

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

RD LEGAL FUNDING, LLC,

Plaintiff,

v.

CONSUMER FINANCIAL PROTECTION
BUREAU; DOES 1-10, inclusive,

Defendants.

Case No. 1:17-cv-00010

COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF

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LLC

Plaintiff RD Legal Funding, LLC (“RDLF”), for its complaint against the Consumer Financial Protection Bureau (the “CFPB” or “Bureau”) respectfully alleges as follows:

PRELIMINARY STATEMENT

1. RDLF brings this action for declaratory and injunctive relief against the CFPB because: (a) the agency’s investigation of RDLF exceeds the scope of its regulatory authority under the Consumer Finance Protection Act (the “CFP Act”) and the Truth in Lending Act (“TILA”); and (b) the agency has violated RDLF’s First Amendment rights by retaliating against RDLF for challenging the agency’s jurisdiction.

2. The CFPB was formed in the aftermath of the financial crisis for the laudable purpose of protecting everyday American borrowers from predatory lenders and unscrupulous creditors.

3. Although the Bureau’s authority over economic matters is broad, it is not unlimited. The CFP Act only regulates “covered person[s] or service provider[s]” who are engaged in “unfair, deceptive, or abusive act[s] or practice[s] under Federal law.” 12 U.S.C. §§ 5531(a), 5536(a). A “covered person” is defined as “any person that engages in offering or providing a consumer financial product or service.” 12 U.S.C. § 5481(6)(A). As pertinent here, a “financial product or service” is defined to include, *inter alia*, extending credit and servicing loans. 12 U.S.C. § 5481(15)(A)(i)-(x).

4. The Bureau also has jurisdiction over violations of TILA and its implementing regulations. TILA and Regulation Z apply to an individual or business that “offers or extends credit.” 12 C.F.R. § 1026.1(c)(1). Thus, the extension of credit is a common basis for jurisdiction under both the CFP Act and TILA.

5. Here, in an overzealous effort to regulate the legal financing industry, the Bureau unilaterally—and erroneously—re-characterized RDLF’s business so as to situate it within these statutory parameters. However, when properly understood, it is clear that RDLF’s conduct falls well outside of the Bureau’s reach, as the Bureau is ignoring the plain English and statutory definitions of “credit.”

6. Contrary to the Bureau's characterization, RDLF is not in the business of extending credit or servicing loans. Rather, RDLF's affiliates purchase receivables from law firms and plaintiffs arising from legal settlements or judgments. In essence, the companies provide immediate liquidity in exchange for a receivable to be paid by a third party in the future—an important service for contingency fee-based law firms and certain plaintiffs that have an immediate need for capital.

7. Because RDLF's business of purchasing legal receivables is based on true sales as a matter of law, it is not based on extending credit and does not fall within any of the other enumerated items considered a "consumer financial product or service" under the CFP Act. Accordingly, RDLF's business falls outside of the Bureau's regulatory authority.

8. Counsel for RDLF raised this jurisdictional issue in a formal petition before the CFPB. Pursuant to the CFPB's own rules of procedure, the issue should have been ruled upon by the Bureau and then, if pursued by the Bureau, presented to a district court for adjudication.

9. Instead of proceeding through the agency and the courts, however, the day after RDLF formally challenged the Bureau's authority, the Bureau retaliated by bypassing its own adjudicatory procedures and taking steps to initiate a formal proceeding against RDLF. Upon information and belief, this constituted an adverse action against RDLF in retaliation for exercising its First Amendment right to petition.

10. As the Bureau has sought to bypass its own procedures that would have placed the scope of its authority before this Court, RDLF requires immediate judicial intervention to cabin the Bureau's overreach. Declaratory and injunctive relief is necessary to prevent RDLF from being forced to submit to an investigation and/or proceeding that the CFPB lacks authority to pursue, and to enjoin the CFPB from taking further retaliatory action in violation of RDLF's First Amendment rights.

JURISDICTION, VENUE, AND PARTIES

11. This court has subject matter jurisdiction over this action pursuant to 28 U.S.C. §§ 1331, 1345, 1346, and 2201.

12. The CFPB has finally determined that it has jurisdiction over RD Legal Funding. The foregoing decision marks the consummation of the decisionmaking process and constitutes a “final agency act” under Section 706 of the Administrative Procedures Act (APA), 5 U.S.C. § 706. *See Sackett v. E.P.A.*, 132 S. Ct. 1367, 1373 (2012) (“ . . . the APA provides for judicial review of all final agency actions”); *id.* at 1374 (“The Court holds that the Sacketts may immediately litigate their jurisdictional challenge in federal court. I agree, for the Agency has ruled definitively on that question.”) (Ginsburg, J. concurring).

13. Venue lies in this district under 28 U.S.C. § 1391(b) and (e), because RDLF does business in this judicial district and a substantial part of the activities alleged herein occurred in this district, and an agency of the United States is a defendant in this action.

14. Plaintiff RDLF is a New Jersey limited liability company with its principal place of business in Cresskill, New Jersey.

15. Defendant CFPB is an agency of the United States that is charged with regulating consumer protection as it relates to financial products and services. CFPB’s business address is 1800 L Street NW, Washington, District of Columbia, 20036.

BACKGROUND

RD Legal Funding

16. RDLF’s founder, Roni Dersovitz, practiced law in New York for 14 years. In 1996, Mr. Dersovitz began using his personal assets to factor law firm receivables and provide a source of funding and liquidity for contingency fee-based law firms. He quickly discovered there was a significant demand for this type of financing. Accordingly, in 1998, Mr. Dersovitz formed RDLF to identify, originate, and purchase legal receivables. RDLF grew quickly, and by

2001, Mr. Dersovitz had dissolved his law practice and begun focusing on legal financing full-time.

17. With the growth and success of RDLF, Mr. Dersovitz decided to create two private funds to raise capital necessary to take better advantage of the deep investment capacity in this area. In September 2007, Mr. Dersovitz launched RD Legal Funding Partners, LP, a Delaware limited partnership, and RD Legal Funding Offshore Fund, Ltd., a Cayman Islands exempted company (collectively, the “Funds”). Both Funds follow the same investment strategy—the Funds seek to generate stable returns for investors, while maintaining capital, primarily through: (a) purchasing from law firms their receivables representing legal fees owed; (b) purchasing from plaintiffs receivables representing their proceeds from legal judgments or settlements; (c) providing loans to law firms through secured lines of credit; and (d) providing capital to law firms to pursue certain other opportunities that do not fall within the categories above.

Consumer Financial Protection Bureau

18. On July 21, 2010, President Obama signed the Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub.L. No. 111–203, 124 Stat. 1376 (2010). Title X of the Dodd–Frank Act established the CFPB as an “independent bureau” within the Federal Reserve System, 12 U.S.C. § 5491(a).

19. Pursuant to the CFP Act, the Bureau is authorized to take action to prevent “covered persons” from “engag[ing] in any unfair, deceptive, or abusive act or practice” in violation of Title X or from violating, or offering or providing consumers with a financial product or service not in conformity with federal consumer financial law (as defined by 12 U.S.C. §§ 5481(14), 5531(a), 5536(a)(1)).

20. A “covered person” is defined as “any person that engages in offering or providing a consumer financial product or service.” 12 U.S.C. § 5481(6)(A).

21. The definition of a “financial product or service” includes “extending credit and servicing loans . . . extending or brokering [certain] leases . . . providing real estate settlement

services . . . engaging in deposit-taking activities . . . selling, providing, or issuing stored value or payment instruments . . . providing check cashing [and related] services . . . providing payments or other financial data processing products . . . providing financial advisory services . . . [certain conduct regarding] consumer report information . . . [and] collecting debt.” 12 U.S.C. § 5481(15)(A)(i)-(x).

22. The CFPB’s structure sets it apart from every other independent administrative agency. Unlike most federal agencies, which are headed by a panel of commissioners appointed for fixed, and often staggered terms, the Bureau is headed by a single Director who purportedly can only be removed for cause—making him “the single most powerful official in the entire United States Government, other than the President,” in terms of unilateral power. *PHH Corp. v. Consumer Fin. Prot. Bureau*, 839 F.3d 1, 16 (D.C. Cir. 2016) (finding structure of CFPB to be unconstitutional) (petition for review *en banc*, pending). Further, whereas most agencies are funded by Congress and thus subject to Congressional oversight, the Bureau’s annual budget, by contrast, is virtually guaranteed.

23. The absence of checks, balances, and oversight resulting from this unique structure triggered constitutional concerns from the legal academy and private sector.¹ On

¹ See, e.g., Eric Pearson, *A Brief Essay on the Constitutionality of the Consumer Financial Protection Bureau*, 47 CREIGHTON L. REV. 99 (2013) (arguing that the constitutional “line has been crossed” by the agency’s structural insulation from oversight); Lee A. Deneen, *Defeating a Wolf Clad as a Wolf: Formalism and Functionalism in Separation-of-Powers Suits*, 48 GA. L. REV. 579 (2014); see also Opinion, *Consumer Financial Protection Racket*, Wall Street Journal (April 24, 2016), <http://www.wsj.com/articles/consumer-financial-protection-racket-1461530729> (describing the agency as an “offense to constitutional governance”). Others have criticized the CFPB as overreaching and ineffective. See, e.g., Todd J. Zywicki, *The Consumer Financial Protection Bureau and the Return of a Paternalistic Command-and-Control Regulation*, 16 FED. SOC’Y PRAC. GROUPS 48 (2015); Ramesh Ponnuru, *CFPB Proves Its Critics Right*, Bloomberg View (Feb. 25, 2015), <https://www.bloomberg.com/view/articles/2015-02-25/cfpb-proves-its-critics-right>; David Francis, *Critics Say Consumer Bureau Is An Overreaching Monster*, The Fiscal Times (May 30, 2013), <http://www.thefiscaltimes.com/Articles/2013/05/30/Critics-Say-Consumer-Bureau-is-an-Overreaching-Monster>.

October 11, 2016, the United States Court of Appeals for the D.C. Circuit held that under the Supreme Court's separation of powers precedents, the CFPB's very structure is unconstitutional. *See PHH Corp.*, 839 F.3d at 36.

24. Additionally, numerous companies have recently charged the Bureau with exceeding its mandate by investigating businesses in industries not subject to its jurisdiction.

25. Most notably, in April 2016, a federal district court in Washington, D.C. rebuked the CFPB for exceeding its statutory authority by issuing a CID to investigate the Accrediting Council for Independent Colleges and Schools. *Consumer Fin. Prot. Bureau v. Accrediting Council for Indep. Colls. & Sch. (ACICS)*, No. 2016 WL 1625084, at *1 (D.D.C. 2016). The CFPB argued that because it had authority to investigate colleges' lending and financial-advisory services, it was therefore *also* authorized to investigate the accreditation of those colleges generally. *Id.* at *3. The court, however, rejected this "post-hoc justification" as a "bridge too far[.]" explaining that the "investigation target[ed] the accreditation process generally. This the CFPB was never empowered to do." *Id.*

26. The Bureau's jurisdictional authority has also been challenged in a proceeding against J.G. Wentworth, LLC ("JGW"), a company in the structured settlement and annuity payment purchasing industry. *In re J.G. Wentworth, LLC*, 2015-MISC-J.G. Wentworth, LLC-0001. In petitioning to set aside a Civil Investigative Demand ("CID") issued by the CFPB, JGW argued that the Bureau lacked jurisdiction because its business does not involve a consumer financial product or service under the CFP Act, and it does not extend "credit" under the meaning of TILA.

27. In an effort to enforce its authority, the CFPB filed a petition in United States District Court, Eastern District of Pennsylvania, *Consumer Financial Protection Bureau v. J.G.Wentworth, LLC*, No 2:16-cv2773-CDJ. JGW opposed it, asserting that, just as in *ACICS*,

the Bureau lacks jurisdiction to investigate its structured settlement and annuity payment purchasing business.²

28. Taken together, these cases reflect the Bureau's pattern and practice of seeking to unilaterally expand its reach through aggressive enforcement actions, rather than submit to the more laborious rulemaking process under the Administrative Procedures Act or work within the jurisdictional framework imposed by law. Moreover, with respect to RDLF, the Bureau has sought to avoid litigating the company's jurisdictional challenge altogether and, instead, has retaliated against the company for challenging the scope of the agency's authority just as it was challenged in the *ACICS* and *JG Wentworth* cases.

Procedural History

29. On July 26, 2016, the Bureau issued a CID to RDLF containing two interrogatories and requesting all versions of any contract used by the company to provide funding to a consumer. RDLF responded to the CID on August 26, 2016, and produced 218 contracts to the Bureau. Those documents consist of the Assignment and Sale Agreements that RD Legal Funding Partners or other related entities entered into with their customers for the purchase and sale of certain receivables relating to: (a) a judgment in the case *Peterson, et al. v. The Islamic Republic of Iran*, United States District Court, District of Columbia; (b) a claim to the September 11th Victim Compensation Fund; and (c) a settlement in the multi-district litigation entitled *In re: National Football League Players' Concussion Injury Litigation*.

30. While there are minor variations among the 218 contracts, they are all clearly identified as Assignment and Sale Agreements, and their terms unambiguously confirm that the transactions they memorialize all involve the sale of a legal receivable by the customer:

- “[Y]ou [the customer] wish to receive an immediate lump sum cash payment in return for selling and assigning a portion of the Award . . . to RD.”

² The United States Chambers of Commerce filed an amicus brief in support of J.G. Wentworth, asking the Court to ensure that the CFPB did not exceed its statutory authority.

- “You hereby sell and assign to RD your interest . . .” in a portion of the Award.
- **“This transaction is a true sale and assignment of the Property to RD and provides RD with the full risks and benefits of ownership of the Property.”**
- “[Y]ou and we intend that this Agreement is a true sale”
- “Upon RD’s payment to you of the Purchase Price, RD will own the Property free and clear of any Adverse Interests.”
- “You understand that you are giving up all of your interest in the Property.”
- “No Recourse. RD is purchasing all of your interest in the Property without recourse against you (other than for Breach). This means that, in the event RD for any reason (other than your Breach of this Agreement) does not receive all of the Property Amount, you will have no obligation to pay RD any portion of the Purchase Price that RD paid to you.”
- **“This is a complex financial transaction. By signing this Agreement, you are assigning your rights to a portion of this Award that you may receive in regard to the Case. In return for your assignment, you will receive an immediate cash payment that is significantly less than the portion of the Award that you are assigning. You are strongly encouraged before signing this Agreement to consult with an attorney and/or trusted financial advisor of your choice, who can assist you in determining whether this transaction will best fulfill your financial needs and objectives and protect your interest in the event you choose to proceed with this transaction.”**

31. On October 27, 2016, the Bureau issued another CID to RDLF, attached hereto as Exhibit A, which sought to depose a representative of RDLF. The Notification of Purpose in the October 27, 2016 CID states:

The purpose of this investigation is to determine whether litigation-settlement-advance firms or other unnamed persons have been or are engaging in unlawful acts or practices relating to the marketing or offering of consumer-financial products or services in violation of §§ 1031 and 1036 of the Consumer Financial Protection Act of 2010, 12 U.S.C. §§ 5531, 5536, the Truth in Lending Act, 15 U.S.C. § 1601 et seq., its implementing regulation, or any other Federal consumer financial law. The investigation also seeks to determine whether Bureau action to obtain legal or equitable relief would be in the public interest.

32. The CID was an affirmative representation by the Bureau, certified by a Deputy Enforcement Director, that the Bureau required additional information to determine whether to proceed further against RDLF.

33. RDLF received the second CID on or about November 1, 2016. On November 9, 2016, counsel for RDLF met and conferred with Bureau staff concerning the CID, and specifically set forth RDLF's view that (1) the Notification of Purpose failed to identify "the nature of the conduct constituting the alleged violation," as required by 12 U.S.C. § 5562(c)(2) and 12 C.F.R. § 1080.5; and (2) the Bureau lacks jurisdiction over RDLF, which does not extend credit or otherwise offer or provide consumer financial products or services as defined in the CFP Act and TILA.

34. The Bureau staff acknowledged these issues, but indicated that it disagreed with RDLF's view. The Bureau did not identify any basis for exercising jurisdiction over RDLF's business, but merely questioned certain legal actions taken by RDLF to enforce two consumer contracts that had been breached.

35. On November 21, 2016, RDLF submitted a Petition to Set Aside the Civil Investigative Demand, based on the CFPB's failure to identify the conduct it was investigating and its lack of jurisdiction over RDLF. Specifically, RDLF explained that: (a) the term "litigation-settlement-advance firms" was created by the Bureau; it is not an existing industry nor accurate depiction of RDLF's business; (b) unlike prior CIDs approved by the Bureau, the CID issued to RDLF did not meet the minimal threshold requirement of identifying the conduct being investigated; and (c) the omission was intentional, as RDLF's business is patently beyond the CFPB's regulatory authority.

36. The very next day, on November 22, 2016, the same CFPB staff member in charge of the CID emailed counsel for RDLF and asked to arrange a time for a call in reference to the CFPB's Notice and Opportunity to Respond and Advise (NORA) process, which is the preliminary step in initiating an enforcement action.

37. RDLF's counsel spoke with CFPB staff on November 28, 2016. During that call, CFPB staff expressed their conclusion that RDLF was mischaracterizing the transactions memorialized by the Assignment and Sale Agreements as true sales when they were in fact consumer loans, and based on that mischaracterization, the CFPB was considering whether to bring misrepresentation, disclosure, and related claims against RDLF under the CFP Act and TILA.

38. The same day, CFPB staff sent a NORA letter to RDLF's counsel, attached hereto as Exhibit B (the "NORA letter"). The letter states that the Bureau "expects to allege that [RDLF] violated the Consumer Finance Protection Act of 2010, 12 U.S.C. §§ 5331, 5336, and the Truth in Lending Act, 15 U.S.C. § 1601 et seq." The Bureau did not assert a basis for jurisdiction in either the NORA letter or in its November 28, 2016 telephone call with counsel for RDLF. Subsequently, CFPB staff reiterated its own conclusion that it has jurisdiction over RDLF.

39. The CFPB's jurisdictional determination and actions against RDLF threaten the viability of RDLF's business operations. Much of this harm cannot be quantified in monetary terms, and cannot be remedied by monetary damages. RDLF has a reasonable likelihood of success on the merits of its claims against the CFPB, and will suffer immediate and irreparable injury if the Bureau is permitted to continue pursuing an unauthorized investigation and/or permitted to continue retaliating against RDLF for asserting its rights in future proceedings.

FIRST CLAIM FOR RELIEF

(Declaratory Judgment)

40. RDLF re-alleges and incorporates paragraphs 1-39 above, as if fully set forth herein.

41. RDLF and its related entities purchase receivables from law firms and plaintiffs arising from legal settlements or judgments. Its factoring business (1) does not involve a consumer financial product or service as defined in the CFP Act; and (2) does not involve any extension of credit that could possibly give rise to a violation of the TILA.

42. The contractual language in the Assignment and Sale Agreements expressly states that the factoring transactions are true sales that result in the assignment of the seller's receivable to RDLF's related entities. Among other things, the contracts state: "**This transaction is a true sale and assignment of the Property to RD** and provides RD with the full risks and benefits of ownership of the Property."

43. Such terms are also consistent with New York law and those of other jurisdictions, which provide that factoring transactions involving the purchase of future receivables constitute sales agreements, not loans. *See Platinum Rapid Funding Grp. Ltd. v. VIP Limousine Servs., Inc.*, No. 604163-15, 2016 WL 4478807, at *5 (N.Y. Sup. June 8, 2016); *see also Singer Asset Fin. Co. L.L.C. v. Bachus*, 294 A.D.2d 818, 820 (N.Y. App. Div. 2002) (stating that a structured settlement payment sale "is not a loan but an absolute assignment").

44. Further, courts "have held that the most important single factor when determining whether a transaction is a true sale is the buyer's right to recourse against the seller." *In re Dryden Advisory Group, LLC*, 534 B.R. 612, 623 (Bkrcty. M.D. Pa. 2015). Here, the Assignment and Sale contracts expressly state that in the event the receivable is not paid by the third party obligor, there is no recourse against the seller.

45. TILA and its implementing regulation are similarly limited to individuals or business that "offer or extend credit." 12 C.F.R. § 1026.1(c)(1). TILA defines the term "credit" as "the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment." 15 U.S.C. § 1602(f); *see also* 12 U.S.C. § 5481(7) (CFP Act defining "credit" as "the right granted by a person to a consumer to defer payment of a debt, incur debt and defer its payment, or purchase property or serves and defer payment for such purchase"). The deferral of payment is plainly required for a transaction to be considered "credit."

46. Here, the Assignment and Sales Agreements make clear that there is (a) no extension of credit by RDLF, as the seller incurs no payment obligation at all (let alone a deferred payment obligation); (b) no incurrence of debt by the seller, and ultimately (c) no debt collection practice by RDLF.

47. Because the factoring agreements are true sales of the seller's receivables, rather than loans or extensions of credit, RDLF does not engage in conduct regulated by the CFP Act or TILA.

48. An actual controversy of a justiciable nature has arisen between RDLF, on the one hand, and the CFPB, on the other hand, regarding whether the agency has jurisdiction to pursue an investigation and/or enforcement action against RDLF. The CFPB has initiated an investigation of RDLF and undertaken steps requiring RDLF to defend itself. RDLF believes that because its factoring business is not subject to the CFP Act or TILA, the agency's investigation is unauthorized and improper. It is necessary and appropriate that a judicial determination be made at this time as to whether RDLF's business is within CFPB's jurisdiction because, among other reasons, it will obviate further action by the CFPB and provide a complete solution for the dispute between the parties.

49. RDLF therefore respectfully requests a declaratory judgment that: (i) the Assignment and Sales Agreements are true, non-recourse sales, and not loans; (ii) RDLF's business does not offer or provide "credit" under TILA because the customer incurs no repayment obligation; and (iii) because RDLF's business is not subject to the CFP Act or TILA, the only two federal consumer financial laws expressly relied on by the CFPB in its NORA letter, the agency lacks jurisdiction and is not authorized to pursue an investigation and/or enforcement action against RDLF.

SECOND CLAIM FOR RELIEF

(For Retaliation Against RDLF for Protected First Amendment Speech)

50. RDLF re-alleges and incorporates paragraphs 1-49 above, as if fully set forth herein.

51. The First Amendment to the United States Constitution guarantees RDLF's right to freedom of speech and to "petition the Government for a redress of grievances."

52. RDLF's Petition to Set Aside or Modify the CID is speech, and literally a petition, protected by the First Amendment.

53. On information and belief, the Bureau's actions against RDLF in proceeding with the investigation and issuing a NORA letter were retaliation for RDLF's exercise of its First Amendment rights. The *very next day* after RDLF exercised its right to petition and formally challenged the Bureau's jurisdiction, the CFPB informed RDLF's counsel that it was proceeding forward with its investigation and "expect[ed] to" bring an enforcement action against RDLF alleging violations of the Consumer Financial Protection Act of 2010 and Truth in Lending Act.

54. Initiation of NORA proceedings to bypass district court review of RDLF's challenge to the CFPB's authority was an adverse action that has injured RDLF.

WHEREFORE, RDLF prays for relief as follows:

(a) An order and judgment declaring that the purchase of legal receivables from consumers via the Assignment and Sale Agreements are true sales under the terms of the parties' contracts and RDLF's business is therefore not subject to the CFP Act;

(b) An order and judgment declaring that RDLF does not extend "credit" within the meaning of 15 U.S.C. § 1602(f) and 12 U.S.C. § 5481(7), and its business is therefore not subject to TILA or the CFP Act;

(c) An order and judgment declaring that the CFPB lacks jurisdiction to investigate and/or bring an enforcement action against RDLF;

(d) An order and judgment enjoining the CFPB from further retaliating against RDLF for exercising its First Amendment right to petition;

(e) An order and judgment enjoining the CFPB from pursuing an administrative proceeding against RDLF; and

(f) Such other and further relief as this Court may deem just and proper, including reasonable attorneys' fees and the costs of this action.

Respectfully submitted this third day of January, 2017.

By: /s/ Eric Kanefsky

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