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April 29, 2010

[REDACTED]  
Phoenix, Arizona 85014

RE: Pre-settlement Lender Licensing

Dear Ms. [REDACTED]:

By e-mail, dated April 19, 2010, to Jodie Robertson, a Financial Credit Examiner in the office of the Administrator, Uniform Consumer Credit Code, you asked, on behalf of an unidentified client, for "an opinion from [this] office whether a pre-settlement lender needs to obtain any special license or registration to engage in that business in the State of Colorado and what those licensing or registration requirements are, if any." Ms. Robertson referred your e-mail to the Administrator, who in turn referred the matter to me for response. I now respond on the Administrator's behalf.

The Administrator concludes that a lender who engages in such transactions, variously called "litigation", "lawsuit", or "legal" "funding", "financing", or "advances", with Colorado consumers must comply fully with Colorado's Uniform Consumer Credit Code, §§ 5-1-101, et seq., C.R.S. 2009 (Code), including licensure.

**Facts**

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Your e-mail states that your client would be

making non-recourse, pre-settlement loans in the State of Colorado. Basically, my client makes an advance to individuals involved in pending litigation based upon its evaluation of the likely settlement amount of the case. If the case does settle, then the advance must be repaid with interest. If the case does not settle and results in a defense

verdict or judgment, then the entire advance or loan is forgiven.

Although sparse, the facts you provide sufficiently explain the nature of your client's business and the transactions it would engage in with Colorado consumers. The Administrator is aware of the business of "pre-settlement", or "litigation", funding. There also apparently is a national trade association - the American Legal Finance Association (ALFA) - that purports to represent this industry and whose website, [www.americanlegalfin.com](http://www.americanlegalfin.com), further explains this business. Accordingly, and despite some factual gaps, the Administrator provides the following analysis and conclusions.

### Analysis

Whether your client's business falls within and requires licensure under the Code requires answers to three questions: (1) are these transactions "loans"; (2) if so, are they "consumer loans"; and (3) are they then "supervised loans"? I discuss these in turn.

The answer to the first question is simple. As you recognize in your e-mail, your client is a "lender" that makes "loans." The Administrator agrees and so interprets the Code.

Any doubt about this question was answered by the Colorado Supreme Court in State ex rel. Salazar v. Cash Now Store, Inc., 31 P.3d 161 (Colo. 2001). There, the Court held that under the Code "a loan is made when a creditor creates debt by advancing money to the debtor." Id. at 166. Here, your client advances money to the consumer. Thus, it makes loans.

Although the loan may be non-recourse, nowhere does the Code or Cash Now require the borrower's personal recourse for an advance to be a loan. Rather, your client's transactions are garden variety, non-recourse secured loans, with the consumer's lawsuit (or its proceeds) as security. The lender looks to this collateral - e.g., the settlement or judgment - for repayment.

Non-recourse secured loans are commonplace. The pawn transaction is one example. Despite the lack of personal recourse, pawns are considered loans. See, e.g., Burnett v. Ala Moana Pawn Shop, 3 F.3d 1261 (9th Cir. 1993); Wiley v. Earl's Pawn & Jewelry, Inc., 950 F.Supp. 1108 (S.D. Ala. 1997).<sup>1</sup>

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<sup>1</sup> ALFA's website makes much of the fact that litigation advances

Further, at least one court has held litigation funding advances were loans. See Rancman v. Interim Settlement Funding Corp., 2001 WL 1339487, \*\*2-3 (Ohio Ct. App. 2001), aff'd, 789 N.E.2d 217 (Ohio 2003).<sup>2</sup>

This brings us to the second question, whether the loans are "consumer loans." Under the Code, a "consumer loan" requires that: (1) the consumer must be a natural person or individual; (2) the debt must be incurred for personal, family, or household purposes; (3) either a loan finance charge is made or the debt is payable in installments; and (4) the principal must not exceed \$75,000.00. See Code § 5-1-301(15)(a).

Based on the facts you provide, it appears element 1 is met. As you say, your client makes advances to "individuals." Element 3 also appears satisfied; you state that, if the consumer's suit settles, the advance is repaid "with interest."

Your facts do not enable me to determine whether elements 2 and 4 are met. Nevertheless, I think it safe to assume that the consumer's debt is incurred "for personal, family, or household purposes." As ALFA's website maintains, "legal funding can provide immediate relief from the mounting burden of accumulating bills, potential eviction or loan foreclosure, and can provide for daily living expenses for the client and their [sic] family." www.americanlegalfin.com, visited April 28, 2010; see id. AboutLegalFunding.asp (litigation advances allow consumers to pay child support, medical bills, and the like).

I similarly assume that many, if not all, of your client's advances do not exceed \$75,000.00. Those transactions that do not exceed this cap (or are secured by an interest in land) are "consumer loans" subject to the Code.

Finally, whether your client must be licensed depends on whether its consumer loans are "supervised loans." See Code § 5-2-301. A "supervised loan" is a consumer loan whose annual percentage rate (APR) exceeds 12%. See Code § 5-1-301(47).

The facts you provide are insufficient to determine your client's loans' APRs. If they exceed 12% - and my guess is they

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are non-recourse. See www.americanlegalfin.com/faq.asp, visited April 28, 2010. Whatever may be this fact's import elsewhere, it is of no moment under Colorado law.

<sup>2</sup> Interestingly, the Ohio Supreme Court voided the transactions based on "champerty and maintenance." 789 N.E.2d at 219.

likely do, see, e.g., Rancman, 2001 WL 1339487, \*1 (litigation advances there had interest rates exceeding 100%)<sup>3</sup> - then your client must be licensed before it can make loans in Colorado.

In sum, based on the limited facts you provide, it is likely that your client would need to be a licensed, supervised lender and otherwise comply with the Code in order to engage in its business in Colorado with Colorado consumers.

Please be advised that this letter is not, nor may be construed as, an interpretation or response of the Administrator pursuant to Code § 5-6-104(4) so as to provide your client "safe harbor." However, it does express the Administrator's interpretation of the Code and enforcement policy regarding "litigation funding" and similar transactions.

Thank you for your attention to this matter. If you have any questions, please do not hesitate to call.

Sincerely yours,

FOR THE ATTORNEY GENERAL



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<sup>3</sup> Generally, the Code prohibits APRs exceeding 36%. See Code § 5-2-201; see also § 18-15-104(1), C.R.S. 2009 (APRs exceeding 45% are criminally usurious).