Solely to Extract a Settlement Offer*, 17 J. LEGAL STUD. 437, 448 (1988) (“Because defendants might be uncertain whether the expected value to the plaintiff of going to trial is negative or positive, a defendant might make a settlement offer to a plaintiff . . .”); D. Rosenberg & S. Shavell, *A Model in Which Suits Are Brought for Their Nuisance Value*, 5 INT’L REV. L. & ECON. 3, 3 (1985) (arguing that a “defendant should be willing to pay a positive amount in settlement to the plaintiff with the weak case—despite the defendant’s knowledge that were he to defend himself, such a plaintiff would withdraw”).



the underlying champertous lawsuit was frivolous. That assumption, however, is no longer true, as a claim may be frivolous and yet yield a nuisance recovery followed by a breach and an enforcement action.

When the underlying forum renders judgment in favor of the plaintiff, the enforcement forum should have no problem finding that the underlying claim was not frivolous. The issue will only arise when the underlying claim results in a settlement. The enforcement forum will have to make its determination based on the totality of the evidence available, including the evidence presented or discovered at the trial level, the results of any dispositive motions, the absolute size of the settlement, its relationship to the plaintiff's claim,<sup>218</sup> and its relationship to the defendant's expected costs of litigation. Although there is no precise formula, the reality is that trial courts are constantly forced to make such determinations about a claim's merit in response to motions for dismissal, sanctions, and summary judgment—without the benefit of fully hearing the claim. The enforcement forum, therefore, with the aid of hindsight and a fully developed record, should be able to separate the nuisance settlements from the legitimate settlements, or the frivolous claims from the meritorious claims.

The fact that in some instances it will be close to impossible to make a determination whether a settlement was a nuisance settlement or whether a claim was meritorious, should not prevent the enforcement forum from making this determination in cases where the totality of the evidence clearly supports a finding one way or another. Instead, when the enforcement forum is uncertain, it should find: (1) that the underlying forum's presumption that the champertous lawsuit was frivolous is not rebutted; (2) that the application of the underlying forum's champerty law to invalidate the champertous agreement would deter other frivolous claims in the underlying forum and further the underlying forum's champerty law's policy against frivolous claims; (3) that the underlying forum therefore has an "interest" in the application of its champerty law by the enforcement forum; (4) that, in the absence of any competing "interest," the underlying forum's champerty law should apply; and (5) that the champertous agreement is illegal and unenforceable. If, on the

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<sup>218</sup> See 52 AM. JUR. 2D *Malicious Prosecution* § 163 (1970) (noting that the size of the settlement relative to the requested damages may nullify any presumption of probable cause that the settlement may have otherwise carried).

other hand, the enforcement forum finds that the settlement was not a nuisance settlement, it should find: (1) that the underlying claim was not frivolous; (2) that the enforcement of the champertous agreement would promote access to courts by other meritorious claimants; (3) that the underlying forum's champerty law's policy against frivolous claims is, therefore, subordinated to its open courts policy; (4) that the enforcement of the agreement would further the underlying forum's champerty law's ultimate policy goals; (5) that the underlying forum has no "interest" in the application of its champerty law to invalidate the champertous agreement; and (6) that the underlying forum's champerty law, therefore, does not apply.

*c. The Defendant State and Harassment*

The defendant state has an interest in preventing harassment, strife, and discord to its residents. This interest, however, is merely the flip side of a forum's interest in deterring frivolous claims. Frivolous claims force defendants to bear the annoyance and cost of defending themselves against baseless litigation, and a state, therefore, has an interest in protecting its residents from frivolous claims. A state, on the other hand, has no legitimate interest in protecting its residents from meritorious claims.

Essentially, then, the policy of discouraging frivolous claims and the policy of preventing harassment, strife, and discord are simply two distinct states' interests against frivolous claims: an enforcement forum's interest in providing access to its courts and a defendant state's interest in protecting defendants from harassment. Noting this, the above discussion pertaining to the underlying forum's interests is equally applicable to the defendant state. In pertinent part, if the underlying forum's policy against frivolous claims is effectuated, the underlying defendant state has no distinct interest in the application of its champerty law. When the enforcement forum determines that the underlying claim may have been frivolous, it will follow the interests of both the underlying forum and the defendant state in the application of their champerty laws. When, however, the enforcement forum determines that the underlying claim was not frivolous, neither the underlying forum nor the defendant state will have a real interest in the application of their champerty laws.

### 3. Policies Favoring Champerty

Although New Jersey's permissive law on champerty might be characterized as passive and neutral, representing no affirmative policy choices, this mischaracterizes New Jersey's interest in the application of its law.<sup>219</sup> At a minimum, New Jersey has an interest in the enforcement of all contracts made in New Jersey, whether for the sale of goods, the sale of shares in a company, or the sale of shares in a lawsuit.<sup>220</sup> The fact that there is no specific policy for the enforcement of champertous agreements<sup>221</sup> does not mean that New Jersey has no interest in the application of its general contract law to enforce a champertous agreement made in New Jersey by a New Jersey corporation.

In addition to New Jersey's general policy of enforcing contracts, there are affirmative policy reasons for enforcing champertous agreements, although New Jersey courts have never expressed them. One such policy is New Jersey's "open courts" policy,<sup>222</sup> a strong constitutional policy of providing access to the courts for all litigants.<sup>223</sup> Champertous agreements further this open courts policy by allowing litigants who cannot bear the costs of litigation to offer

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<sup>219</sup> See *infra* notes 237-48 and accompanying text (discussing *Koro Co. v. Bristol-Myers, Co.*, 568 F. Supp. 280, 286-87 (D.D.C. 1983), in which the court relied on this mistaken assumption to apply New York instead of New Jersey law).

<sup>220</sup> See *Saxon Constr. & Management Corp. v. Masterclean of North Carolina, Inc.*, 641 A.2d 1129, 1131 (N.J. Super. Ct. Law Div. 1992) ("[I]t has long been the law that the principle of freedom of contract permits competent parties to make . . . agreements as they wish unless the agreement violates public policy . . ."). See generally E. ALLAN FARNSWORTH, *CONTRACTS* 9 (2d ed. 1990) (describing the function of contract law as "furthering the general economic good by encouraging parties to enter into such productive transactions").

<sup>221</sup> But see N.J. STAT. ANN. § 2A:25-1 (West 1987) (specifically allowing assignment of any contract claim).

<sup>222</sup> See Susan L. Martin, *Syndicated Lawsuits: Illegal Champerty or New Business Opportunity?*, 30 AM. BUS. L.J. 485, 486 (1992) ("American policy favoring wide open court doors supports the syndication of lawsuits in certain circumstances and the continued erosion of a champerty defense."); Simon, *supra* note 21, at 11 ("[S]yndication helps claim holders raise sufficient funds to see their claims through."); Abraham, *supra* note 52, at 1298-99 (pointing out a contradiction in states that maintain champerty laws while purporting to maintain "open courts" policies); Cox, *supra* note 13, at 154 (suggesting that "lawsuit syndication can enhance the efficacy of our judicial system by assuring meritorious claim holders adequate means of adjudicating their claims").

<sup>223</sup> This is actually a constitutional right in New Jersey. See *State ex rel. D.H.*, 353 A.2d 570, 572 (N.J. Juv. & Dom. Rel. Ct. 1976) (holding that "though the right of access to the courts is not specifically guaranteed by the New Jersey Constitution, it is a natural and inalienable right derived from Article 1").

shares in their claims in exchange for funds or an agreement to finance their lawsuits. Similar to its policy of providing open courts to all litigants, New Jersey has an interest in the availability of legal redress for all wrongs against New Jersey residents, even in other states. Champerty may further this interest as well. In addition, New Jersey may have an interest in the prompt recovery of compensation and redress for legal wrongs.<sup>224</sup> Champerty allows a plaintiff to sell her claim for an immediate recovery.

In general, however, only New Jersey's policy of enforcing all contracts made in New Jersey will be furthered by the application of New Jersey's law and the enforcement of Champerco's agreements.<sup>225</sup> Its open courts policies are not implicated unless either the underlying champertous lawsuit is in New Jersey or the plaintiff in the underlying lawsuit is a New Jersey resident.

#### 4. Summary of Interest Analysis

Three possible modern policies underlying champerty laws have been identified: (1) preventing speculation in litigation, (2) deterring frivolous claims, and (3) preventing harassment, strife, and discord.

Preventing speculation in litigation, to the extent this policy represents a paternalistic policy against gambling, creates only a false conflict, as the gambler, Champerco, is a New Jersey corporation, and Champerco's agreements are enforceable under New Jersey law. To the extent that the policy of preventing speculation in litigation represents a policy of deterring frivolous claims believed to result from speculation in litigation, the policy creates a doubtful deference interest, if any, in the application of the underlying forum's champerty law. Assuming that Champerco can demonstrate that the underlying claim was patently nonfrivolous, the underlying forum's "interest" is dubious because the policies underlying this champerty law will be furthered more by not having its champerty law applied than by having it applied. Whether the

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<sup>224</sup> See, e.g., *supra* note 88 (discussing New York's policy of facilitating prompt recovery for a certain class of plaintiffs).

<sup>225</sup> The interest of the "place of contracting" is obvious from the great weight the Restatement gives, and the dispositive weight the traditional approach gives, to the place of contracting. This interest also finds support in some of the Restatement's choice-of-law principles, including the protection of the parties' "justified expectation," the "basic policies underlying [contract] law," "predictability . . . of result," and "ease in the determination and application of the law." RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6(2)(d)-(g) (1971).

underlying forum's open courts policy and frivolous claims policy are viewed as dual conflicting policies or as two means to achieve one ultimate policy goal, the balance of these two policies favors the enforcement of Champerco's agreement when the underlying claim was clearly not frivolous and the agreement helped the plaintiff have his day in court.

The policy of preventing harassment, strife, and discord is simply the interest of the defendant state in protecting its constituents from frivolous claims, and as such, creates no distinct state interest other than the underlying forum's interest in eliminating frivolous claims.

On the other side of the coin, two possible policies underlying New Jersey's law permitting champerty were identified: (1) the general policy of enforcing contracts, and (2) the policy of providing open courts. While the second policy conflict creates only a false conflict in most situations, the first policy creates a real "interest."

Although the underlying forum's policy against frivolous claims and the defendant state's policy of preventing harassment create only dubious state "interests," these interests may be sufficient to rise above the level of a false conflict. Therefore, there may be a true conflict between New Jersey law and the champerty laws of the underlying forum and defendant state. There is no accord among the commentators as to how to resolve a true conflict under interest analysis.<sup>226</sup> We need not concern ourselves, however, with the proper approach, since we deal here with a choice-of-law clause, and the Restatement's approach is essentially the only one.

#### E. *The Restatement Revisited*

Under the Restatement, the parties' choice of law will be applied unless its application will contravene a fundamental policy of a state with a materially greater interest that would be the state of applicable law in the absence of an express choice of law.<sup>227</sup>

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<sup>226</sup> Brainerd Currie suggested that the forum should apply its own law. Robert Leflar has suggested applying the better law. For a discussion of Currie's and Leflar's views, see *supra* note 149.

<sup>227</sup> See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)(b); see also *supra* part IV.B.2 (discussing the choice-of-law clauses under the Restatement). There is an additional exception to the application of the parties' choice of law where "the chosen state has no substantial relationship to the parties or the transaction and there is no other reasonable basis for the parties choice." RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187(2)(a). This exception poses no obstacle for Champerco as Champerco is a New Jersey company and its champertous agreements are negotiated and

## 1. Fundamental Policy

When is a policy "fundamental?" The comments to the Restatement say that a fundamental policy is not "likely to be represented by a rule tending to become obsolete."<sup>228</sup> Since champerty laws are "tending to become obsolete,"<sup>229</sup> their underlying policies are most probably not "fundamental." Another "important consideration [to determine whether a state's policy is fundamental] is the extent to which the significant contacts are grouped in [that] state . . . , [and] the extent to which the significant contacts are grouped in the state of the chosen law."<sup>230</sup> The contacts to Champerco's agreements will generally be clustered in New Jersey, including the place of negotiation, the place of contracting, and the place of incorporation and offices of Champerco. The grouping of the contacts, therefore, is a strong indication that the policies underlying the relevant states' champerty laws are not "fundamental." In fact, as discussed above, on a pure contacts-counting basis, New Jersey would generally be the place with the "most significant relationship" to Champerco's agreements.<sup>231</sup> Thus, there is good reason to doubt that any of the relevant states' champerty policies are "fundamental."

## 2. Materially Greater Interest

Regardless of whether or not any of the relevant states' champerty policies are "fundamental" or whether they create true conflicts, those states would not have a "materially greater interest" than New Jersey in the application of their champerty laws to Champerco's agreements. The interest analysis set forth previously yielded only two possible states with an "interest" in the application of their champerty laws: the underlying forum and the defendant state. Neither of these states, however, has a "materially greater interest" than New Jersey.

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executed in New Jersey.

<sup>228</sup> RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 cmt. g.

<sup>229</sup> *Brown v. Bigne*, 28 P. 11, 13 (Or. 1891) ("In some of the states the whole doctrine is regarded as entirely obsolete."); 14 AM. JUR. 2D *Champerty & Maintenance* § 1 (1964) ("In many states [the doctrines of champerty and maintenance] are declared to be obsolete and to have no existence at all.").

<sup>230</sup> RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 cmt. g.

<sup>231</sup> See *supra* part IV.B.1.

Our interest analysis uncovered serious weaknesses in the underlying forum's deterrence interest in the application of its champerty law to Champerco's agreements. Where it is apparent, albeit with hindsight, that the underlying claim was in fact not frivolous and the champertous agreement actually enabled a meritorious claimant to vindicate her claims, the open courts policy underlying champerty laws favors enforcement of the agreement. In fact, the enforcement of such champertous agreements would actually further the underlying forum's policy against frivolous claims by furthering that policy's ultimate purpose of ensuring access to courts for meritorious claimants. Therefore, the underlying forum's interest in the application of its champerty law to invalidate Champerco's agreement is relatively weak.<sup>232</sup>

For the same reasons, the defendant state has only a weak interest in the application of its champerty law. The defendant state has an interest in protecting its residents from frivolous claims only, not from legitimate claims. Thus, the defendant state has an interest in the application of its law only to the extent that invalidating the agreement will further the underlying forum's policy against frivolous claims.

On the other hand, New Jersey's interest in the application of its contract law to enforce Champerco's agreements is relatively strong. New Jersey has an interest in protecting the expectations of a New Jersey corporation when those expectations are based on an agreement made in New Jersey and valid under New Jersey law. Were it not for the fact that such agreements were disapproved by other states, New Jersey's interest in the application of its law to enforce the agreements would be indisputable. Therefore, neither the interest of the underlying forum nor that of the defendant state is "materially greater" than New Jersey's interest.

In conclusion, under the Restatement, Champerco's New Jersey choice-of-law clauses should be enforced, New Jersey law should be applied, and Champerco's champertous agreements should be enforced.

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<sup>232</sup> Its interest is weak even though the underlying forum itself would not conduct a policy analysis and would indiscriminately apply its champerty law.

## F. *The Forum*

### 1. Subjective Interest Analysis

While, objectively, the Restatement's choice-of-law clause analysis, and its built-in interest analysis, dictate the enforcement of Champerco's agreements, the reality is that a forum's interest analysis is likely to be neither correct nor objective.<sup>233</sup> First, interest analysis is complex and confusing. Courts cannot truly be expected to conduct anything more than a superficial interest analysis, and certainly not the thorough analysis of the preceding section.<sup>234</sup> Second, the process of determining and evaluating the policies and purposes of competing laws is too subjective to predict reliably the results courts will reach. When a court is required to weigh another state's policies against its own conflicting policies, it is not difficult to imagine a court failing to give the proper deference and respect to the other state's policies. Furthermore, the malleability of interest analysis makes it vulnerable to result-seeking courts.<sup>235</sup> Champerco cannot rely solely on choice-of-law clauses and the Restatement's interest analysis to constrain courts to reach results they prefer not to reach.<sup>236</sup>

*Koro Co. v. Bristol-Myers Co.*,<sup>237</sup> one of the only champerty choice-of-law cases, is an excellent illustration of the misapplication of interest analysis and the misunderstanding of the competing policies. In *Koro*, the validity of a champertous agreement was at issue. The result turned on whether New York or New Jersey law governed the agreement.<sup>238</sup> The District Court for the District of Columbia began by applying the Restatement's "contacts" analysis to the agreement to determine the center of gravity.<sup>239</sup> Interest-

<sup>233</sup> See SEDLER, *supra* note 148, at 74 ("When the forum would be applying its own invalidating rule in the absence of an express choice, it usually will not recognize that choice, and contrary to the approach of the Restatement Second, it will not consider whether the policy involved in its invalidating rule is 'fundamental' as opposed to being 'strong.'").

<sup>234</sup> See Posnak, *supra* note 174, at 1170 (discussing the difficulty some of the nation's top jurists have had with interest analysis).

<sup>235</sup> See *infra* notes 237-48 and accompanying text.

<sup>236</sup> See SEDLER, *supra* note 148, at 73-74 ("Looking to the results of the decided cases, it is fair to say that in practice an express choice of law usually will *not* be recognized where the matter in issue involves a *strong policy* of the forum or the state whose law the forum would be applying in the absence of an express choice.").

<sup>237</sup> 568 F. Supp. 280 (D.D.C. 1983).

<sup>238</sup> See *id.* at 286.

<sup>239</sup> *Id.*



ingly, this analysis was inappropriate in light of the express New York choice-of-law clause in the agreement.<sup>240</sup> The court then analyzed New York's and New Jersey's competing policies on champerty and weighed their relative interests in the application of their laws to the determination of the validity of the champertous agreement:<sup>241</sup>

Here, New York has a clearly enunciated public policy against champerty, in the form of § 489 of the Judiciary Law, whereas New Jersey has no stated policy against champerty, but it no longer recognizes the doctrine. In such a situation, New York clearly has the stronger interest in the enforcement of its policy. Application of New York law would frustrate no New Jersey policy, whereas application of New Jersey law would certainly impair the purpose underlying the New York statute, namely the prevention of trafficking in litigation claims.<sup>242</sup>

Although the *Koro* court correctly concluded that New York law applied and invalidated the agreement,<sup>243</sup> its interest analysis was entirely superficial and flawed. First, the court made no effort to determine the true nature of the policies underlying New York's champerty statute. The court's recitation of New York's policy of "prevent[ing] trafficking in litigation claims" adds little color to the policies behind New York's champerty statute.<sup>244</sup> Consequently, the court failed properly to consider whether New York really had an "interest" in the application of New York's champerty law, that is, whether it would further the purposes and policies of the law. The *Koro* court made no attempt to explain why the "application of New Jersey law would certainly impair the purpose underlying the

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<sup>240</sup> The court should have applied the "fundamental policy" test of § 187 of the Restatement (Second) of Conflict of Laws. Under § 187, § 188's most significant relationship test only becomes relevant once the court determines that the application of the parties' choice of law would violate the fundamental policy test. It is possible, however, that the court ignored the parties' choice of New York law, since the agreement was clearly champertous and invalid under New York law and the parties obviously did not intend for their agreement to be invalid. See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 cmt. e (1971) ("If the parties have chosen a law that would invalidate the contract, it can be assumed that they did so by mistake.").

<sup>241</sup> This was done under § 6(2)(c) of the Restatement (Second) of Conflict of Laws, made relevant under § 188(2) in evaluating the contacts listed in § 188(2)(a)-(e).

<sup>242</sup> *Koro*, 568 F. Supp. at 286-87.

<sup>243</sup> The agreement contained a New York choice-of-law clause, and the contacts were heavily concentrated in New York. See *id.* at 286.

<sup>244</sup> For a critical analysis of the policy against speculation in litigation, see *supra* part IV.D.1.

New York statute."<sup>245</sup> Second, the court incorrectly assumed that New Jersey's passive stance on champerty somehow meant that New Jersey had no interest in the enforcement of the agreement. The *Koro* court's lack of deference to New Jersey's policies is not surprising, in light of the fact that champerty is illegal in the District of Columbia.<sup>246</sup>

A thorough interest analysis would have revealed that New Jersey did have an interest in the application of its law, and, contrary to the court's holding, New York had no interest in the application of its law. The original plaintiff's business was located in New Jersey, and New Jersey has an interest in the availability of open courts to its residents.<sup>247</sup> New Jersey also had an interest in the enforcement of a contract between two New Jersey businesses. Furthermore, the court's holding, that the application of New Jersey law would frustrate New York's policy of preventing trafficking in litigation claims, is questionable in light of the fact that the litigation was in the District of Columbia.<sup>248</sup> *Koro*, thus, illustrates the misapplication of interest analysis and its susceptibility to subjective application.

## 2. Section 90 and Forum Denials

Even if courts could be expected to apply interest analysis correctly and objectively, Champerco still cannot rely on interest analysis to constrain a court to reach results the court prefers not to reach. The reason is that a court can legally refuse to exercise jurisdiction over an action that is contrary to a strong public policy

<sup>245</sup> *Koro*, 568 F. Supp. at 287.

<sup>246</sup> Indeed the *Koro* court expressly stated that its own policy against champerty was a factor in its decision to apply New York's consonant law. *See id.* In a footnote, the court even hinted that it might have been willing to apply its own law outright had the parties raised such an argument. *See id.* at 287 n.2.

<sup>247</sup> Although the original plaintiff assigned its claim, New Jersey has an interest in the availability of legal redress to injured residents whether through direct prosecution of their claim or through selling the claim or a portion thereof to another.

<sup>248</sup> Assuming that the policy of preventing speculation in litigation is aimed at discouraging frivolous claims that are presumed to arise from trafficking in litigation, only the forum, here the District of Columbia, had an interest in the application of its law against champerty. However, another policy underlying New York's champerty statute, as the *Koro* court recognized in passing, is the prevention of "strife, discord and harassment" (that is, protecting New York residents from frivolous claims). *See Koro*, 568 F. Supp. at 288. If the defendant in *Koro*, Bristol-Myers, was a New York corporation or did business in New York, then New York did have an interest in the application of its champerty statute to protect Bristol-Myers from harassment.

of the forum.<sup>249</sup> Therefore, a forum with a strong public policy against champerty may very well refuse to entertain an enforcement action on a champertous agreement.

In *American Optical Co. v. Curtiss*,<sup>250</sup> the University of Michigan assigned its claim against the defendants to American Optical.<sup>251</sup> The dispute involved the ownership of a patent that was developed by the defendants through their research at the University.<sup>252</sup> The University claimed that the patent was the property of the University.<sup>253</sup> American Optical was interested in using the patent and wanted it to be made public to avoid having to pay any royalties.<sup>254</sup> The University of Michigan wanted to vindicate its rights.<sup>255</sup> The University agreed to assign the claim to American Optical, and American Optical agreed to prosecute the claim and make the patent public if it succeeded.<sup>256</sup> The District Court in New York held that, even though Michigan law governed the agreement,<sup>257</sup> the agreement was contrary to New York's public policy against champerty.<sup>258</sup> The court, therefore, refused to entertain the lawsuit.<sup>259</sup>

In *Kracht v. Perrin, Gartland & Doyle*,<sup>260</sup> the plaintiff brought an action on a legal malpractice claim that was assigned to him by

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<sup>249</sup> See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 90 (1971) ("No action will be entertained on a foreign cause of action the enforcement of which is contrary to the strong public policy of the forum.").

<sup>250</sup> 56 F.R.D. 26 (S.D.N.Y. 1971).

<sup>251</sup> See *id.* at 28.

<sup>252</sup> See *id.* at 27.

<sup>253</sup> See *id.* at 28.

<sup>254</sup> See *id.*

<sup>255</sup> See *id.*

<sup>256</sup> See *id.*

<sup>257</sup> It is worth noting that the court was of the opinion that, under Michigan law, the contract may have been void for champerty. See *id.* at 30 n.6 (referring to 15 MICH. STAT. ANN. § 21.311 (West 1994) and MICH. COMP. LAWS ANN. § 450.681 (West 1990 & Supp. 1995) (prohibiting the practice of law by corporations)).

<sup>258</sup> See *American Optical*, 56 F.R.D. at 29-30.

<sup>259</sup> The court gave American Optical the opportunity to have the suit reinstated if it joined or substituted the University as a party-plaintiff. See *id.* at 32. The University was later added as a party, but doing so destroyed diversity jurisdiction. See *American Optical Co. v. Curtiss*, 59 F.R.D. 644, 646 (S.D.N.Y. 1973). American Optical released one of the defendants to restore diversity, but the court held that the released defendant was an indispensable party and dismissed the suit for failure to join an indispensable party. See *id.* at 651 ("It seems self-evident that a decree of cancellation of an agreement will inevitably affect all parties to such an agreement and, therefore, all parties should be present.").

<sup>260</sup> 219 Cal. App. 3d 1019 (Ct. App. 1990).

operation of law.<sup>261</sup> The defendant argued that California law applied, under which legal malpractice claims are unassignable.<sup>262</sup> The plaintiff argued that Oregon law applied, under which the assignment was legal.<sup>263</sup> The California Court of Appeal held that, even if Oregon law governed the assignment, California courts would not entertain such a lawsuit, since the assignment of a legal malpractice claim violated California public policy.<sup>264</sup>

Section 90 of the Restatement recognizes a forum's interest in refusing to accommodate lawsuits that are contrary to a strong public policy of the forum.<sup>265</sup> The comment to section 90 states that the rule has a narrow application: "Actions should rarely be dismissed because of the rule of this Section."<sup>266</sup> *American Optical* and *Kracht* demonstrate, however, that a forum's public policy against champerty<sup>267</sup> may be sufficient to motivate a court to refuse to entertain a lawsuit tainted with champerty.

To ensure the enforceability of its champertous agreements, and thus the viability of investing in litigation, Champerco must ensure the availability of a favorable forum that will entertain enforcement actions on its champertous agreements. Champerco must also ensure that the forum will apply the Restatement's choice-of-law interest analysis in a favorable manner and/or apply New Jersey law.

### G. Forum Selection Clauses

To ensure the availability of a favorable forum, Champerco can include a New Jersey forum-selection clause in its champertous agreements.<sup>268</sup> The forum-selection clause should designate New Jersey as the sole and exclusive forum for any litigation arising

<sup>261</sup> See *id.* at 1021.

<sup>262</sup> See *id.* at 1023-26.

<sup>263</sup> See *id.* at 1026.

<sup>264</sup> See *id.* at 1027-28.

<sup>265</sup> See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 90 (1971).

<sup>266</sup> *Id.* § 90 cmt. c.

<sup>267</sup> Although the public policy in *Kracht* was the more specific policy against the assignment of legal malpractice claims, the court cited champerty as one of the bases underlying the law. See *Kracht*, 219 Cal. App. 3d at 1023-24 (noting that "assignability would encourage commercialization of claims" which, in turn, would "promote champerty").

<sup>268</sup> See SEDLER, *supra* note 148, at 71-72 ("The lawyer can maximize the likelihood of the express choice of law clause being recognized by including a forum selection clause. . . . When the suit is brought in the state whose law is chosen in the governing instrument, the likelihood of recognition of the express choice of law clause is thereby increased.").

from the champertous agreement. This serves dual purposes. First, it gives New Jersey courts jurisdiction over any enforcement action by Champerco. New Jersey courts will exercise jurisdiction on the basis of the forum-selection clause,<sup>269</sup> follow the New Jersey choice-of-law clause,<sup>270</sup> apply New Jersey law, and enforce the agreement. Second, the forum-selection clause prevents the plaintiff from bringing an action to rescind the champertous agreement in another state that, perhaps, will not follow the New Jersey choice-of-law clause.<sup>271</sup> Even if the plaintiff defaults in Champerco's New Jersey enforcement action, the default judgment will be given full faith and credit in all other states, even though those states would not entertain the action or enforce the champertous agreement.<sup>272</sup>

#### H. *The Total Solution*

The total solution, then, to investing in litigation without running afoul of champerty laws is to execute the champertous agreements in New Jersey, include New Jersey choice-of-law and forum-selection clauses in the agreement, and bring the underlying champertous lawsuit in the real plaintiff's name. If these three steps are taken, investing in litigation is possible and practicable in any state. Champerty will likely pose no obstacle in the underlying lawsuit, since the plaintiff's standing will not be predicated on a champertous agreement, and investors are ensured of a means of enforcing their agreements against breaching plaintiffs.

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<sup>269</sup> See *National Micrographic Sys. v. Canon U.S.A.*, 825 F. Supp. 671, 677 (D.N.J. 1993) (“[F]orum selection clauses do not offend the public polic[y] of . . . New Jersey.”); *Wilfred MacDonald, Inc. v. Cushman, Inc.*, 606 A.2d 407, 409 (N.J. Super. Ct. 1992) (“Forum selection provisions have long been enforced in New Jersey.”).

<sup>270</sup> See *Turner v. Aldens*, 433 A.2d 439, 441 (N.J. Super. Ct. App. Div. 1981) (“It is well settled that the law of the state chosen by the parties will be honored so long as that choice does not contravene a fundamental policy of New Jersey.”). *But see* *Winer Motors, Inc. v. Jaguar Rover Triumph, Inc.*, 506 A.2d 817, 821 (N.J. Super. Ct. App. Div. 1986) (applying Connecticut law to a franchise agreement and refusing to recognize an express New Jersey choice-of-law clause).

<sup>271</sup> See *SEDLER*, *supra* note 148, at 71-72 (“[W]here there is a forum selection clause and the suit is brought in another forum, that court will often recognize the forum selection clause and decline to exercise jurisdiction.”).

<sup>272</sup> See U.S. CONST. art. IV, § 1, cl. 1 (“Full Faith and Credit shall be given in each State to the public Acts, Records, and judicial Proceedings of every other State.”).

## CONCLUSION

A plaintiff's risk-bearing ability effects a plaintiff's decision whether or not to pursue a claim and the amount for which a plaintiff is willing to settle. This creates the opportunity for the trade of claims from poorer risk-bearers, who place a low value on a claim, to better risk-bearers, who place a higher value on a claim. Trade of claims to better risk-bearing parties also eliminates two important strategic bargaining problems,<sup>273</sup> thereby encouraging settlement and increasing settlement amounts. These theoretical gains of trade suggest the existence of a market for investing in litigation.

Investing in litigation, however, violates the letter and spirit of the law against champerty, whether in force by statute, by common law, or as a general rule of public policy. Champertous agreements are, therefore, generally unenforceable in almost every jurisdiction, except New Jersey. An investor may avoid the dismissal of her claim by bringing suit in the plaintiff-assignor's name, whose standing is not predicated upon a champertous agreement. The proceeds of any judgment or settlement, however, will be paid to the plaintiff-assignor who is the named-plaintiff. The investor, therefore, is at risk that after a substantial recovery the plaintiff-assignor will repudiate her agreement with the investor, and the agreement will be unenforceable because of champerty.

Investors, nevertheless, can safely invest in litigation with the security of an enforceable agreement by contracting around champerty laws. This can be accomplished by providing New Jersey choice-of-law and forum-selection clauses in a champertous agreement and by negotiating and executing the agreement in New Jersey. Champertous agreements are valid and enforceable under New Jersey law. Where the agreement is executed in New Jersey, New Jersey courts will enforce a New Jersey choice-of-law clause. Under choice-of-law principles, the policies underlying all the relevant states' champerty laws—generally, the policy against frivolous claims—do not generate a materially greater interest than New Jersey in the application of those states' champerty laws. Applying New Jersey law, New Jersey courts will enforce the investors' agreements. The forum-selection clause will ensure that New Jersey has jurisdiction to enforce the agreement and that no

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<sup>273</sup> The two strategic bargaining problems, threat credibility and bilateral monopolies, are explained in detail in part I.B.

other jurisdictions will entertain an action to rescind the agreement. Investors are therefore ensured of a means of enforcing their champertous agreements, and litigation investment companies are legally and practically viable.

