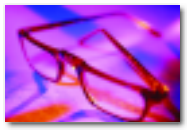

Borrowing To Finance a Lawsuit

Going to court is sure getting expensive.

With some types of litigation now requiring cash outlays of six figures for experts, deposition costs, computer graphics and the like, both clients and the lawyers representing them are frequently having to borrow the funds necessary to get to the courthouse.

There is nothing unusual about clients borrowing money from banks or relatives in order to pay for attorneys' fees and litigation expenses. And most lawyers have lines of credit and other banking sources to meet the expenses they incur on behalf of clients until they are reimbursed. An Arizona ethics opinion[1] even allows a lawyer to pass on interest and carrying costs to the client for loans the lawyer takes out to cover court costs and expenses of litigation.

But what happens when traditional sources are not available?

Lawsuit lending is becoming a big business. Many of these services make non-recourse high-interest loans to litigants secured by the assignment of their claims. In cases involving personal injuries, these claims are usually tort claims and are not assignable in Arizona.[2] Other kinds of claims, such as breach of contract cases, can be assigned, and may serve as security for the litigation loan. But there are some aspects of lawsuit loans that involve ethical considerations.

New Ethics Opinions are on p. 51.

Opinions and the Rules of Professional Conduct are available at www.myazbar.org/Ethics

Take the situation in which the lawyer deals directly with the client.

First, the client in effect "borrows" money from the lawyer when the lawyer agrees to wait until the end of the case to collect all of the unpaid portion of his fee. There is certainly nothing unethical about that. And if the client wins, the lawyer is "secured" because of his charging lien on the resulting judgment.[3] But if the lawyer wants to be secured in the event the client's case is not successful, or the judgment is not enough to pay the lawyer what is owed, how does the lawyer secure the "debt"?

In a recent Arizona case, it was held that the lawyer could take an assignment of a contract right held by the client to secure payment of the lawyer's fees, but only for an amount equal to the unpaid fees and no more.[4] This would also apply to other non-tort claim assets of the client, such as a deed of trust on real property or a security interest in marketable securities. The *Skarecky* case did not mention this, but lawyers should proceed on the assumption that any such agreement with a client will be considered a business transaction subject to the requirements of ER 1.8(a)[5]. For example:

1. the terms of the arrangement must be reasonable, fair to the client and fully disclosed to the client in a manner the client can understand;
2. the client must be advised in writing of the advisability of seeking the advice of independent counsel; and
3. the client must give "informed consent,"[6] in a writing signed by the client, to the transaction's essential terms and the lawyer's role in the arrangement, including whether the lawyer is representing the client in the transaction.

Other than securing unpaid amounts owing to you as the lawyer, you are otherwise prohibited from lending money to a client in connection with pending or contemplated litigation except for advances of court costs and expenses of litigation.[7]

It is not ethically improper to assist your client in obtaining a loan from a lawsuit lender.[8] There are rules, however.

First, as the lawyer, you cannot have an interest in the lawsuit lender that would affect your independent judgment on behalf of your client.[9] If your interest in making sure the loan is repaid is greater than your interest in diligently representing your client, then you have a "concurrent conflict of interest.[10] The same problem would occur if you as the lawyer co-signed or guaranteed a loan provided by a lawsuit lender.[11]

Second, in assisting your client in obtaining a lawsuit loan, do not violate any client confidences relating to the representation unless you get the client's consent to do so.[12] The lawsuit lender's records may be subject to discovery, and there may be information concerning the representation you might give to a lender that you would not want other people to see.

Third, there is an ethical obligation on all lawyers to disclose material facts to third parties, such as a lawsuit lender, when disclosure is necessary to avoid assisting a fraudulent act by a client.[13] If the lawsuit lender requires your client to assign his tort personal injury claim to secure the loan, you may not misrepresent or imply to the lender that the assignment is valid. Avoid a claim by the lawsuit lender that it was induced, based on erroneous beliefs it formed from something you said or did not say, to forego obtaining some other effective form of security from the client.[14] It is also unethical for the lawyer to agree to repay the loan in whole or in part from his fee: That has been held to be "fee-splitting" prohibited under the ethics rules.[15] Finally, the terms of any loan may not affect the lawyer–client relationship, such as a prohibition against the client discharging the lawyer.[16]

— ENDNOTES on p. 59

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endnotes

1. Ariz. Ethics Op. 01-07 (September 2001).
2. *Allstate Insurance Co. v. Druke,* 576 P.2d 489 (Ariz. 1978).
3. *See* David. D. Dodge, *Enforcing Your Right to Get Paid: Ethics, Lien Rights and Retainers,* ARIZ. ATT'Y, Oct. 2005, at 26.
4. *Skarecky & Hornstein, P.A. v. 3605 North 36th Street Co.*, 825 P.2d 949 (Ariz. 1992).
5. Rule 42, ARIZ.R.S.CT.
6. This is a defined term and means the agreement by a person to a proposed course of conduct after the lawyer has communicated adequate information and explanation about the material risks of and reasonably available alternatives to the proposed course of conduct. ER 1.0(e).
7. ER 1.8(e).
8. Ariz. Ethics Op. 91-22 (Sept. 30, 1991).
9. *Id*. at 2.
10. ER 1.7(a)(2) prohibits the representation of a client if there is a significant risk that the lawyer's responsibilities to a third person or a personal interest of the lawyer will materially limit the lawyer's ability to represent the client.
11. Ariz. Ethics Op. 91-22, *supra* note 9, at 3; Ariz. Ethics Op. 9119 (June 17, 1991).
12. ER 1.6 (Confidentiality of Information).
13. ER 4.1 (Truthfulness in Statements to Others); Ariz. Ethics Op. 91-22, *supra* note 9, at 3.
14. *Id*. at 3, *citing* Ariz. Ethics Op. 8802 (Jan. 11, 1988).
15. ER 5.4(a); Utah Bar Ass'n Op. 9711 (1997).
16. ER 5.4(c) (a lawyer shall not permit a person who recommends, employs, or pay the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal service); Mich. State Bar Op. RI 321 (2000) (agreement between lender and plaintiff so onerous it created irreconcilable conflicts of interest between lawyer and his client).