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CHARTING LITIGATION FINANCING IN MINNESOTA

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Litigation financing is having a moment. Increasing in popularity, litigation financing (also known as champerty) allows third parties to provide funding to the plaintiffs in exchange for a portion of the financial recovery from the lawsuit. While proponents of litigation financing argue that it increases access to justice and decisions on the merits for those with limited financial resources to pursue costly litigation, such funding is not without its concerns.

Champerty was prohibited under Minnesota law until June 2020 when, in the case *Maslowski v. Prospect Funding Partners LLC*, the Minnesota Supreme Court abolished the state's long-standing prohibition. 944 N.W.2d 235 (Minn. 2020). In that case, Ms. Maslowski sought litigation financing services from Prospect Funding Partners LLC to help fund her living expenses while her personal injury matter remained pending; in exchange, she agreed to turn over a portion of her settlement or judgment proceeds to Prospect Funding Partners. *Maslowsk*i, 944 N.W.2d at 236. However, upon settlement, Ms. Maslowski refused to pay the agreed-upon amount, arguing that the litigation financing agreement was unenforceable due to Minnesota's prohibition against champerty. *Id.* at 237. Noting shifts in societal and market attitudes towards litigation financing, as well as developments in the rules of civil procedure and professional responsibility which address "the abuses of the legal process that necessitated the common-law prohibition," the Court overturned the prohibition, and thus opened the door to third-party litigation financing in Minnesota. *Id.* at 238–39.

While it is now legal, litigation financing is not limitless. In issuing its opinion, the Minnesota Supreme Court expressed its concerns about "uncounseled" financing agreements and attempts by litigation financiers to "control the course of the underlying litigation"—a particular concern that necessitated the original prohibition against champerty. *Id.* at 241. A critical eye towards litigation financing agreements, therefore, is warranted.

The case was then remanded to the district court for an enforceability determination. On appeal, the Minnesota Court of Appeals affirmed the findings of the district court that parts of the agreement—namely, the liquidated damages provisions, the penalty clauses, and the interest rate provision—were unenforceable, unconscionable, and usurious, respectively. *Maslwoski v. Prospect Funding Partners LLC*, 978 N.W.2d 447, 454–59 (Minn. Ct. App. 2022).

Notably, the Court found that the penalty clauses in the financing agreement impeded Maslowski's relationship with her attorneys and her ability to control her lawsuit. *Id.* at 457. The penalty clauses maintain certain requirements, such written notice of Maslowski's intent to hire new counsel, a requirement that the new counsel execute the acknowledgements of the financing agreement, and reasonable efforts by Maslowski "not to enter into any settlement agreement or covenant" that would restrict Prospect Funding's rights to information relating to lawsuit proceeds, all at the risk of financial penalty. *Id.*

The court found that such penalties were unconscionable, as they could have induced Maslowski to remain with an unsatisfactory attorney or to select an attorney based on Prospect Funding's preferences, all of which restricted "the freedom of [Maslowski] to select counsel of [her] choice" and to control her lawsuit. *Id.* The Court also agreed with the district court that the 60% annual repurchase rate of the financing agreement was usurious and in violation of Minnesota Statue § 334.01. *Id.* at 458. Maslowski's "absolute obligation" to pay this interest if she recovered financially in the lawsuit, coupled with the restrictive nature of the agreement, resulted in an agreement that was "designed to compel Maslowski to bring her underlying legal claim to financial resolution, which results in Prospect receiving excessive interest." *Id.*

While these recent opinions have helped establish safeguards against exploitation through litigation financing, they also demonstrate that great care should be taken when reviewing a litigation financing agreement. Agreements should be written such that the client maintains the ability to control their lawsuit; the financing arrangement should not be the source of pressure on a client to pursue a trial over other avenues, such as settlement. Agreements should also plainly spell out the terms of the funding, including the source of the funds and any repayment terms, so as to avoid any future confusion or unexpected liability.

Ultimately, litigation financing can be a powerful tool that provides access to justice to individuals and companies lacking the financial resources to maintain a lawsuit. However, Minnesota's recent court decisions on the subject highlight how easily litigation financing may go from resourceful to exploitative. Thus, it is important that all parties—lawyers, clients, and financiers—are on the same page before proceeding with such an agreement.

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