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VOL. 15, NO. 6

NOVEMBER-DECEMBER 2021

## Litigation Funding: What Transactional Lawyers Should Know

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*“I’m not a litigator. Why should I care about litigation funding?”*

This common (but understandable) misconception of litigation funding is why many transactional lawyers are missing easy opportunities to generate new business and be better partners to existing clients.

As transactional attorneys, you are uniquely positioned to understand your clients’ challenges and help identify solutions. You understand their business models, motivations, strengths and weaknesses, what they need right now and what they may need in the future. Transactional attorneys often understand their clients better than anyone else.

This article explains how transactional attorneys with a working knowledge of funding are better equipped to help their clients, and provides a crash course and background information needed to identify when funding might be an option.

The key is recognizing that legal claims — both active and dormant — are company assets

capable of being monetized in many ways and for many different reasons, and that funding is a tool for maximizing the value of those assets.

Not surprisingly, use of litigation funding is on the rise. According to one recent study, there are approximately 50 active funders in the U.S. litigation funding market with combined assets under management exceeding \$11.3 billion.<sup>1</sup> Funders closed more than 300 transactions in 2020, committing nearly \$2.5 billion towards new investments.<sup>2</sup> Given the unique relationship transactional lawyers have with their clients, they are uniquely positioned to identify opportunities that could benefit from funding.

### The Basics of Litigation Funding

As a transactional attorney, you don’t need to be an expert in funding (or litigation) to leverage funding to help your clients. All you need to know are the basics so you can identify when funding might provide a solution or be an option to help. Here are nine things you should know:

1. Clients of all shapes and sizes are increasingly taking advantage of funding. From start-ups, inventors and high-growth companies to private equity, Fortune 500s,

<sup>1</sup> Westfleet Insider: 2020 Litigation Finance Market Report

<sup>2</sup> *Id.*

and even universities, funding is being deployed in a wide-variety of practical, problem-solving ways. For example, public universities are using funding to pursue patent enforcement campaigns to protect their intellectual property without using taxpayer dollars. Private equity funds are using funding to pursue and monetize valuable claims without any adverse impact on EBITDA. Start-ups are using funding as a source of growth and working capital, and to avoid siphoning capital from the core business. And many companies, particularly during the pandemic, have used funding to help alleviate short-term cash flow and liquidity issues without taking on any associated liabilities.

2. Funding is not a loan, no cost, and non-recourse to the client and firm. At bottom, litigation funding is an investment in a legal claim by an independent third-party funder. The funder is making a non-recourse investment in exchange for an agreed-upon stake in the outcome of the case. There is no cost to the client because the legal spend is covered by the funder. If the case is successful (settlement or judgment), the funder receives a portion of litigation proceeds as a return on its investment. If the case fails, the funder is owed nothing.

3. More than just paying litigation attorneys' fees and expenses. Traditionally, the most well-known type of funding involves the funder *paying the law firm* for attorneys' fees and expenses on behalf of the client, as bills are tendered. Likely more interesting to transactional attorneys is a category of funding tools known as "monetization," which involves the funder making cash payments *directly to your client* in exchange for a portion of future recovery, if any. In other words, funding can be used to "monetize" litigation

claims and immediately convert them into capital, similar to other types of business assets. Notably, funding arrangements can be structured to provide for both monetization and payment of fees and expenses.

4. Funding can be used for lump-sum capital infusions and ongoing payment of Operating Expenses. These are two of the many ways monetizations can be structured, depending on your client's particular needs and preferences. For example, some companies prefer to structure monetizations as a series of contractual payments (which provides additional accounting benefits that can boost the company's value), while other companies prefer to structure them to cover defense costs from unrelated cases (which can help a company manage its overall legal budget). These are just examples, but this type of structural flexibility is a hallmark of litigation funding.

5. Help your clients maximize the value of dormant assets (legal claims), with no negative balance sheet implications. This can be done in a couple ways: *First*, because all legal spend is covered by the funder, clients have the ability to pursue valuable claims they might otherwise abandon for reasons unrelated to the merits — such as negative balance sheet implications or budgetary constraints. A recent survey of in-house lawyers indicates that 70% of companies have unenforced awards worth \$20 million or more.<sup>3</sup> Funding offers a way to unlock the value of those assets. *Second*, through monetization, clients can immediately convert a portion of the dormant asset value into non-recourse capital, without any associated costs or liabilities. This enables your client to lock-in a return, even if the case ultimately fails.

<sup>3</sup> Burford Capital Legal Finance Survey 2020.

Monetization also allows your client to book an accelerated recovery in accordance with the client's timing and structural preferences (e.g., up-front lump sum or regular installment payments).

**6. Protect IP and generate ongoing revenue.**

For companies with valuable patents and other IP, funded enforcement campaigns allow companies to protect their IP from infringers, and generate revenue through licensing arrangements that provide for running-royalties.

**7. Ensure capital remains dedicated to core business operations.** Every dollar spent on litigation or an enforcement campaign is one less dollar spent supporting your client's core business. So, every penny saved on legal is a penny earned for the core business.

**8. Funding can yield accounting and valuation benefits.** For public companies, for example, there is no litigation spend to report because the company's spend is covered by the funder. Funding also protects P&L and EPS by avoiding any adverse impact on the balance sheet, thus preserving company value, while at the same time adding predictability and improving financial forecasting. As noted above, in the context of monetization, a cash infusion boosts the bottom line and can be structured as series of contractual payments booked as ongoing revenue.

This is notable because even where the client ultimately prevails after years of litigation, the recovery is treated as a one-time extraordinary event that likely doesn't impact market perceptions or the company's book value. Funding thus offers a way to avoid drag on the balance sheet during litigation, as well as an opportunity to affirmatively increase operating profit, and, by extension, enterprise value.

**9. Funders are passive investors — attorneys and their clients retain complete control.**

Funders do not interfere with counsel, practice law, provide legal advice, or control strategy or settlement decisions. All legal and strategic decision-making power remains with the client and its attorneys.

## Conclusion

The goal of this article was to dispel a common misconception that litigation finance is just for litigators, and provide transactional attorneys a crash course to identify when funding might be an option to help your clients. As transactional attorneys, you understand your clients' needs and challenges better than anyone else, and are best positioned identify solutions. By having a working knowledge of litigation funding, you have more tools at your disposal to help craft creative solutions, and be a better partner to your clients.

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