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**RE: Administrative Interpretation: Legal/ Litigation Funding Transactions
Administrative Interpretation 3.104,106-1403**

In recent months, the question has arisen as to whether a legal funding transaction constitutes a "loan" under the South Carolina Consumer Protection Code ("the Code"), S.C. Code Ann. § 37-1-101 *et seq.*¹ The Department concludes that such transactions, also referred to as "third-party litigation financing," "lawsuit lending," "pre-settlement funding," "litigation funding," and "non-recourse cash advances," meet the definition of a loan; thus, a lender who engages in the offering or provision of such activities must comply with the Code.

Adopted in 1974, the Code governs the regulation of consumer credit transactions and sets forth general creditor and consumer rights and responsibilities including, disclosures, maximum charges, and licensing. *See* § 37-1-101 *et seq.*, specifically § 37-3-301; § 37-3-305; § 37-3-502. Pursuant to section 37-1-301(11), a consumer credit transaction includes a consumer loan. A "consumer loan" is defined as:

a loan made by a person regularly engaged in the business of making loans in which:

- (a) the debtor is a person other than an organization;
- (b) the debt is incurred primarily for a personal, family, or household purpose;
- (c) either the debt is payable in installments or a loan finance charge is made; and
- (d) either the principal does not exceed twenty-five dollars (ninety thousand as adjusted) or the debt is secured by an interest in land.

See § 37-3-104; § 37-1-109.

The Code defines a loan as including, among other activities, "The creation of debt by the lender's payment of or agreement to pay money to the debtor or to a third party for the account of the debtor;" and "The forbearance of debt arising from a loan." *See* § 37-3-106(1) & (4). While "debtor" is defined as an obligor in a credit transaction, "debt" is not a defined term. *See* § 37-1-301(14). The Official Comments to the 1968 Uniform Consumer Credit Code ("UCCC"),

¹ Further reference to the South Carolina Code of Laws will be by Code section only.

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however, state that a loan is created when the “creditor creates debt by advancing money to the debtor.” Unif. Consumer Credit Code § 3.106, 7 U.L.A. 612 (1997) Section 37-3-109(a) defines a loan finance charge, in pertinent part, as:

the sum of all charges *payable directly or indirectly* by the debtor and *imposed directly or indirectly by the lender* as an incident to the extension of credit, including any of the following types of charges which are applicable: interest or any amount payable under a point, discount or other system of charges, however denominated...

Emphasis added.

When interpreting statutory provisions, the words of a statute must be given their plain meaning and consistently construed within the parameters of the statute’s purpose and subject. Ga. Carolina Bail Bonds, Inc. v. City of Aiken, 354 S.C. 18, 23, 579 S.E.2d 334, 336 (Ct. App. 2003). Statutes must be read as a whole and sections which are part of the same general statutory scheme must be construed together and each given effect, if it can be done by any reasonable construction. Higgins v. State, 307 S.C. 446, 415 S.E.2d 799 (1992). Further, the statutory provisions of the Code shall be liberally construed and applied to promote the Title’s underlying purposes and policies, which include to protect consumers and make uniform the law amongst various jurisdictions. See § 37-1-102(1); § 37-1-102(2)(d), (g), (e); Davis v. NationsCredit Financial Services Corporation, 326 S.C. 83, 86, 484 S.E.2d 471, 472 (1997); Camp v. Springs Mortgage Corp., 310 S.C. 514, 516, 426 S.E.2d 304, 305 (1993).

Generally, a litigation funding product involves the advancement of funds to a plaintiff in a civil action for the purpose of paying living expenses by someone who is not a party or who does not otherwise have a role in the lawsuit. See Oasis Legal Fin. Group, LLC v. Suthers, 2013 COA 82, P2 (Colo. App. 2013); American Legal Finance Association, <http://www.americanlegalfin.com> (last accessed October 28, 2014). The contract delineates a sum certain due pursuant to a delineated schedule after a settlement or court award and net litigation proceeds are paid. *Id.* Some payment schedules include an increased amount due over time while others impose a monthly use fee in addition to the initial amount funded. *Id.*; Odell v. Legal Bucks, 665 S.E.2d 767, 770-771 (N.C. App. 2008), *review denied* 676 S.E.2d 905 (N.C. 2009); Fausone v. U.S. Claims, Inc., 915 So.2d 626, 627 (Fla.App.2005). Interest rates in these transactions can reach the triple digits. See Odell, 665 S.E.2d at 770-771 (Interest rate capped at 325% of loan amount); Fausone, 915 So.2d at 627 (Interest rate imposed exceeded 200%). If the consumer receives less than the amount owed, the full amount received is due to the litigation funder, while no monies are required to be paid if the consumer fails to collect any funds. See Oasis, 2013 COA at P3 (Colo. App. 2013); Odell, 665 S.E.2d at 770-771.

The argument of a person engaging in the buying of future assets as opposed to making loans is not a novel one in South Carolina. In Martin v. Pacific Mills, the South Carolina Supreme Court found the practice of advancing funds to workers in exchange for a portion of their unearned wages amounted to a loan, as opposed to a “bill of sale” as argued by the plaintiff. Martin v. Pacific Mills, 160 S.C. 458, 158 S.E. 831 (1931). As the Court said, “the scheme of

the plaintiff was cunningly devised, but thinly veiled, to make what was plainly a loan a bill of sale—an attempted evasion of the usury law.” 160 S.C. at 462, 158 S.E. at 832. *See also* Rainwater v. Boyette, 151 S.C. 474, 149 S.E. 254 (1929) (Holding that a Court will look beyond the purported form of a transaction to its substance in determining whether a transaction was employed to evade usury laws).

Given the plain language of the Code and necessity to interpret its provisions liberally to further the protection of consumers, transactions similar to litigation funding have also more recently been determined to constitute loans pursuant to the Code. The absence of an unconditional obligation to repay an advance of funds has not dissuaded South Carolina courts and the Department in ruling a transaction is a loan either.

Prior to the implementation of a full exemption from the Code, the Department interpreted its provisions as covering pawn transactions, transactions in which the consumer is not “unconditionally obligated” to repay the loan/ redeem the pawn. § 37-1-202(4); Administrative Interpretation No. 1.202-8108 (September 8, 1981); *see also* Unif. Consumer Credit Code § 1.202(4), 7 U.L.A. 511 (1997). The Department also has taken the position that tax refund discounting, better known as refund anticipation loans, is subject to the Code. In Income Tax Buyers v. Hamm, the court agreed with the Department in holding that such transactions are not sales, but rather loans. Income Tax Buyers v. Hamm, No. 91-CP-40-3193 (S.C. Cir. Ct., Jan. 14, 1992). The transaction at issue in Hamm was structured in a manner where the consumer if, and only if, the tax refund was not received from the government within a specified time period, would be obligated to pay what was borrowed. *Id.* at 3. Viewing the true substance of the transaction as opposed to the form, the court stated the absence of such an obligation by the consumer would not have convinced the judge to rule otherwise. *Id.* at 3-4; *see also* State ex rel. Salazar v. Cash Now Store, Inc., 31 P.3d 161 (Colo. 2001) (Colorado Supreme Court adopted the Hamm reasoning in holding a similar tax refund advancement was a loan as opposed to a sale and assignment).

While South Carolina case law and administrative interpretations indicate litigation funding is a loan product subject to the Code, prior to issuing interpretations and rulings, the Department is directed to additionally assess and take into consideration those of other Uniform Consumer Credit Code States. *See* §§ 37-6-104(3)(a), (b)(ii); 37-1-102(e). Colorado, Indiana, Idaho, Iowa, Kansas, Maine, Oklahoma, Utah, Wisconsin and Wyoming administer and enforce versions of the UCCC. In July 2009, the Kansas Office of the State Bank Commissioner issued a letter confirming its position that “plaintiff agreements” constitute loans under the Kansas UCCC. In Re Cambridge Mgmt. Group (Kan. Office of State Bank Comm’r July 7, 2009). The Office based its decision on a 2006 Kansas Supreme Court decision pertaining to the definition of a consumer loan and the broad definition thereof, recognizing that a debt is created through the advancement of funds prior to a resolution being realized and the lack of a statutory requirement of an absolute obligation to repay the funds. *Id.*; Decision Point, Inc. v. Reece & Nichols Realtors, Inc., 282 Kan. 381, 144 P.3d 706 (Kan. 2006). Colorado arrived at a similar conclusion, stating that litigation advances meet the definition of a “loan” and “consumer loan” pursuant to Colorado law. In Re Pre-Settlement Lender Licensing (Colo. Att’y Gen. April 29, 2010). The informal interpretation rejects the argument that the loan being purportedly non-recourse removes it from the purview of the Colorado UCCC and cites similar non-recourse

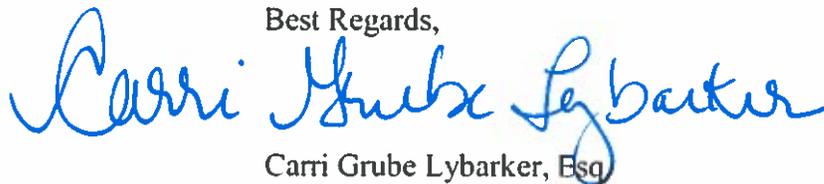
loans, such as pawn transactions. *Id.* The Colorado Attorney General has also prevailed on this argument in District Court and the Colorado Court of Appeals. Oasis Legal Fin. Group, LLC v. Suthers, 2013 COA 82 (Colo. App. 2013). A Supreme Court ruling on the matter is pending.

Maine and Oklahoma have addressed litigation funding in a different manner. Both Legislatures passed industry specific regulatory statutes. Maine's "An Act to Regulate Pre-settlement Lawsuit Funding" took effect January 1, 2008. 9-A MRSA §§ 12-101 to 12-107. This law specifically excludes legal funding from the definition of a consumer credit transaction. 9-A MRSA § 12-103(2). Oklahoma implemented an industry specific licensing statute within its UCCC in 2013. O.S. §§ 14A-3-801 to -817. As South Carolina law does not have a similar statutory scheme, the Department does not find such implementations of assistance in our review.

Taking all of the above into account, the Department concludes that a litigation funding transaction meets the definition of a loan as monies are given to the consumer. The broad concept of a "loan" under the UCCC certainly encompasses those circumstances where the consumer does not have an unconditional obligation to repay. The potential for non-payment in a litigation loan transaction is similar to a pawn transaction - the goods pawned may not have the value anticipated, thus the lender would not receive payment (whether full or at all), nor is there an alternate means to collect. Refund anticipation loans place the lender in a like position whereby conditions are placed on the consumers obligation- payment is only required under specified circumstances. Based on the information reviewed, the loans also meet the definition of "consumer loan." The persons engaging in lending do so on a regular basis; the debtors are consumers using the funds for medical expenses, to avoid foreclosure or other personal, family or household purposes; a finance charge is imposed either in the form of an interest charge or other additional amounts added to the initial sum advanced; and the monies given to the consumer do not exceed \$90,000.

Therefore, persons engaged in activities described herein shall comply with all applicable provisions of the Code. Pursuant to sections 37-6-104(4) and 37-6-506(3), reliance upon an administrative interpretation provides protection from any penalties authorized by the Code even if the administrative interpretation is subsequently declared invalid by a court or is rescinded. Please do not hesitate to contact the Department should you need any further information.

Best Regards,



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