

BEFORE THE ADMINISTRATOR
STATE OF WISCONSIN
DEPARTMENT OF FINANCIAL INSTITUTIONS
DIVISION OF BANKING

In re Morgan Drexen, Inc.

Case No. 10-S-127

DECISION AND ORDER

On October 5, 2011, the State of Wisconsin, Department of Financial Institutions, Division of Banking (“Division”) issued a Complaint and Notice of Hearing and Prehearing Conference (“Complaint”) to Respondent Morgan Drexen, Inc. (“Respondent” or “Morgan Drexen”). The Division’s Complaint alleges that Morgan Drexen has been and is currently conducting business in Wisconsin as an adjustment service company within the meaning of Wis. Stat. § 218.02(1)(a). The Division contends that Morgan Drexen’s business operations in Wisconsin fail to comply with Wis. Stat. § 218.02 and related administrative code provisions, including by:

- a. Conducting business as an adjustment service company without licensing by the Division as required by Wis. Stats. §§ 218.02(1)(a) and 218.02(2)(a)1;
- b. Charging a budget set up fee of more than \$25, in violation of Wis. Admin. Code § DFI-Bkg 73.01;
- c. Charging monthly fees to debtors in excess of the lesser of 10% of the amount of money paid to Respondent to be distributed to a creditor or creditors or \$120 in any one calendar month, in violation of Wis. Admin. Code § DFI-Bkg 73.01;

- d. Engaging in oppressive and deceptive practices and charging fees in violation of Wis. Stat. § 218.02.

DFI seeks an order for the following:

- a. Requiring Morgan Drexen to cease and desist from violating Wis. Stat. § 218.02 and Wis. Admin. Code § DFI-Bkg 73.01, in the manner described above;
- b. Requiring Morgan Drexen "to correct the conditions resulting from the violation" of Wis. Stat. § 218.02, which DFI contends should result in Morgan Drexen disgorging fees collected from Wisconsin debtors in the amount of approximately \$4,935,419.37;
- a. Assessing forfeitures against Morgan Drexen pursuant to Wis. Stat. § 220.04(9)(f), totaling at least \$986,000.00 for 986 violations of Wis. Stat. § 218.02.

On November 9, 2011, Morgan Drexen filed an answer to the Division's complaint, admitting that it is not licensed with the Division as an adjustment service company and that the fees charged to customers do not comply with Wis. Stat. § 218.02 and the attendant administrative code provisions. (*See* Respondent Morgan Drexen Inc.'s Answer to Complaint and Request for Declaratory Relief ("Answer")). However, Morgan Drexen asserts that it is not an adjustment service company subject to Wis. Stat. § 218.02 but instead provides administrative and paralegal support for lawyers. Morgan Drexen asserts the following defenses:¹

¹ Included in Morgan Drexen's list of putative affirmative defenses are allegations regarding the efficacy of the services performed by Morgan Drexen and the benefits to consumers. Those are not appropriate defenses. "The economic desirability of laws is exclusively a legislative concern." *State v. Ross*, 259 Wis. 379, 384, 48 N.W.2d 460 (1951). The only justiciable defenses properly before this administrative tribunal are whether Morgan Drexen's activities meet the statutory definition and whether the application of the statute to Morgan Drexen is unconstitutional.

- a. Morgan Drexen is not an “adjustment service company as that term is used in Wis. Stat. § 218.02(1)(a) because it is not engaged in the business of “prorating the income of a debtor”;
- b. Morgan Drexen is not engaged “as principal” in the business of prorating the income of a debtor because Morgan Drexen is acting as an agent on behalf of attorneys;
- c. The conduct for which the Division seeks to regulate the respondent are actually services performed on behalf of attorneys engaged in the practice of law, and the Division is constitutionally prohibited from regulating the practice of law.

Morgan Drexen seeks a declaration that Respondent is not subject to regulation by the Division because: (a) such regulation would violate the separation of powers doctrine, which prevents any branch other than the judicial branch from regulating or licensing attorneys and their agents who assist in the provision of legal services; and (b) Respondent is not an “adjustment service company” as that term is used in Wis. Stat. § 218.02(1)(a).

This matter is a Class 2 proceeding under Wis. Stat. § 227.01(3)(b), pursuant to which a three-day contested case hearing commenced on June 19, 2012. The parties presented opening statements and were afforded a full opportunity to proffer supporting evidence and testimony. The parties developed an extensive record, filing a litany of documentary evidence and twelve deposition transcripts. Division counsel traveled to Morgan Drexen headquarters in California to take depositions of Morgan Drexen personnel and affiliated lawyers, and the principal actors involved in this case appeared at hearing in person to testify. Following the hearing, the parties submitted lengthy principal and response briefs in support of their positions.

FINDINGS OF FACT

1. Morgan Drexen, a Nevada corporation headquartered in California, was founded in 2007 by Walter Ledda. Ledda is the former principal of companies who performed debt settlement services until 2004 when the Federal Trade Commission brought an action against those companies and Ledda personally for misrepresentations to consumers, lack of proper disclosures and violations of do-not-call regulations. Ledda personally settled with the Federal Trade Commission for \$1,356,000 and ceased operating those debt settlement companies. (Hearing Transcript (“Hr. Tr.”), pp. 382, 418-419; Joint Ex. 11b (Ledda Depo.), pp. 29, 34-45, 57).
2. Morgan Drexen is a nationwide debt settlement company that solicits customers in Wisconsin and other states. (Hr. Tr., pp. 89-90, 409)
3. In 2007, Morgan Drexen contracted directly with 37 Wisconsin residents to provide “Debt Negotiation Services,” whereby Morgan Drexen would directly negotiate with the debtors’ creditors and attempt to settle the unsecured debts of those residents. (DFI Exs. 4a, 1d; Hr. Tr., pp. 457-458).
4. Morgan Drexen’s debt settlement program counsels debtors to stop making payments to their creditors and instead requires the debtors to make monthly installment payments into an escrow account where the funds would accrue and later be paid out to creditors if Morgan Drexen successfully negotiated a settlement. (Hr. Tr., pp. 98-99, 101-102, 109-112).
5. Under Morgan Drexen’s debt settlement program, funds received from debtors would first be used to pay Morgan Drexen’s various fees, and moneys would only be paid out to creditors after those fees were paid and enough funds accumulated so that Morgan Drexen, in its discretion, determined that a settlement offer would be made or solicited from creditors. Upon

settlement with a creditor, Morgan Drexen would also receive a “settlement fee” of 25% of the difference between the debt owed and the settlement amount. Morgan Drexen agreed to directly provide this debt settlement service to those Wisconsin debtors. (DFI Ex. 4a).

6. Morgan Drexen was engaged as principal when directly contracting with the 37 Wisconsin debtors to provide debt settlement services. (DFI Ex. 4a).

7. The first Wisconsin debtor with whom Morgan Drexen contracted filed a complaint against Respondent with the Division. The Division contacted Morgan Drexen and informed that it was unlawfully conducting business as an unlicensed adjustment service company and must cease and desist such illegal activity and refund all of the money paid by the debtor. In response, Morgan Drexen refunded the money and informed the Division that they had no other Wisconsin residents enrolled in their program. (DFI Ex. 4a; Testimony of Jean Plale, June 8, 2012 (“Plale Testimony”); Question 23):

8. The Division subsequently received eight other complaints from Wisconsin debtors who received debt settlement services from Morgan Drexen. (Plale Testimony, Questions 22-32).

9. In 2007, Morgan Drexen began providing the same debt settlement services under the guise of providing paralegal support for attorneys. Morgan Drexen entered into an arrangement with three attorneys: Lawrence Williamson, a Kansas lawyer, Vincent Howard, a California lawyer, and Eric Rosen, a Florida lawyer. The attorneys had not practiced in the area of debt settlement before entering into this arrangement. The arrangement was that they would offer debt settlement services nationwide, marketing their business arrangement as legal services where the lawyers would directly contract with debtors “supported” by Morgan Drexen ostensibly as a paralegal firm. The three lawyers made a “gentlemen’s agreement” to divide up

the fifty states into three regions: debt settlement clients on the East Coast were Rosen's, those on the West Coast were Howards', and clients in the middle of the country would be Williamson's. Howard was responsible for recruiting attorneys in each state to act as "local counsel" because Williamson, Howard, and Rosen were not licensed to practice law in those states. Howard, Williamson, and Rosen are "engagement counsel" and claim to associate with "local counsel" in every state in order to provide, what they call, "debt settlement legal services" in those states. (Joints Exs. 4a; 4b; 11i (Williamson Depo.), pp. 28-29, 31, 44-45, 59, 62; 111 (Howard Depo.), pp. 14-15, 114; Hr. Tr., pp. 77-78, 86-90; 691, 695-696).

10. The contracts previously utilized by Morgan Drexen to contract directly with debtors for debt settlement were modified to cover this purported "legal service" arrangement. However, the overall model and fee structure previously utilized by Morgan Drexen to settle debts was retained. Under the guise of a "legal service," the contracts between the debtors and the lawyers provided for the same debt settlement service that Morgan Drexen had previously offered directly to consumers, and the contracts expressly excluded the provision of any legal services such as litigation or bankruptcy. (DFI Exs. 4a – Ex. 4e; Joint Exs. 11b, pp. 194-196; 11k (Stockinger Depo.), pp. 101-103, 106-107; Hr. Tr., pp. 371-374).

11. Under the initial arrangement between Morgan Drexen and the three lawyers, debtors were charged the same fees, with the exception that the monthly "maintenance fee" was increased from \$45 to \$48 and the "establishment fee" of 25% was re-named "engagement fee" with the same percentage. (DFI Exs. 4a – 4e; Joint Exs. 6a, pp. 0001-0002; 6c, pp. 0001-0002).

12. In July 2007, Wisconsin attorney Tiffany Stockinger signed up to become a "local counsel." The terms of her retainer were set forth in an engagement letter drafted by Howard, retaining Stockinger to act as local counsel to Howard's California law firm "to perform

whatever legal services are necessary for [Howard's] client that [Howard] cannot provide" in Wisconsin. The engagement letter specified that Stockinger would only perform services at Howard's request and with his pre-approval. Stockinger received a monthly retainer of \$500 up to a client base of 300, with an additional \$2.50 per client per month for once the client base surpassed 300. (Joint Exs. 4c; 11k, pp. 26-27).

13. Williamson, not Howard, was the engagement counsel for all Wisconsin clients purportedly serviced by Stockinger as local counsel even though Stockinger did not have a retainer agreement with Williamson as she did with Howard. (DFI Ex. 4b; Joint Ex. 11i, p. 149).

14. Between 2007 and 2009, Wisconsin debtors who signed up for the debt settlement program entered into a debt negotiation and settlement service agreement with Williamson, with Stockinger acting as local counsel. However, the agreement was solely for the provision of debt settlement services and did not provide for legal representation in the event that the client was sued. A separate contract with additional fees was required before legal representation would be provided. (DFI Exs. 4b; 4e; Joint Exs. 11i; pp. 149; 11k, p. 120).

15. In June 2009, Stockinger entered into a contract with Morgan Drexen to serve as "engagement counsel" for Wisconsin debtors serviced by Morgan Drexen. The June 2009 contract remained in effect until January 2011 when Stockinger signed a different contract. Under this contract, Morgan Drexen hired Stockinger for "supervision and approval of client settlements" and agreed to pay Stockinger a minimum of \$1,000 advanced each month for the first 300 clients "from all fees received by [Morgan Drexen] from the STOCKINGER client base" and an additional \$2.50 per client for each client over that 300-client base. (Joint Ex. 4d).

16. Until 2009, with respect to the clients serviced by Morgan Drexen where Stockinger served as "local counsel," Respondent admits that Morgan Drexen was not

Stockinger's agent. (Morgan Drexen, Inc.'s Corrected Post-Hearing Response Brief ("MD Response Brief"), p 16, n. 5).

17. With respect to the clients serviced by Morgan Drexen where Stockinger served as "engagement counsel" under the June 2009 contract, Morgan Drexen was engaged as principal and was not the agent of attorneys. Neither Stockinger nor any other attorney practicing law in Wisconsin had the right to control Morgan Drexen's work. (Joint Exs. 4a – 4e; 11l, p. 114; 13; Hr. Tr. pp. 253, 373-374).

18. In October 2010, the Federal Trade Commission established a new rule prohibiting debt relief companies engaged in telemarketing from charging debtors "up front" fees. Morgan Drexen modified its contract with debtors to something Morgan Drexen terms a "hybrid" or "non-formal bankruptcy" debt negotiation service. However, this contract does not allow for the provision of any bankruptcy or legal services. Instead, the only relation to bankruptcy under this new "hybrid" contract is that Morgan Drexen prepares a mock bankruptcy petition for the debtor and sends it to creditors in an effort to persuade them that the debtor is judgment proof. For this purported service, the debtor is charged what Morgan Drexen calls an "engagement fee" as a purported legal retainer. However, if the debtor does want to hire an attorney and file for bankruptcy, the debtor must enter into a separate contract with the attorney and pay an additional fee. (Joint Exs. 11b, pp. 202-203; 11k, pp. 132-135; Hr. Tr. pp. 326-332).

19. Under Morgan Drexen's attorney model for providing debt settlement services, the service is largely automated and all of the essential functions of the service are performed by Morgan Drexen personnel. Once a debtor is enrolled, monthly withdrawals are automatically withdrawn from the debtor's bank account. The amounts are determined by a formula calculated by Morgan Drexen's employees, with Morgan Drexen's fees determined as a percentage of the

debtor's outstanding debts enrolled. When these withdrawals accumulate sufficient to pay for Morgan Drexen's engagement fee, the excess debtor funds are placed into a trust account to which Morgan Drexen has access. If Morgan Drexen personnel successfully negotiate a settlement with a creditor, Morgan Drexen forwards the funds to creditors in payment of the negotiated settlement. (Joint Exs.10, 11b, p. 154; 11j, p. 85; 11k, pp. 101-107, 122-124, 176-177; Hr. Tr. Pp. 371-374).

20. Morgan Drexen, rather than the attorneys, directly negotiates with creditors to settle clients' debts. Morgan Drexen also performs the same functions as it had when contracting directly with debtors, including conducting client intake, analyzing debtors' budget and the potential amounts that could be saved by settling with the creditors, preparing the payment schedule for the debtors, directly handling all communications with both creditors and the debtor-clients, the accounting, intake and payments out to creditors of client funds, and the distribution of funds to all the attorneys. Client funds were placed in trust accounts to which Morgan Drexen had access and which was accounted for and distributed by Morgan Drexen. (Joint Exs. 11d, pp. 36, 47-48, 50, 53-54, 60, 114; 11k, pp. 63-69, 85-88, 93-99, 117-120, 175-177; Hr. Tr., pp. 101-103, 282, 358-359, 361, 371-374, 405, 425-426, 440-443, 487-490, 743-744).

21. Morgan Drexen devised a formula projecting the estimated amount of savings a debtor will achieve through the debt settlement program. Morgan Drexen determines how long the debtor will remain in the program to achieve those projected savings and the amount of monthly payment the debtor must make, taking into account that Morgan Drexen's fees would first be deducted on a monthly basis. Stockinger does not know how Morgan Drexen makes this

determination, has no input on how it is done, and has never asked that any fees or charges be modified. (Hr. Tr., pp. 365-366, 369; Joint Ex. 11k, pp. 103-108).

22. No attorney licensed to practice law in Wisconsin provides any training to Morgan Drexen employees. (Hr. Tr., pp. 746-747; Joint Ex. 11e, pp. 77-81; 11k, p. 70).

23. Stockinger does not have expertise in drafting contracts and relies on Morgan Drexen to perform that work. (Joint Ex. 11k, pp. 89, 101).

24. Morgan Drexen sometimes settles debts on an installment basis, whereby the debtor's obligation to the creditor is resolved by distributing proportional amounts to the creditor. Morgan Drexen has prepared written guidelines that its personnel must follow for installment settlements. (Joint Ex. 10; Hr. Tr., pp. 439-440).

25. Morgan Drexen, not Stockinger, has specialized knowledge of the credit industry, including knowledge of the timing and circumstances in which creditors are willing to accept reductions in the debt owed. This knowledge is "secret" and "proprietary" to Morgan Drexen and is not shared with Stockinger. In "approving" the settlements negotiated by Morgan Drexen, Stockinger usually has no idea why or how the settlement was reached. Settlement approval occurred through an Internet-based portal where the attorney could simply click a button to indicate approval. Stockinger would approve the settlement if it looked "reasonable" to her. However, if an attorney in the Morgan Drexen program does not respond to the settlement proposal within 24 hours, it is deemed automatically approved. (DFI Rebuttal Ex. 5d; Joint Ex. 11k, pp. 128-131, 177; Hr. Tr. pp. 373-374, 478-483).

26. In January 2011, Stockinger and Morgan Drexen entered into a new contract for Stockinger to continue serving as "engagement counsel" for Wisconsin clients that modified some of the provisions of the July 2009 contract but did not provide the attorney with the right to

control Morgan Drexen's debt settlement activities. With respect to the clients serviced by Morgan Drexen where Stockinger served as "engagement counsel" under the January 2011 contract, Stockinger did not have the right to control Morgan Drexen's debt settlement activities. No other attorneys had the right to control Morgan Drexen's debt settlement activities. Morgan Drexen is engaged as principal and is not the agent of attorneys under this agreement. (Joint Exs. 4a – 4f; Joint Ex. 13).

27. Neither Attorney Williamson nor Attorney Howard provided any legal services to Wisconsin debtor-clients serviced by Morgan Drexen. (Hr. Tr. pp. 253; Joint Ex. 111, p.114).

28. Morgan Drexen places advertisements in Wisconsin in radio and television media, urging Wisconsin residents overwhelmed with debt to contact Morgan Drexen at a 1-800 number that connects with Morgan Drexen's offices in Southern California. Some of these advertisements identify Attorney Stockinger, others identify a law firm that is not licensed to practice in Wisconsin, and others identify no attorney at all. (Hr. Tr., pp. 334-336, 339; Joint Ex. 11b, p. 100; DFI Exs. 5a, 5b, DFI Rebuttal Ex. 1).

29. As of June 2012, Wisconsin debtors remitted \$8,072,442.04 in funds to Morgan Drexen. (Plale Testimony, Question 52).

30. As of June 2012, \$3,819,360.11 of the funds remitted to Morgan Drexen by Wisconsin debtors was paid out to creditors. The remaining 52.7% of funds, \$4,253,081.93, was paid as fees for the debt settlement service. (Plale Testimony, Question 53).

31. From 2007 through January 31, 2012, a total of 1,890 debtors contracted for debt settlement services provided by Morgan Drexen. (Plale Testimony, Question 55).

32. 618 of Morgan Drexen's now-inactive customers were in the debt settlement program for less than 8 months. These 618 debtors signed up a total of 4,685 separate credit

accounts to be negotiated and settled by Morgan Drexen. Of those 4,685 separate accounts, only 10 were settled, with a total of \$6,162.18 of debtor funds distributed to creditors in payment of the 10 settlements. Those Wisconsin debtors paid \$230,746.28 in fees for this service. (Plale Testimony, Question 58).

33. Debtors enrolled in the Morgan Drexen debt settlement program typically do not speak with the attorney that is purportedly representing them, do not know how to contact the attorney, receive no legal counsel of any kind, and often do not understand that they are supposed to be represented by an attorney. (Hr. Tr., pp. 604-605, 632-635, 646-650, 669-670, 673).

34. Morgan Drexen has never been licensed as an adjustment service company in Wisconsin. (Plale Testimony, Question 65).

CONCLUSIONS OF LAW

1. The Division shall enforce all laws relating to adjustment service companies in the State of Wisconsin, and shall enforce and cause to be enforced every law relating to the supervision and control thereof, pursuant to Wis. Stat. § 220.02(2)(b).

2. Morgan Drexen is an “adjustment service company” as defined by Wis. Stat. § 218.02(1)(a) because it is in the business of prorating the income of a debtor to the debtor’s creditors.

3. The Division does not have to prove that Morgan Drexen, a corporation, is “engaged as principal” to be covered by Wis. Stat. § 218.02. Notwithstanding that, with respect to at least 1,890 Wisconsin residents serviced by the Respondent between 2007 and the present,

Morgan Drexen was “engaged as principal” in the business of prorating and was not the agent for attorneys.

4. Morgan Drexen has been conducting business as an adjustment service company in Wisconsin illegally and without licensure by the Division as required by Wis. Stat. § 218.02.

5. Morgan Drexen has been charging fees for adjustment service company activities in excess of the maximum fixed by the Division, in violation of Wis. Stat. §218.02 and Wis. Admin. Code § DFI-Bkg 73.

6. Applying Wis. Stat. § 218.02 and attendant administrative code provisions to Morgan Drexen is constitutionally permitted and does not violate the separation of powers doctrine.

7. The Division may impose forfeitures against Morgan Drexen of up to \$10,000 for each violation of the adjustment service company law that Morgan Drexen committed.

8. The Division may require Morgan Drexen to make restitution of fees illegally charged to Wisconsin debtors by virtue of its power to establish the maximum fees that an adjustment service company may charge and to correct the conditions resulting from Morgan Drexen’s violations of those maximum fees.

DISCUSSION

I. MORGAN DREXEN’S BUSINESS ACTIVITIES IN WISCONSIN CONSTITUTE A “BUSINESS OF PRORATING THE INCOME OF A DEBTOR TO THE DEBTOR’S CREDITOR OR CREDITORS” WITHIN THE MEANING OF WIS. STAT. § 218.02.

Morgan Drexen conducts prorating services as defined by the Wisconsin Court of Appeals in *JK Harris Fin. Recovery Sys., LLC v. Dep't of Fin. Insts.*, 2006 WI App 107, 293 Wis. 2d 753, 718 N.W.2d 739. Morgan Drexen “negotiates a reduction or extended payment on

behalf of the debtor for the debtor's outstanding debt with that creditor," therefore, "it is in fact dividing the debtor's income proportionately and is engaged in the activity of prorating the debtor's income," subject to the requirements of Wis. Stat. § 218.02. See *JK Harris*, 2006 WI App 107, ¶ 16.

In *JK Harris*, the defendant debt settlement company's activities were described as follows:

- a. It contacts creditors and negotiates a reduction or extended payment on behalf of the debtor for the debtor's outstanding debt with that creditor;
- b. It works with the debtor directly to set up a self-established budget and financial plan to assist the debtor in managing his or her finances, including making payments to creditors who have reduced their indebtedness or extended the time for payments;
- c. In consideration of these services JK [Harris] receives a flat fee from the debtor.

(*Id.*, ¶ 4). The Court of Appeals accepted the definition of "prorating" as meaning "to divide, distribute, or assess proportionately," which the Court explained:

This definition can be reasonably read to mean that taken separately or in combination with each other, three activities are considered to be prorating. The activities are i) to divide proportionately, ii) to distribute proportionately or iii) to assess proportionately.

The division correctly argues that the element of receiving and disbursing funds, or taking the physical possession of funds does not have to be present for prorating to occur. When JK H[arris] negotiates a reduction or extended payment on behalf of the debtor for the debtor's outstanding debt with that creditor, it is in fact dividing the debtor's income proportionately and is engaged in the activity of prorating the debtor's income, and as such is an entity subject to the requirements of [WIS. STAT. § 218.02].

Id., ¶ 16 (emphasis added). The Court of Appeals elaborated:

The Division found, and JK Harris acknowledges, that, in return for a flat fee from a debtor, it negotiates with creditors to obtain reductions or extended payments on behalf of the debtor, and it then "works with the debtor" to set up a "self-established" budget and financial plan that includes "making payments to creditors who have reduced their indebtedness or extended the time for payments." It seems clear that the subject, purpose and result of JK Harris's communications with debtors and creditors is the apportioning ("dividing proportionately") of the debtor's income to (or among) his or her creditors. Put another way, the division of the debtor's income proportionately to his or her creditor or creditors would not occur absent JK Harris's involvement.

2006 WI App 107, ¶ 22. Morgan Drexen dismisses these passages as dicta and insists that the Court's statements not be taken literally. Respondent contends that these portions of the decision were simply the Court's recitation of the Division's own position and not the holding of the Court. It points out that the defendant in *JK Harris* did not argue, as Morgan Drexen does, that the act of prorating requires "proportionality." (Morgan Drexen, Inc.'s Post-Hearing Brief (MD Brief"), pp. 48-67).

But, the entire controversy in *JK Harris* was framed by the Court as whether a business engages in prorating when it: (1) contacts creditors and negotiates a reduction or extended payment on behalf of the debtor; (2) works with the debtor directly to set up a self-established budget and financial plan to assist the debtor in managing his or her finances, including making payments to creditors who have reduced their indebtedness or extended the time for payments; and (3) receives a flat fee for its services. *Id.*, ¶ 4. The Court of Appeals expressly held that such activity was prorating, and this cannot be disregarded nor relegated to mere dictum. *See State v. Holt*, 128 Wis. 2d 110, 123, 382 N.W.2d 679, 686 (Ct. App. 1985), *superseded by statute on other grounds* ("When an appellate court intentionally takes up, discusses and decides a question germane to a controversy, such a decision is not a *dictum* but is a judicial act of the court which it will thereafter recognize as a binding decision.").

Morgan Drexen asserts that it is providing "debt settlement" services and not "prorating" because there is no "proportional" distribution of the debtor's income. Respondent claims that it settles debts "sequentially" so that an entire debt is settled at a discrete point in time and therefore lacks proportionality. Morgan Drexen's argument is a rhetorical distinction without substantive difference.

Respondent's "debt settlement" model exudes the same premise determined to constitute "prorating" in *JK Harris*: (1) Morgan Drexen develops a budget from which a portion of the debtor's income will be placed in escrow to pay the debtor's outstanding obligations; (2) once there are sufficient funds in the debtor's trust account, Morgan Drexen contacts creditors and negotiates a reduction or extended payment of the debtor's obligations; and (3) Morgan Drexen receives various fees for these services. *Cf. JK Harris*, 2006 WI App 107, ¶ 4. Morgan Drexen, like the debt settlement company in *JK Harris*, conducts prorating because it makes a proportional division of the debtor's income.

It is not conclusive, as Respondent claims, that Morgan Drexen sometimes negotiates debts so that nothing is owed by the debtor and there is no distribution, proportionate or otherwise, made to the creditor. *JK Harris* unambiguously explained that "one who prorates amounts of money may do so by distributing money proportionately, but the act of prorating may be accomplished in other ways (i.e., by dividing or assessing proportionately)." 2006 WI App 107, ¶ 17. Morgan Drexen makes a proportional division of the debtor's income by apportioning the debtor's income into escrow on a monthly basis for the purpose of making payments to creditors. This is prorating because it is the "apportioning" of the "debtor's income to (or among) his or her creditors."² 2006 WI App 107, ¶ 22.

Respondent's argument is also factually wrong. Morgan Drexen *does* make proportional distributions of debtor funds, entering into settlements whereby creditors are repaid on an installment basis. Morgan Drexen's own settlement guidelines contemplate installment payments. (Joint Ex. 10 ("Installment Settlement Guidelines")). The guidelines require that

² Contrary to Respondent's protestations, there is no requirement that prorating be conducted with mathematically-precise proportionality. Such cramped, hyper-technical reading of the statute was rejected by *JK Harris* and must be similarly rejected here.

funds in the debtor's trust account not be spent entirely on a single settlement because that creates "a disproportionate settlement pattern for the clients." Instead, the guidelines require that only 75 percent of funds in the trust account may be used for a first payment and "then some other formula that figures out how to calculate the rest of it." (Hr. Tr., pp. 439-440). This too fulfills the definition of prorating. *JK Harris*, 2006 WI App 107, ¶ 17.

JK Harris is precisely consistent with the legislature's intent in enacting Wis. Stat. § 218.02. According to the Report of the State Banking Commission and Interim Advisory Legislative Committee to Investigate Finance Companies (1935) ("SBC Report"), the legislation was intended to cover businesses who "attempt to adjust the debts of individuals by making agreements with all the creditors of any particular debtor, whereby his creditors are either paid proportionally or his debts are reduced by compromise and liquidated for a smaller amount." (SBC Report, p. 56); *Cf. JK Harris*, 2006 WI App 107, ¶16 ("When JK H[arris] negotiates a reduction or extended payment on behalf of the debtor for the debtor's outstanding debt with that creditor, it is in fact dividing the debtor's income proportionately and is engaged in the activity of prorating the debtor's income...")

Morgan Drexen offers a novel interpretation of this legislative history, declaring:

The 'legislature's two-pronged definition of 'adjustment service company' was intended to cover these two different business practices. Section 218.02(1)(a) covers both (1) "the business of prorating the income of a debtor to the debtor's creditor(s)" and (2) "the business...of assuming the obligations of any debtor by purchasing the accounts the debtor may have with the debtor's several creditors." Wis. Stat. § 218.02(1)(a). The first provision covers those bureaus that undertook to divide the debtor's income proportionally among his creditors; the second covers those bureaus that liquidated the debtor's obligations for a lesser amount – **that is by purchasing those obligations from the debtor's creditors for an amount less than the total due** – and then requiring the debtor to pay off the debt to the bureau.

(MD Brief at p. 60) (emphasis added).

Respondent's argument is a rhetorical leap with no mooring in statutory text, legislative history, or case law. Morgan Drexen offers no support for its declaration that the statute was aimed only at a particular subset of businesses who liquidate a debtor's obligations by purchasing them from the debtor's creditors. The same document that Morgan Drexen cites states that the legislature was concerned generally with businesses who liquidate the debtor's obligations by negotiating a reduction of the debt, *i.e.* who "attempt to adjust the debts of individuals by making agreements with all the creditors of any particular debtor, whereby his creditors are either paid proportionally or his debts are reduced by compromise." (SBC Report, p. 56) (emphasis added). This confirms that the definition of prorating was intended to cover both debt resolution through proportional payments to creditors *and* the general negotiation and compromise of that same debt.

II. THE STATUTE DOES NOT REQUIRE THAT MORGAN DREXEN, A CORPORATION, BE "ENGAGED AS PRINCIPAL" TO BE AN ADJUSTMENT SERVICE COMPANY.

Respondent asserts that it cannot be an adjustment service company because it was not "engaged as principal," which Morgan Drexen argues is a separate statutory element of Wis. Stat. § 218.02(1)(a) that must be proven by the Division. The Division maintains that Morgan Drexen was engaged as principal but also that it is not necessary for Morgan Drexen to be a principal to be covered by the statute.

Statutory interpretation begins with the language of the statute. If the meaning of the statute is plain, the inquiry ends. *State ex rel. Kalal v. Circuit Court for Dane County (In re Criminal Complaint)*, 2004 WI 58, ¶ 45, 271 Wis. 2d 633, 681 N.W.2d 110. Statutory language is given its common, ordinary, and accepted meaning, except that technical or specially-defined

words or phrases are given their technical or special definitional meaning. *Id.* Statutory language is interpreted in the context in which it is used; not in isolation but as part of a whole; in relation to the language of surrounding or closely-related statutes; and reasonably, to avoid absurd or unreasonable results. *Id.*, ¶ 46. In addition to the language of the statute, "scope, context, and purpose are perfectly relevant to a plain-meaning interpretation of an unambiguous statute." *Id.*, ¶48.

When interpreting a statute, a court focuses on "statutory meaning" as opposed to "legislative intent," relying heavily on "intrinsic" sources such as the words of the statute, including dictionary definitions, in addition to the statutory context, scope, and purpose. *See State ex rel. Kalal*, 2004 WI 58, ¶¶ 36-52. As a rule, Wisconsin courts do not consult "extrinsic" sources of statutory interpretation unless the statute is ambiguous, although extrinsic sources may be used to confirm or verify plain statutory meaning. *Id.*, ¶¶ 50-51.

Moreover, Wis. Stat. § 218.02 is a remedial statute, and the Division is charged by the legislature with the "duty" and "power" to "prevent evasions of this section" and "protect debtors from oppressive or deceptive practices of licensees." *See JK Harris*, 2006 WI App 107, ¶ 21; Wis. Stat. § 218.02(7). A narrow interpretation of Wis. Stat. § 218.02 is inconsistent with this legislative mandate. *Id.*

The statute defines an adjustment service company as:

"[A] corporation, limited liability company, association, partnership or individual engaged as principal in the business of prorating the income of a debtor to the debtor's creditor or creditors, or of assuming the obligations of any debtor by purchasing the accounts the debtor may have with the debtor's several creditors, in return for which the principal receives a service charge or other consideration."

Wis. Stat. § 218.02(1)(a) (emphasis added).

Respondent contends that, for the statute to apply, the Division must prove that any "corporation, limited liability company, association, partnership or individual" in the business of

prorating was hired “as principal” directly by the debtor. Respondent’s construction of the statute is grammatically incorrect, deviates from rules for statutory interpretation, and distorts the statutory language beyond its context and plain meaning.

Morgan Drexen’s interpretation implies an element not written in the statute: that an adjustment service company be “engaged as principal” *directly by the debtor*. (MD Brief, p. 29). The word “engaged” in that context presumably means the same as “hired” or “contracted” and would shield from the statute’s reach a company such as Morgan Drexen who is subcontracted to adjust a debtor’s obligations. However, language requiring the debtor to directly hire an adjustment service company is not part of the statute, and it would be improper to graft it onto the statute by judicial fiat. *See Peterson v. Midwest Sec. Ins. Co.*, 2001 WI 131, ¶ 19, 248 Wis. 2d 567, 636 N.W.2d 727 (a court “cannot rewrite [a statute] in the exercise of interpreting it.”).

If the word “engaged” meant the same as “hired,” then the statute would be grammatically nonsensical. Under Morgan Drexen’s position, an adjustment service company would be defined essentially as one who is “hired as principal by the debtor.” But, as Respondent argues elsewhere (MD Brief, p. 29), a debtor does not hire the adjustment service company to act as principal; the debtor *hires the company to act as the debtor’s agent*. If the statute meant what Respondent claims, the modifying phrase should read “engaged as agent” by the debtor.

The common and ordinary definition of the word “engage,” today and contemporaneous with the time of statutory enactment, is “[t]o employ or involve one’s self; to take part in; to embark on.” Black’s Law Dictionary 661 (3rd ed. 1933); *accord* Black’s Law Dictionary 549 (7th ed. 1999). This definition should be used because it fits the statutory context without requiring

additional language to be read into the statute. And such definition plainly captures the conduct of an adjustment service company like Morgan Drexen who performs services on a subcontracted basis.

Morgan Drexen incorrectly argues that the qualifier “engaged as principal” applies to any entity or individual in the business of prorating and requires analysis of whether the adjustment service company is an agent or a principal.³ According to Respondent, “engaged as principal” modifies the entirety of what precedes it, namely a “corporation, limited liability company, association, partnership or individual...” *Id.* But, it is absurd to read the statute that way since a “corporation, limited liability company, association, [or] partnership” already satisfies such element. *See State ex rel Kalal*, 2004 WI 58, ¶ 46 (statutes must be construed to avoid surplusage and absurd and unreasonable results). As opposed to sole proprietors, who may or may not conduct prorating activities through employees or other agents, a corporation in the business of prorating is always a principal because it can only act through its agents and employees who perform the prorating activities on the entity’s behalf.⁴ Thus, even accepting Respondent’s erroneous interpretation does not shelter Morgan Drexen, Inc. from the statute’s reach.

The significant grammatical flaws in Morgan Drexen’s statutory interpretation arise from its disregard of the principal of construction known as the “doctrine of the last antecedent.” *See*

³ It is not readily apparent that the term “principal” in the statute is unambiguously used in the context of agency law. Notably, a violation of Wis. Stat. § 218.02 is subject to criminal penalties. *See* Wis. Stat. § 218.02(10). A “principal” in the context of criminal law includes both principals and agents who aid and abet illegal activity. *See* Wis. Stat. § 939.05. “When two or more persons aid and abet each other in the commission of a crime, all being present, all are principals, and equally guilty.” *Holland v. State*, 91 Wis. 2d 134, 143-144, 280 N.W.2d 288 (1979). This too would cover Morgan Drexen’s activities regardless of whether it was acting as an agent for another. The parties do not discuss this possible definition of the term, so I assume without deciding that the statute refers to a “principal” as meant by the law of agency.

⁴ The common and ordinary definition of “principal” in this context is “[o]ne who authorizes another to act on his or her behalf as an agent.” *Black’s Law Dictionary* 1210 (7th ed. 1999)

Dagan v. State, 162 Wis. 353, 354, 156 N.W. 153 (1916). “The rule is that qualifying or limiting words or clauses in a statute are to be referred to the next preceding antecedent, unless the context or the evident meaning of the enactment requires a different construction.” *Fuller v. Spieker*, 265 Wis. 601, 605, 62 N.W.2d 713 (1954); accord *Jorgenson v. Superior*, 111 Wis. 561, 566, 87 N.W. 565 (1901); *Service Inv. Co. v. Dorst*, 232 Wis. 574, 576-578, 288 N.W. 169 (1939); *In re Trust of Bowler*, 56 Wis. 2d 171, 179-180, 201 N.W.2d 573 (1972); *Vandervelde v. Green Lake*, 72 Wis. 2d 210, 215, 240 N.W.2d 399 (1976); see also *Barnhart v. Thomas*, 540 U.S. 20, 26, 124 S. Ct. 376, 157 L. Ed. 2d 333 (2003); *Adamowicz v. IRS*, 552 F. Supp. 2d 355, 367 (S.D.N.Y. 2008). As an exception, the modifier may be deemed to apply to all preceding terms and not only the immediate antecedent term when the modifying clause is separated from antecedents by commas. See *Service Inv. Co.*, 232 Wis. 574, 577.

Here, the modifying clause is not set off by commas, confirming that the phrase modifies only the nearest antecedent term. See *Id.* Thus, the clause “engaged as principal” qualifies only the immediately preceding term “individual;” it imposes no qualifications on a “corporation, limited liability company, association, [or] partnership.” The statute does not require the Division to prove that Morgan Drexen, a corporation, is a “principal” before it will be subject to the Division’s purview.

The “context or the evident meaning” of the statute does not indicate a different construction, see *Fuller*, 265 Wis. 601, 605, because the doctrine fits harmoniously with the statute. Wis. Stat. § 218.02 regulates and requires licensure of adjustment service companies; it does not separately license those companies’ individual employees. See Wis. Stats. §§ 218.02(2)-(6). This contrasts with other businesses regulated by the Division under Chapter 218, such as collection agencies and motor vehicle dealers who are regulated as entities while

their representatives are also individually licensed. *See* Wis. Stats. §§ 218.04(2); 218.0114(1); *see also Georgina G. v. Terry M. (In the Interest of Angel Lace M.)*, 184 Wis. 2d 492, 511-512, 516 N.W.2d 678 (1994) (statutes in the same chapter which assist in implementing the chapter's goals and policy should be read *in pari materia* and harmonized if possible).

In defining an "adjustment service company" under Chapter 218, the legislature used the phrase "individual engaged as principal" simply to distinguish between individuals providing prorating services as sole proprietors and individuals performing such services on behalf of their employer. The modifying clause clarifies that, while employees of adjustment service companies are not individually licensed and regulated by the Division, individuals conducting business as adjustment service companies (*i.e.* unincorporated sole proprietorships) are covered by the statute. Respondent is organized as a corporation, so it is irrelevant whether Morgan Drexen was otherwise "engaged as principal."

The Division's application of Wis. Stat. § 218.02 to Morgan Drexen is consistent with the plain meaning of the statutory text, the context of the statutory scheme, and the legislative history. It is also in harmony with the legislature's mandate to broadly interpret the adjustment service company law to effectuate its remedial purpose. The law would be readily subject to evasion if adjustment service companies could avoid regulation simply by arranging their affairs to serve some nominal principal. Therefore, the Division does not need to prove that Morgan Drexen is "engaged as principal" for the statute to apply.

III. TO THE EXTENT TO WHICH THE STATUTE REQUIRES A CORPORATION TO BE ENGAGED AS PRINCIPAL, MORGAN DREXEN MEETS THAT CRITERION.

Notwithstanding the foregoing, the parties have devoted considerable effort to arguing the factual merits of whether Morgan Drexen is “engaged as principal.”⁵ The same result follows. Under the definition propounded by the Respondent, Morgan Drexen is “engaged as principal” and subject to the statute.

Agency is a specific legal relationship comprised of three elements: (1) the conduct of the principal showing that the agent is to act for him or her; (2) the conduct of the agent showing that he or she accepts the undertaking; and (3) the understanding of the parties that the principal is to control the undertaking. WIS. JI - CIVIL 4000 (2006); *see also Sevey v. Jones*, 235 Wis. 109, 111–12, 292 N.W. 436, 437–38 (1940). An agency relationship exists only when these elements are present. *Id.*; *see also* Restatement (Third) Agency, § 1.02 (2006).

“However, the mere authority to act for another does not, without more, establish agency as a matter of law. Agents and independent contractors both act on behalf of the principal. The critical distinction is the degree of control exercised by the principal.” *Envirologix Corp. v. City of Waukesha*, 192 Wis. 2d 277, 295, 531 N.W.2d 357 (Ct. App. 1995). “The most-important single indicium is who has retained the right to control the details of the work.” *Bond v. Harrel*, 13 Wis. 2d 369, 374, 108 N.W.2d 552 (1961). “There are many relationships in which one acts for the benefit of another which are to be distinguished from agency by the fact that there is no

⁵ The parties disagree over the burden of proof. The Division argues that the burden is on Morgan Drexen to establish that it was acting as an agent. *See Felland v. Sauey*, 2001 WI App 257, ¶ 28, 248 Wis. 2d 963, 637 N.W.2d 403 (“When agency is an issue in a case, the general rule is that the burden of proof lies with the party asserting the existence of the agency relationship.”). Morgan Drexen ripostes that “engaged as principal” is a statutory element that must be proven by the Division. Because the Division has proven this purported element with substantial evidence, I assume without deciding that it has the burden of proof.

control by the beneficiary." *Renich v. Klein*, 230 Wis. 123, 128-130, 283 N.W. 288 (1939) (citations omitted).

There "is not necessarily an agency relationship because the parties to a transaction say that there is, or contract that the relationship shall exist, or believe it does exist." *Sevey*, 235 Wis. 109, 112. The parties labeling of their relationship is not controlling. *See* Restatement (Third) Agency, § 1.02. It is also appropriate to consider whether the parties' agency characterization serves a function other than circumventing the law. *See* Restatement (Third) Agency, § 1.02, comment b; *Commissioner v. Bollinger*, 485 U.S. 340, 349-350, 108 S. Ct. 1173, 99 L. Ed. 2d 357 (1988) (it is reasonable for government agency "to demand unequivocal evidence of genuineness" of the agency relationship, including proof that the putative agent actually functions as agent and not principal for all purposes).

A. Evidence Cited by Morgan Drexen Does Not Establish an Agency Relationship.

Morgan Drexen correctly notes that memorializing an agency agreement in a contract is "one of the best ways to prove" the understanding that an agency relationship exists. (MD Response Brief, p. 13). Yet, aside from a rote recitation of the tasks Morgan Drexen was to perform under one of the contracts (MD Brief, p. 41), Respondent ignores the specific provisions of its contracts with attorneys and provides no analysis of how the contracts create a right for the attorneys to control Morgan Drexen.

Instead, Morgan Drexen contends that agency is shown because of the following: the agency relationship was disclosed to lawyer's debtor-clients and was referenced in correspondence that Howard sent to local counsel, was established by witness testimony, lawyers stopped using Morgan Drexen without losing clients, and a bankruptcy trustee entered into a support services agreement with Morgan Drexen. (MD Brief, pp. 38-48). These grounds are

largely immaterial to the question of whether attorneys had the right to control Morgan Drexen's debt settlement activities.

Much evidence cited by Respondent consists of generic, self-serving testimony by Morgan Drexen CEO Ledda and his attorney cohorts Stockinger, Williamson, and Howard. This testimony carries little probative weight. The witnesses testified without specificity, relying largely on blanket assertions that Morgan Drexen was the attorneys' agent and that the attorneys "supervised" Morgan Drexen. Their testimony contained contradictions on key points and often ran counter the express provisions of the contracts into which they entered. After closely observing these witnesses, it was apparent that they lacked credibility, and the veracity of their testimony is doubtful.⁶

The correspondence and contracts between the attorneys and debtors (as opposed to the contracts between the attorneys and Morgan Drexen which define their relationship and which Respondent disregards) do not establish that Morgan Drexen was an agent. Although attorneys sometimes referenced Morgan Drexen as their "administrative agent," other references merely

⁶ For instance, in an effort to support the notion that this debt settlement service was the brainchild of attorneys, Howard explained that he invited Williamson to work with him as a co-equal "engagement counsel" because they were friends. But, in the face of Williamson's contradictory testimony, Howard admitted that he did not even know Williamson before he asked him to help divide up the country for a nationwide debt settlement practice. When asked to explain why they agreed to split up the country, Howard could only respond, "I don't know." (Hr. Tr., pp. 731-732).

Likewise, it was difficult to believe Stockinger's testimony that the choice of law provision in her contracts with Wisconsin debtors was a "typo" when it specified that the law of the state of California would apply to a purported attorney-client relationship between a Wisconsin lawyer and a Wisconsin resident. (Hr. Tr., pp 380-381). The same choice of law provision states that the agreements are being "made and entered into in Cedarburg, Wisconsin," with the "typo" requiring the agreement to be construed "according to the laws of the State of California" appearing in every contract. (Joints Exs. 6a - 6e).

Although a full recital of the evidence would be improper, *see* Wis. Stat. § 227.47(1), it is appropriate to provide impressions of these witnesses because the agency must determine whether to accept or reject a hearing examiner's findings, and the agency, not the hearing examiner, is ultimately responsible for credibility determinations. *See Hakes v. LIRC*, 187 Wis. 2d 581, 523 N.W.2d 155 (Ct. App. 1994). Other examples where testimony proffered by Respondent lacked credibility and persuasiveness are noted in the Division's post-hearing briefs.

state that the attorneys were "supported by" Morgan Drexen or that Morgan Drexen was their service provider. These references are not conclusive as to agency, *see Sevey*, 235 Wis. 109, 112, and do not establish that the attorneys have the right to control Morgan Drexen's work.

That attorneys may have stopped using Morgan Drexen's services without losing their clients also does not establish a right of control. Whether Morgan Drexen acquiesced to the attorneys keeping their clients without utilizing Morgan Drexen, despite Respondent's contractual rights to service those clients, is not the pertinent issue. Nor is it material whether attorneys have input into the forms and contracts that Morgan Drexen utilized because Morgan Drexen still retains discretion to change those documents. Agency depends on the right of control; it is immaterial whether or not the right of control is exercised. *See Madix v. Hochgreve Brewing Co.*, 154 Wis. 448, 450-452, 143 N.W. 189 (1913); Restatement (Third) of Agency § 1.01 cmt. C.

Whether Morgan Drexen was hired to provide paralegal support for a bankruptcy trustee is irrelevant to whether Morgan Drexen was the agent for attorneys performing debt settlement services. Respondent touts this example to lend legitimacy to its visage of a paralegal support firm. But whether Morgan Drexen actually did act as a true paralegal in that single instance says nothing about whether Morgan Drexen was acting as an agent for attorneys when providing debt settlement services in Wisconsin.

Finally, it is undisputed that, before it began holding itself out as a service provider for attorneys, Morgan Drexen directly contracted with 37 Wisconsin debtors in 2007 to provide debt settlement services. Under even Morgan Drexen's reading of the statute, it was "engaged as principal" with respect to those 37 clients.

B. Attorneys Do Not Establish an Agency Relationship with Morgan Drexen.

In addressing whether Morgan Drexen was an agent, the parties disagree over the identity of the principal or principals. The Division argues that Stockinger is the only attorney licensed to practice law in Wisconsin, and because Respondent claims to be engaged in the practice of law subject to the sole jurisdiction of the Wisconsin Supreme Court, Stockinger should be the only attorney whose relationship with Morgan Drexen matters for determining agency.

Morgan Drexen claims that the Division is employing a “blindness tactic” by disregarding the out-of-state lawyers who purportedly supervise Morgan Drexen on Stockinger’s behalf:

The DFI attempts to justify this blindness tactic on the incorrect ground that only Wisconsin lawyers can practice law in Wisconsin, so only the contributions of a Wisconsin lawyer, i.e., Ms. Stockinger, can be relevant. That is not right. Mr. Williamson associated with Ms. Stockinger in providing services to Wisconsin clients. Hr’g Tr. 267–29 (Stockinger). As so associated, he is perfectly able to provide legal services in Wisconsin (see SCR 20:5.5)—lawyers from other states do so frequently. Ignoring the contributions of Mr. Williamson and Mr. Howard in setting up how Morgan Drexen provides outsourced support to lawyers cannot be reconciled with the right of any unlicensed lawyer to associate himself or herself with a locally licensed lawyer to practice law in Wisconsin.

(MD Response Brief, p. 16).

Morgan Drexen is wrong. There is no such thing as “the right of any unlicensed lawyer to associate himself or herself with a locally licensed lawyer to practice law in Wisconsin.” Practicing law in this state is a privilege, not a right. *See* Comment to SCR 23.02. SCR 20:5.5 significantly restricts the so-called “right to associate” that Respondent touts. The rule permits the provision of legal services by a lawyer not licensed to practice in this state when they are “undertaken in association with a lawyer who is admitted to practice in this jurisdiction and who actively participates in the matter.” SCR 20:5.5(c)(1). But, to comply with the rule, the legal services provided by the unlicensed attorney may occur only “on an occasional basis.” SCR 20:5.5(c).

The out-of-state attorneys purporting to “associate” with Attorney Stockinger are not doing so on an occasional basis. To the contrary, Respondent insists that these unlicensed attorneys are systematically and constantly supervising Morgan Drexen on Stockinger’s behalf. This could violate rules that prohibit an out-of-state attorney from maintaining “a systematic and continuous presence in this jurisdiction for the practice of law” or providing legal services on more than “an occasional basis” when “associated” with a Wisconsin lawyer. SCR 5.5(b)(1); SCR 5.5(c).

Perhaps concerned that their continuous presence in this state could be considered unauthorized practice of law, Attorneys Howard and Williamson were adamant that neither performed legal services with respect to Wisconsin clients. Williamson, “engagement counsel” to Stockinger’s “local counsel,” clarified that he only performed oversight over “non-legal” aspects of Morgan Drexen’s work. (Hr. Tr. pp. 253; Joint Ex. 111, p.114). The Wisconsin Supreme Court has no jurisdiction to regulate out-of-state attorneys who are not performing “legal services” in Wisconsin. *See* SCR 20:8.5(a).

Morgan Drexen’s argument is tautological. Crucial to Morgan Drexen’s defense is the notion that the Division is prohibited from regulating its business activities under Wis. Stat. § 218.02 because those activities are the practice of law controlled by attorneys who are subject to the sole purview of the Wisconsin Supreme Court. Respondent claims that the necessary right of control was held by Williamson and Howard and exercised on Stockinger’s behalf, and this control must be attributed to Stockinger because the out-of-state lawyers “associated” with her.⁷

⁷ It is not clear amongst Attorneys Stockinger, Williamson, and Howard, who was the “engagement counsel” for the clients that Stockinger served as local counsel. The only local counsel contract was between Stockinger and the Howard’s law firm. (Joint Ex. 4c). Stockinger, however, thought that she was on retainer with Williamson, and Williamson was apparently the only attorney with whom Stockinger associated as local counsel. (Joint Ex. 11k, p. 26). Williamson first testified that he was the engagement counsel for hundreds of Wisconsin

But, the out-of-state attorneys who claim to fulfill the role of principal also claim to not be providing any legal services in this state, so they are not subject to the Wisconsin Supreme Court's jurisdiction. Respondent's position cannot co-exist with itself.

Nonetheless, accepting Morgan Drexen's position leads to the same result. The contractual arrangements and practices of Morgan Drexen and its affiliated attorneys do not establish an agency relationship even considering the roles of Howard and Williamson because neither of those attorneys had the right to control Morgan Drexen. *Cf. Scally v. Hilco Receivables, LLC*, 392 F. Supp. 2d 1036, 1040-1041 (N.D. Ill. 2005) (right of control was not established by the fact that alleged principal to a debt collection agency had monthly conference calls and daily and weekly email communications with the agency, reserved final approval for any settlements at less than 80 percent of the debt owed, and had control over the reporting of its debtors' debt to credit reporting agencies).

After its initial foray providing debt settlement services directly to Wisconsin residents, Morgan Drexen re-classified itself as a paralegal and administrative support firm. It entered into a series of contracts with the attorneys, with later contracts modifying the terms of their relationship but never vesting the attorneys with a right to control Morgan Drexen. Notably, none of these contracts state that Morgan Drexen is to serve as agent to the attorneys or would have any fiduciary obligations to the attorneys or their clients.

clients until 2009, at which point he withdrew and Stockinger became engagement counsel. After a break in his deposition where he consulted with Morgan Drexen's attorney, Williamson changed his testimony and said that he was still engagement counsel for the Wisconsin clients that Stockinger served as local counsel. (Joint Ex. 11j, pp. 149, 161-162).

When Stockinger acts as “local counsel” under her retainer letter with Attorney Howard, “engagement counsel” Williamson has a written agreement with Morgan Drexen.⁸ (Joint Exs. 4e; 11i, Exs. 3, 6). The contracts declare that the attorneys would “supervise” Morgan Drexen but no meaning is attached to this term and the contracts expressly prohibit attorneys from supervising the activities of Morgan Drexen personnel. The substantive provisions of these agreements do not confer a right of control on the attorneys:

- a. The contract was the final and entire expression of the agreement between the parties and could only be modified in writing;
- b. With respect to “debt resolution and bankruptcy services”, the lawyers agreed to subordinate their independent judgment to the provisions of the contract, and would only exercise independent judgment when engaged in the “practice of law”;
- c. The lawyers would “supervise” Respondent’s work, but Morgan Drexen retained the sole right to “manage the employment and internal supervision of its own administrative staff and other employees without [the lawyer’s] supervision, interference, or control”;
- d. A “Quality Control Questionnaire” was mandated for performing client intake , which Morgan Drexen produced “at its own expense, with its own experience” and which Morgan Drexen could modify at its own discretion;
- e. Morgan Drexen granted the lawyers non-transferable rights to access and use Morgan Drexen’s proprietary computerized communication and case management system, with the lawyers agreeing to maintain the confidentiality of this proprietary information;

⁸ Although Stockinger became an “engagement counsel” directly with Morgan Drexen in 2009, she apparently still serves today as Williamson’s “local counsel” for any clients that signed up for the debt settlement services before Stockinger was elevated to “engagement counsel.” (Joint Ex. 11j, pp. 149, 161-162).

- f. Morgan Drexen would produce marketing and advertising materials, subject to the lawyers' approval, to promote the debt settlement services. The contract also provided that Morgan Drexen would have to approve the business name of the attorney to be advertised;
- g. Morgan Drexen retained the "sole discretion" to provide services under the contract through any entity it deemed appropriate;
- h. Morgan Drexen retained the right to "change the method, manner of, and procedures for 'non-legal' servicing clients, requiring only notice to and not approval by the lawyer. The lawyers were also required to give "great weight and deference to any procedural recommendations" made by Morgan Drexen and had to adopt those recommendations "if reasonable";
- i. In the event that the lawyer terminated the contract with Morgan Drexen prior to its expiration, all payments due to Morgan Drexen would become immediately due and payable and would constitute a lien against any fees generated from clients;
- j. The lawyer was obligated to provide timely cooperation to Morgan Drexen;
- k. Provided that certain criteria in the contract were met, Morgan Drexen had the right to assign its contract with the lawyers to any third party without the lawyer's approval;
- l. The lawyer was only permitted to assign its rights under the contract with Morgan Drexen's approval;
- m. Morgan Drexen was granted a security interest in its share of any monies paid by the debtor-clients.

(Id).

In June 2009, Stockinger was hired by Morgan Drexen to serve as “engagement counsel” for Wisconsin debtors serviced by Morgan Drexen. Stockinger’s lack of control is more pronounced under this agreement; the contract plainly grants Morgan Drexen the right of control:

- a. The contract was the final and entire expression of the agreement between the parties and could only be modified in writing;
- b. Morgan Drexen agreed to compensate Stockinger for her “supervision and approval of client debt settlements” a minimum of \$1,000 monthly for the first 300 clients and an additional \$2.50 for each client over 300, and an additional \$500 per month for “managerial supervision over other counsel and for marketing advice”;
- c. “The ‘Poison Pill’ Provision” required Stockinger to pay Morgan Drexen \$1,100 “for each debtor under management in the event STOCKINGER chooses to compete with [Morgan Drexen] and takes clients previously serviced by [Morgan Drexen]”;
- d. With respect to “debt resolution and bankruptcy services,” Stockinger agreed to subordinate her independent judgment to the provisions of the contract, and would only exercise independent judgment when engaged in the “practice of law”;
- e. Stockinger was required to give “great weight and deference” to any procedural changes recommended by Morgan Drexen and to adopt those changes if reasonable;
- f. Stockinger would “supervise” Morgan Drexen’s work, but Morgan Drexen retained the sole right to “manage the employment and internal supervision of its own administrative staff and other employees without [the lawyer’s] supervision, interference, or control”;
- g. A “Quality Control Questionnaire” was mandated for performing client intake, which Morgan Drexen produced “at its own expense, with its own experience”. Morgan Drexen

could modify the questionnaire at its own discretion but Stockinger could not modify anything without Morgan Drexen's approval;

h. Stockinger was not permitted to "directly or indirectly ignore, circumvent, or nullify any disclaimer" prepared by Morgan Drexen;

i. Stockinger could not disapprove or prohibit the dissemination of the marketing and advertising materials produced by Morgan Drexen unless there was "cause," defined in the contract as "copy or images that would be deemed deceptive, unfair, inflammatory, derogatory, indecent, or inconsistent with permissible advertising under Wisconsin Bar rules;

j. The contract also provided that Morgan Drexen would have to approve the business name of the attorney to be advertised;

k. Morgan Drexen retained the "sole discretion" to provide services under the contract through any entity it deemed appropriate;

l. Morgan Drexen retained the right to "change the method, manner of, and procedures for 'non-legal' servicing clients, requiring only notice to and not approval by the lawyer. The lawyers were also required to give "great weight and deference to any procedural recommendations" made by Morgan Drexen and had to adopt those recommendations "if reasonable";

m. In the event that the lawyer terminated the contract with Morgan Drexen prior to its expiration, all payments due to Morgan Drexen would become immediately due and payable and would constitute a lien against any fees generated from clients;

n. The lawyer was obligated to provide timely cooperation to Morgan Drexen;

o. Provided that certain criteria in the contract were met, Morgan Drexen had the right to assign its contract with the lawyers to any third party without the lawyer's approval;

p. The lawyer was only permitted to assign its rights under the contract with Morgan Drexen's approval;

q. Morgan Drexen was granted a security interest in its share of any monies paid by the debtor-clients.

(Joint Ex. 4d).

In January 2011, Stockinger signed a new contract to act as "engagement counsel." This iteration removed some of the most obvious examples of how Morgan Drexen controlled the relationship, including eliminating the "poison pill" clause and the provision indicating that Morgan Drexen would pay Stockinger for her "supervision" rather than Stockinger paying Morgan Drexen to provide services to her.⁹ But it still suffers from the same infirmities as Williamson and Howard's contracts, preserving Morgan Drexen's principal role in providing debt settlement services and granting Morgan Drexen discretion in performing those services without supervision by Stockinger. (Joint Ex. 4f).

The Division's expert aptly characterized this relationship as one where "the nonlawyer assistant tail emphatically waves the lawyer dog." (Joint Ex. 13, p. 7). His opinion that the attorneys in the Morgan Drexen debt settlement program do not and cannot exercise a meaningful right of control is well founded. Substantial evidence supports the Division's position that Morgan Drexen is not the lawyers' agent, that Morgan Drexen is the principal, and that Morgan Drexen's attorney model is, both in execution and intention, a pretense designed to evade regulation under Wis. Stat. § 218.02.

⁹ Morgan Drexen handles all receipts and distributions of client funds and performs all of the accounting of these funds, so the characterization of who pays whom is a rhetorical distinction that is easily manipulated and completely within Morgan Drexen's control. Even Stockinger testified that the labeling of these fees and expenses was "semantics." (Joint Ex. 11k, p. 175).

IV. IT IS CONSTITUTIONAL TO APPLY WIS. STAT. § 218.02 TO MORGAN DREXEN.

The final issue to be considered is Respondent's affirmative defense that applying the adjustment service company law to Morgan Drexen is an unconstitutional violation of separation of powers. This defense rests on the notion that Morgan Drexen acts as a paralegal support firm for attorneys engaged in the practice of law. According to Respondent, the Wisconsin Supreme Court has sole jurisdiction over the practice of law, and applying Wis. Stat. § 218.02 to lawyers and their paralegals imposes an unconstitutional encroachment on that judicial power.

Respondent devotes considerable effort to defending attorneys' use of out-of-state paralegal support firms and what it deems the unlimited "right" of unlicensed attorneys to "associate" with lawyers in this state and perform legal services in Wisconsin. But, the Division does not quarrel with the notion that lawyers may permissibly outsource paralegal support or that out-of-state attorneys may work with local counsel to provide legal services to Wisconsin clients. Rather, the Division charges that Morgan Drexen's paralegal service is a façade that masquerades an adjustment service company as the practice of law in order to evade regulation under Wis. Stat. § 218.02.

A. Morgan Drexen's Debt Settlement Services Do Not Require a License to Practice Law.

Adjustment service companies operating pursuant to Wis. Stat. § 218.02 do not need to be licensed as attorneys regardless of whether their activities fall under the strict definition of the practice of law. The Wisconsin Supreme Court defines the "practice of law" as the "application of legal principles and judgment with regard to the circumstances or objectives of another entity or person(s) where there is a client relationship of trust or reliance and which require the knowledge, judgment, and skill of a person trained as a lawyer." SCR 23.01. The practice of

law includes but is not limited to the “[n]egotiation of legal rights or responsibilities on behalf of another entity or person(s).” *Id.*

As *JK Harris* makes clear, the adjustment service company law applies to companies who negotiate on behalf of debtors to reduce their obligations to creditors. Adjustment service companies do not need to be attorneys to perform this service, suggesting that prorating activities do not require the “application of legal principles and judgment” or the “knowledge, judgment, and skill of a person trained as a lawyer.”¹⁰ Although Morgan Drexen performed all of the essential tasks of the debt settlement service, Morgan Drexen did not provide any legal services to the debtors. [Hr.Tr. pp. 94, 188; Joint Ex. 11k, pp. 87, 90).

Stockinger’s “supervision” and “approval” of Morgan Drexen’s debt settlement activities does not evince these principles enumerating the practice of law. Stockinger displayed a rather astonishing lack of knowledge about Morgan Drexen and the clients assigned to her. Stockinger did not recognize her own client’s names and struggled to identify the names of Morgan Drexen employees with whom she had worked. (Joint Ex. 11k, pp. 67, 79, 81, 85-86, 162-165). Perhaps this should not be surprising because she only spends about 20 hours per week servicing approximately six hundred Morgan Drexen clients. (Joint Ex. 11k, pp. 25; Hr. Tr., p. 285) Wisconsin debtors in the Morgan Drexen program uniformly testified that they thought that Morgan Drexen was settling their debts; never spoke or corresponded with an attorney, and did not even understand that they were represented by an attorney. (Hr. Tr., pp. 373-374; 604-605, 632-635, 646-650, 669-670, 673).

¹⁰ Respondent asserts that “Wisconsin law is clear” that “the compromise of the debtor’s obligation to his or her creditor is the practice of law”, citing *State ex rel. Junior Ass’n of Milwaukee Bar v. Rice*, 236 Wis. 38, 56, 294 N.W. 550 (1940). The case says the opposite. While the Court noted a number of activities would constitute the unauthorized practice of law if conducted by insurance adjusters, one activity which the Wisconsin Supreme Court notably found *did not* constitute the practice of law was [n]egotiating settlements or adjustments for or on behalf of insurance companies with others in a representative capacity.” *Id.* at 55.

Morgan Drexen, not Stockinger, has specialized knowledge of the credit industry, including knowledge of the timing and circumstances in which creditors are willing to accept reductions in the debt owed. This knowledge is “secret” and “proprietary” to Morgan Drexen and is not shared with Stockinger. (Joint Ex. 11k, p. 177). In “approving” the settlements negotiated by Morgan Drexen, Stockinger usually has no idea why or how the settlement was reached. Settlement approval occurred through an Internet-based portal where the attorney could simply click a button to indicate approval. Stockinger would approve the settlement if it looked “reasonable” to her. (Hr. Tr., pp. 373-374). However, if an attorney in the Morgan Drexen program does not respond to the settlement proposal within 24 hours, it is deemed automatically approved. (DFI Rebuttal Ex. 5d).

Morgan Drexen’s conception of the practice of law reduces lawyers to automated cogs in a nationwide debt settlement machine. That is completely inconsistent with the control necessary to make an attorney the principal, much less an attorney’s ethical obligations to provide zealous advocacy on behalf of clients. To the extent to which these debt settlement activities constitute legal services, substantial evidence shows that those services are performed by Morgan Drexen without meaningful supervision by Stockinger or any other attorney practicing law in Wisconsin.

This raises the question of whether Morgan Drexen is engaged in the unauthorized practice of law. The definition of the practice of law could include any adjustment service company because negotiating debt settlements on behalf of a debtor is obviously the “[n]egotiation of legal rights or responsibilities on behalf of another entity or person(s).” But, SCR 23.01 cannot be read in isolation because the rule exempts numerous activities from licensure by the Wisconsin Supreme Court. See SCR 23.02(2). At least one exception is

directly applicable here, exempting “[a]ny other activities that the Supreme Court has determined by rule or by published opinion do not constitute the unlicensed or unauthorized practice of law or which are permitted under a regulatory system established by the Supreme Court, Wisconsin Statutes, Administrative Code or common law.” SCR 23.02(2)(k) (emphasis added).

It is apparent that the Wisconsin Supreme Court was concerned that creating a specific and uniform definition of the practice of law would disturb a number of regulatory systems already in place. As SCR 23.02(2) reflects, numerous activities not previously regulated by the Supreme Court would have otherwise been swept up when the Court established a uniform definition for the first time in 2011. SCR 23.02(2) addresses that concern by exempting those activities from licensure by the Supreme Court.

The negotiation and settlement of debts by non-attorneys is permitted subject to a regulatory system established under Chapter 218, Wis. Stats. Thus, regardless of whether prorating activities meet the technical definition of the practice of law, those activities do not require licensure or oversight by the Supreme Court and may be regulated by the Division. Arranging for attorneys to act as a front for the adjustment service company does not transform those regulated activities into the practice of law.

B. Applying Wis. Stat. § 218.02 to Morgan Drexen Does Not Violate the Separation of Powers Doctrine.

Respondent argues that Wis. Stat. § 218.02 is an unconstitutional violation of separation of powers as applied to Morgan Drexen. Although an administrative tribunal has no power to declare a statute facially unconstitutional, it does have authority to determine whether the law is constitutionally applied in a given case. *Metz v. Veterinary Examining Bd.*, 2007 WI App 220, ¶ 21, 305 Wis. 2d 788, 741 N.W.2d 244.

The doctrine of separation of powers is implicit in the division of governmental powers among the judicial, legislative and executive branches. *State ex rel. Friedrich v. Circuit Court*, 192 Wis. 2d 1, 12-13, 531 N.W.2d 32 (1995). Each branch has a core zone of exclusive authority into which the other branches may not intrude. *Id.* However, this rule is not strict and absolute, because “the doctrine envisions a system of separate branches sharing many powers while jealously guarding certain others, a system of “separateness but interdependence, autonomy but reciprocity.” *Id.*

If a statute falls within the judiciary's core zone of exclusive authority, the court may abide by the statute if it furthers the administration of justice, “as a matter of comity or courtesy rather than as an acknowledgement of power.” *Id.* at 13-14 (citation omitted). “Thus the court acknowledges the legislature's power to declare itself on questions relating to the general welfare and the court complies with the legislature's declared policy as long as the policy aids but does not obstruct “the court in its own exclusive sphere.” *Id.* at 14 (citations omitted). “A statute within the area of power shared by the two branches, yet outside of the judiciary's exclusive authority, will be constitutional only if it does not unduly burden or substantially interfere with the judicial branch.” *Id.*

Wis. Stat. § 218.02 makes no exception for attorneys or their service providers, and it would be folly to imply such exemption as Respondent urges. If the legislature wanted to exempt attorneys, it certainly would have included such exemption as it does elsewhere in Chapter 218. See Wis. Stat. § 218.04(1)(a) (exempting attorneys at law authorized to practice in this state from the definition of a collection agency); see also *Georgina G.*, 184 Wis. 2d 492, 511-512 (statutes in the same chapter must be read *in pari materia*). Reading an exception into the statute where none exists would be legislating not judging.

The legislature's authority in this area is well established: it has the power to enact legislation for the general welfare and to require occupational licensing and regulation for the protection of consumers. See *State ex rel. Friedrich*, 192 Wis. 2d 1, 15 (concluding that the legislature shares power with the judiciary in setting compensation for court-appointed attorneys); *Laufenberg v. Cosmetology Examining Board of Wisconsin Dep't of Regulation & Licensing*, 87 Wis. 2d 175, 184-185, 274 N.W.2d 618 (1979) (occupational licensure and regulation). Wis. Stat. § 218.02 is thus a proper exercise of the legislature's authority. The only question is whether that exercise of authority unduly encroaches upon judicial power.

Given the factual findings underlying this decision, it is questionable whether the judiciary has any authority to regulate Morgan Drexen's activities.¹¹ As noted, the out-of-state attorneys claim to not be providing legal services in Wisconsin, and there is no substantial evidence to the contrary. (Hr. Tr. pp. 253; Joint Ex. 111, p.114). Moreover, Respondent affirms that Stockinger was never Morgan Drexen's principal while she served as local counsel between 2007 and 2009. (MD Response Brief, p 16, n. 5). In light of these admissions, there is no basis by which the Wisconsin Supreme Court could assert jurisdiction over Morgan Drexen's activities during that period. And, given her lack of control over Morgan Drexen and the dearth of activity by Stockinger which could be reasonably characterized as applying legal principles and judgment, it does not appear that there is any attorney in Morgan Drexen's debt settlement program who is providing legal services in Wisconsin.

Morgan Drexen suggests the practice of law occurs through its negotiation strategy of preparing a bankruptcy petition for a debtor-client and sending it to creditors to persuade them

¹¹ This is not to say that the Supreme Court cannot regulate Attorney Stockinger for her activities and association with Morgan Drexen. As an attorney licensed in Wisconsin, Stockinger is accountable to the Wisconsin Supreme Court for her overall conduct. Stockinger is not a party to these proceedings and this decision does not address whether she can be personally regulated by the Division.

that the debtor is judgment proof. But, the debt settlement contracts do not allow for the provision of bankruptcy services, and a client must enter into an additional contract with an attorney before any bankruptcy petition is filed or any bankruptcy services are provided. (Joint Exs. 11b, pp. 202-203; 11k, pp. 132-135; Hr. Tr., pp. 326-329). Sending a mock bankruptcy petition to a creditor is not the practice of law. Nor is it clear what purpose this tactic serves other than to impart the veneer that legal services are being provided.

However, even assuming that these debt settlement services fall within an ambit of authority shared by the judiciary, applying Wis. Stat. § 218.02 to Morgan Drexen does not unduly burden or substantially interfere with the judicial branch. *Cf. Brown v. Consumer Law Assocs., LLC*, 283 F.R.D. 602, 609 (E.D. Wash. 2012) (applying Washington's debt adjustment act to attorneys does not violate the separation of powers doctrine and is no different than applying criminal laws to lawyers). Morgan Drexen's contrary position is poorly developed and unpersuasive.

Morgan Drexen contends that administrative code provisions limiting the time for retaining debtors' funds and distributing them to creditors conflicts with its debt settlement model which requires debtors to make payments into escrow until a sufficient amount has accrued to spur settlement discussions with creditors. See Wis. Admin. Code DFI-Bkg § 73.03(7). Respondent does not argue that this administrative code provision conflicts with a Supreme Court Rule, but only that it conflicts with Morgan Drexen's business model. That does not mean that the adjustment service company law imposes an undue encroachment on judicial authority. It means that Morgan Drexen's business model is illegal in Wisconsin.

Respondent also argues that the Division's powers under Wis. Stat. § 218.02 to examine an adjustment service company's records conflicts with the attorney-client privilege. But,

Respondent points to no instances where the Division has insisted on reviewing privileged materials. To the contrary, both before and during these proceedings, the Division has acquiesced to Respondent's assertions of privilege. Nor does the Division's examination of Respondent's accounting of debtor funds and the fees paid to Morgan Drexen or attorneys conflict with the attorney-client privilege. See *Dyson v. Hempe*, 140 Wis. 2d 792, 819, 413 N.W.2d 379 (Ct. App. 1987) ("...a lawyer-client privilege does not attach to communications between the client and the lawyer respecting fees.").

Morgan Drexen also contends that the adjustment service company law imposes a conflict of interest on attorneys because the administrative code limits the fees that may be charged debtors to \$120 per month. Respondent contends that this will incentivize attorneys to delay settlements in order to charge as much as possible.¹² Yet, that same incentive is already inherent in Morgan Drexen's current model, with Respondent charging monthly fees for its services on top of a variety of other fees. A cap on those monthly fees doesn't change the nature of the incentive; it only limits the harm a dishonest practitioner can inflict on the debtor. And while Morgan Drexen's more lucrative fee structure admittedly provides incentives for lawyers to violate their ethical and fiduciary obligations, it is much harder to believe that a lawyer would risk disbarment and criminal prosecution to defraud a client of \$120 per month.

Morgan Drexen also states that the fee limitation conflicts with Supreme Court rules governing the reasonableness of attorney fees. Respondent devotes scant analysis to this argument in two post-hearing briefs comprising 145 pages, so it is not clear how Respondent believes there to be a conflict. (MD Brief, p: 75). The Wisconsin Supreme Court has held that

¹² Attorneys' ethical obligations of diligence and truthfulness and their fiduciary duties to their clients are apparently of no consequence in Respondent's judgment.

authority to regulate an attorney's compensation is a power shared by both the legislature and the judiciary. *See State ex rel. Friedrich*, 192 Wis. 2d 1, 15. That case presented a more compelling argument than here because it concerned the permissible compensation of attorneys appointed by the court. *Id.*

Finally, Respondent's argues that the Division's regulation of Morgan Drexen makes it impossible for the attorneys to provide "debt settlement legal services" in Wisconsin. According to those attorneys, they cannot provide these services without Morgan Drexen's proprietary knowledge and computer program and their administrative capabilities to service hundreds of clients for a single lawyer. But, those attorneys' inability to cost-effectively provide debt settlement services in accordance with the statute does not transform those services into the practice of law. Nor does Respondent argue that any rules of professional conduct encourage an individual lawyer to spend only 20 hours per week in service of 600 individual clients.

And, this underscores the control that Morgan Drexen wields in the relationship. Morgan Drexen is functionally capable of providing debt settlement services legally without attorneys, as delineated above and evidenced by its direct contracting with 37 Wisconsin debtors when it first began operating in this state. While the attorneys may need Morgan Drexen to perform all of the essential tasks of these debt settlement services, the only reason why Morgan Drexen needs attorneys is to shield itself from otherwise applicable regulations.

Respondent accuses the Division of holding a "contrived worldview" by refusing to recognize Morgan Drexen as the paralegal support firm it claims to be. Respondent insists that its debt settlement "legal services" model is unique and differentiates Morgan Drexen from other businesses performing debt settlement services. But that is not true. Courts and commentators alike have observed that Morgan Drexen is a "prototypical debt settlement company" and but

one of many who has employed an “attorney model” in an effort to evade regulation. *See, e.g., HSBC Bank Nev., N.A. v. Cournoyer*, 2013 R.I. Super. LEXIS 16, 17-18 (R.I. Super. Ct. 2013) (citing Civil Court and Consumer Affairs Committees, N.Y.C. Bar Association, Profiteering From Financial Distress: An Examination of the Debt Settlement Industry 1 at 70, 150 (May 2012)).¹³

I am mindful that the Division has applied Wis. Stat. § 218.02 to Wisconsin law firms and that such action does raise legitimate concerns if those lawyers are engaged in the practice of law, have a primary role in performing debt settlement activities, and have the right to control subordinates performing any such activities under their supervision. It may be that applying the statute in that instance is a bridge too far. But, that is not this case. This decision is limited to the facts adduced which demonstrate that Morgan Drexen is a non-agent adjustment service company engaged in a deceptive and pernicious form of jurisdictional arbitrage.

V. SANCTIONS REQUESTED BY THE DIVISION ARE PERMISSIBLE AND APPROPRIATE

As remedies for Morgan Drexen’s violations of the adjustment service company law, the Division seeks an order imposing forfeitures in the amount of \$1,000.00 per violation and requiring Morgan Drexen to disgorge the fees it has collected from Wisconsin debtors. Morgan Drexen, of course, opposes this request in its entirety. For the following reasons, the Division’s request for forfeitures is granted in the amount of \$1,890,000.00 and Morgan Drexen is further ordered to disgorge fees as restitution to Wisconsin debtors in the amount of \$4,253,081.93.

¹³ The NYC Bar Association White Paper is available at: <http://www2.nycbar.org/pdf/report/uploads/DebtSettlementWhitePaperCivilCtConsumerAffairsReportFINAL5.11.12.pdf> (last visited April 17, 2013).

A. The Division's Request for Disgorgement is Granted.

Respondent contends that the Division has no authority to order disgorgement of fees under its authority to "correct the conditions" resulting from violations of the adjustment service company law. Morgan Drexen relies on *Larimore v. Comptroller of Currency*, 789 F.2d 1244, 1250-51 (7th Cir. 1986) for the proposition that the power to "correct the conditions" resulting from a legal violation does not include the power to order disgorgement. *Larimore* is factually inapposite and statutorily distinct from the case at bar.

In *Larimore*, the federal Comptroller of Currency sought to impose personal liability and damages against an individual director of a banking institution under its authority to "correct the conditions" resulting from statutory violations pursuant to 12 U.S.C. § 1818. The Comptroller sought to impose such damages even though the statute specifically permitted damages to be assessed only in the event that liability was determined by a district court and despite the fact that the individual director was not personally enriched by the violations. 789 F.2d 1244, 1248-49. After scrutinizing the legislative history, the Seventh Circuit found that the Comptroller's power to "correct the conditions" could not otherwise permit such penalties in light of the statutory scheme. Notably, the Seventh Circuit's analysis was rejected by other circuits and ultimately Congress, who found that the authority to order disgorgement was implied by an agency's power to correct conditions. See *del Junco v. Conover*, 682 F.2d 1338 (9th Cir.1982), cert. denied, 459 U.S. 1146, 103 S. Ct. 786, 74 L. Ed. 2d 993 (1983) (finding that the power to "correct the conditions" permitted the Comptroller to recover monies from bank officers when the bank has suffered losses as a consequence of the officer's actions); *Hoffman v. Federal Deposit Ins. Corp.*, 912 F.2d 1172, 1174-1175 (9th Cir. 1990); accord *First Nat'l Bank v. Department of Treasury, Office of Comptroller of Currency*, 568 F.2d 610, 611 (8th Cir. 1978)

(per curiam); see also *Akin v. Office of Thrift Supervision Dep't of Treasury*, 950 F.2d 1180, 1184 (5th Cir. 1992) (“Congress expressly rejected the narrow interpretation of § 1818 given by the Seventh Circuit.”).

The instant action does not seek to impose monetary damages against an individual who was not personally enriched and who was not proven to have committed wrongdoing. After providing full process and demonstrating violations with substantial evidence, the Division seeks disgorgement of fees illegally charged by Morgan Drexen. This is an appropriate exercise of the Division’s power to limit fees that an adjustment service company may charge and duty to enforce the law by correcting the conditions resulting from violations of those limits.

Unlike the Comptroller in *Larimore*, which was restricted to correcting unsafe and unsound banking practices, the Division has more expansive powers to protect Wisconsin debtors from deceptive and oppressive practices and to establish the maximum fees that adjustment service companies may charge. Wis. Stat. § 218.02(7). Concurrent with these powers is the ability to “correct the conditions resulting from the violation” of Wis. Stat. § 218.02. Wis. Stat. § 220.04(9)(d). As a creature of the legislature, the Division has such powers as the legislature expressly confers upon it and those that are necessarily implied by the statutes under which it operates. *Racine Fire & Police Com. v. Stanfield*, 70 Wis. 2d 395, 399, 234 N.W.2d 307 (1975). The Division’s power to correct the conditions resulting from the charging of illegal fees would be meaningless if it lacks the authority to order those fees disgorged. As such, the Division’s power to order restitution is necessarily implied by the statute, and the Division’s disgorgement remedy is an appropriate exercise of these powers.

The Division requests that the entirety of the fees paid by Wisconsin debtors be disgorged. Morgan Drexen argues that only its share of fees could be subject to disgorgement

and that the Division has not proven the specific amounts that went to Morgan Drexen and to the attorneys who are not parties to this administrative action. This is a disingenuous argument because Morgan Drexen is the only one who possesses that information, and it has refused to produce it.

Morgan Drexen protests that it cannot tell the Division how much of the fees from Wisconsin debtors it retained. Morgan Drexen asserts that "Morgan Drexen charged lawyers for services generally, rather than on a lawyer-client, by lawyer-client basis [sic] for scores (or more) of clients. It did not present lawyers with a separate invoice or line item for time devoted to each of the lawyer's clients." (MD Response Brief, p. 60). This is not true because Morgan Drexen, for at least a couple years, indisputably contracted to pay Stockinger rather than the other way around. It is also untrue if one accepts Respondent's own proposed finding of fact, which states that:

For most services, Morgan Drexen charges the lawyer for the time spent on the client's file or for the task performed for the client. Morgan Drexen's systems require its employees to record all activity on behalf of a law firm's client into the automated client file. Phone calls, document uploading, mailings, and other activities are recorded in their duration or amount in the client file to which they relate. Morgan Drexen's system tallies the charges incurred for each lawyer's client and invoices lawyers for these services.

(MD Brief, p. 18) (record citations omitted).

Prior to hearing, the Division brought a motion to compel production of the fee distribution. The undersigned hearing officer denied the motion because Morgan Drexen represented that it did not possess the information and would have to re-engineer its entire database at the cost of hundreds of employee hours to produce it. With the benefit of a hearing and fuller understanding of Morgan Drexen's operation, that representation appears misleading and implausible.

The information needed to assess the total fees retained by Morgan Drexen does not depend on a breakdown by each client, and it is simply not credible that Morgan Drexen's sophisticated personnel and computer systems could not readily produce an accounting of the fees that it retained from Wisconsin debtors. Morgan Drexen received all of the funds from debtors, made all transfers of those funds between and among accounts shared with the attorneys and performed all of the accounting of those funds for Stockinger. Simply deducting the amounts that were distributed to Stockinger from the total amount billed to all Morgan Drexen clients that she claims to represent would provide the answer.

Morgan Drexen's inability to produce this simple answer confirms what the Division has already proven: Morgan Drexen-affiliated attorneys are not practicing law and have no control over Morgan Drexen's activities. Respondent claims that it directly charges the lawyers rather than the clients and does not differentiate by each client but instead bills in client batches of "scores (or more)." (MD Response Brief, p. 60). Yet, Morgan Drexen is performing the near-entirety of debt settlement services for these clients, and those charges are passed on directly to the clients. (Joint Ex. 11k, p. 105 (Stockinger affirming that charges for Morgan Drexen's debt settlement services are passed on to the clients)).

If Morgan Drexen cannot provide the attorneys with a breakdown of the fees it charged, then attorneys practicing law cannot comply with their ethical obligations to ensure that such fees are reasonable or even that the services for which Morgan Drexen charged were actually performed. Attorneys may only charge reasonable fees, and such reasonableness depends upon the context in which the fees are charged, including both the amounts involved and the results obtained. SCR 20:1.5(a). An attorney cannot charge a blanket fee of every client regardless of those clients' individual circumstances, the amount of time needed to secure each client's

objectives, or the outcome achieved for the client. *Id.* A lawyer's clients are not widgets to be batch processed on an assembly line.

Regardless of whether Morgan Drexen disseminated a portion of fees to attorneys, the full measure of fees paid by the debtors is the appropriate measure of restitution. Restitution and disgorgement are equitable remedies, and equity cannot be defeated by accounting gimmicks. Where the value of the benefit retained by a recipient who wrongly obtained the funds is less than the amount conferred by the victim, the loss to the victim is the appropriate measure of restitution. See Restatement (Third) of Restitution and Unjust Enrichment, §§ 52(2)(b); 49 comment e. (2011). Thus, the full amount of fees that were illegally charged of Wisconsin debtors is the correct amount to be disgorged.

B. The Division's Request for Forfeitures is Granted.

The Division requests an order imposing forfeitures in the amount of \$1,000.00 per violation, and argues that there is at least one violation per each debtor that Morgan Drexen enrolled in its program. A total of 1,890 Wisconsin debtors enrolled in the Morgan Drexen program between April 26, 2007 and January 31, 2012.¹⁴

Morgan Drexen argues that there is "no basis" in the statutes to permit such forfeitures. Respondent's argument is confused and borders on frivolous. First, Respondent asserts that the requested forfeiture "would impermissibly offend the maximum fine limit in § 218.02(10)," so any forfeiture must be limited to the \$500 permitted under that subsection. Wis. Stat. § 218.02(10) enumerates criminal penalties that may be imposed for violations of Chapter 218,

¹⁴ The Division's post-hearing brief mistakenly states that there were only 986 debtors. This figure was derived from an analysis of Morgan Drexen's records by Jean Plale, the Director of the Bureau of Licensed Financial Services within the Division of Banking. In her analysis, Ms. Plale stated that there were 986 debtors enrolled in the program from the period of January 6, 2009 to May 20, 2011. The total amount of Wisconsin debtors serviced by Morgan Drexen for the entire time period are listed in a different section of her report and broken down by year, totaling 1,890 debtors. (See Plale Testimony, Questions 44-46, 55).

including imprisonment. Corporations cannot be imprisoned, so this section has no applicability to Morgan Drexen as an entity. The Division's authority to assess forfeitures against adjustment service companies is completely independent of that subsection, which Morgan Drexen contradictorily acknowledges on the same page of its brief. (See MD Response Brief at p. 61).

Under Wis. Stat. § 220.04(9)(d), the Division may issue a cease and desist order against any "regulated entity" and order the entity to correct the conditions resulting from the violation or practice. As part of the order, the Division may impose a forfeiture of up to \$10,000 for each violation. Wis. Stat. § 220.04(9)(f)1. A "regulated entity" subject to forfeitures includes an adjustment service company. See Wis. Stat. § 220.04(9)(a)1; Wis. Stat. § 220.02(2)(b).

Unquestionably, the Division has authority to impose the forfeitures it seeks.

Next, Respondent offers an abbreviated argument relying on inapposite cases to proclaim that imposing forfeitures would be "unconstitutionally excessive."¹⁵ (MD Response Brief at pp. 61-62). At first, Morgan Drexen suggests that any forfeiture in excess of \$500 would be impermissible, but then claims that a forfeiture exceeding \$1,000 would offend the constitution. (*Id.*) It is thus not clear what amount of forfeiture the Division could constitutionally impose under Respondent's view. Morgan Drexen makes no attempt to address the factors governing a constitutionally excessive forfeiture and offers no analysis to support its position. The argument cannot be addressed because it is not clear what Morgan Drexen is arguing.

¹⁵ Other than generally stating the premises that Respondent contends support its constitutional argument, the two cases cited by Morgan Drexen are completely off point. In *Wis. Bell, Inc. v. PSC*, 2003 WI App 193, 267 Wis. 2d 193, 670 N.W.2d 97, the Court of Appeals held that the Public Service Commission could not seek forfeitures because it was not authorized to do so by the statutes. The Division is authorized to seek forfeitures so the case is inapposite. In *Wisconsin v. Bergquist*, 2002 WI App 39, 250 Wis. 2d 792, 641 N.W.2d 17, the Court found that the state did not refute the defendant's argument that the forfeiture of his firearms was unconstitutional so the argument was deemed admitted without any substantive analysis. Although *Bergquist* enumerates the factors for determining an excessive forfeiture, Respondent does not address them anywhere in its voluminous briefs.

Finally, Respondent claims that “the only conceivable statutory provision Morgan Drexen could have violated is the requirement that adjustment service companies obtain a license.” (MD Response Brief at p. 61). In Morgan Drexen’s view, this means that there could have been only a single violation subject to a maximum forfeiture of \$10,000. (*Id.*) That is absurd.

Morgan Drexen has violated numerous provisions of the adjustment service company law, including not only the licensure requirement but also the requirement to use forms approved by the Division, time limitations for holding debtor funds, requirement to report to the Division, and the prohibitions against charging excessive fees, sharing office space with a practicing attorney, using false, misleading and deceptive advertising, and oppressive and deceptive practices in general. See Wis. Stat. § 218.02; Wis. Admin. Code § DFI-Bkg 73.01. Morgan Drexen charged prohibited fees to all of 1,890 Wisconsin debtors and engaged in unlicensed and prohibited adjustment service company activity with respect to each, despite being notified by the Division back in 2007 that such conduct was illegal. Under no rational view of the facts or law could these rampant violations be reduced to a single licensure infraction.

Though Respondent characterizes the requested forfeiture as “outrageous and excessive,” the Division is not even seeking the full measure of forfeitures authorized by the legislature. Given that there were multiple violations of the law with respect to each Wisconsin client, the Division would be justified in assessing forfeiture at several times the number of debtors illegally serviced by Morgan Drexen. Moreover, the law permits the Division to impose a forfeiture of up to \$10,000 for each violation; the Division requests only \$1,000.

Therefore, the Division’s request for forfeitures will be granted for each of the 1,890 statutory violations in the amount of \$1,000 per violation. These forfeitures are not assessed

lightly. But, the legislative history of Wis. Stat. §218.02, and the criminal penalty that may be imposed for violations, strongly indicate that the State of Wisconsin views illegal adjustment service company activity as a significant threat to the welfare of its residents. The facts of this case aptly color that concern.

Substantial evidence supports the Division's charge that Respondent has engaged in deceptive and oppressive practices towards hundreds of Wisconsin residents, willfully refused to comply with the laws of this State, and employed deception in an effort to evade those laws. This convinces that forfeitures are necessary and appropriate and consistent with the Division's duties to enforce the law as mandated by the legislature.

ORDER

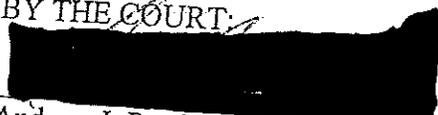
Based on the foregoing, IT IS HEREBY ORDERED:

1. Morgan Drexen's Petition for Declaratory Relief is hereby denied and dismissed forthwith.
2. Morgan Drexen shall immediately cease and desist any and all violations of Wis. Stat. § 218.02 and Wis. Admin. Code § DFI-Bkg 73.
3. Morgan Drexen shall not, directly or indirectly, conduct or attempt to conduct adjustment service company business with Wisconsin residents.
4. Within 30 days of the effective date of this Order, Morgan Drexen shall remit payment to the Division in the amount of \$4,253,081.93 as restitution for fees illegally charged Wisconsin debtors. Morgan Drexen shall coordinate the form and manner of this remittance with the Administrator of the Division of Banking.
5. Within 30 days of the effective date of this Order, Morgan Drexen shall remit payment to the Division in the amount of \$1,890,000 as forfeitures for committing at least 1,890 violations of the adjustment service company laws. Morgan Drexen shall coordinate the form and manner of this remittance with the Administrator of the Division of Banking.
6. The effective date of this Order is the date on which it is signed.

IT IS SO ORDERED.

Dated: 4-25-2013

BY THE COURT:


Andrew J. Parrish
Administrative Court Judge

NOTICE: Pursuant to Wis. Stats. §§ 227.48(2) and 227.49, Respondent may file a petition for rehearing within 20 days after the effective date of this Order. Pursuant to Wis. Stats. §§ 227.48(2) and 227.52, Respondent may file a petition for judicial review within 30 days after the effective date of this Order. The identification of the party to be named as respondent therein is the Wisconsin Department of Financial Institutions, Division of Banking. Pursuant to Wis. Stat. § 227.47(1), the parties for the purpose of review under Wis. Stat. § 227.53 are: Morgan Drexen, Inc., 1600 S. Douglass Road, Suite 100, Anaheim, CA 92806 and the Wisconsin Department of Financial Institutions, Division of Banking, 201 W. Washington Ave., Suite 500, PO Box 7876, Madison, WI 53707-7876.