How Commercial Litigation Funding Can Help Small Firms and Solo Practitioners

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By David Gallagher

This article is the first in a two-part series covering the burgeoning topic of litigation funding. This article provides a brief introduction to two forms of commercial litigation funding that can help solo practitioners and small firms. Part two will cover ethical and other issues arising in the context of litigation funding, with an emphasis on implications for small firms and solo practitioners.

Put simply, litigation financing is the practice of spreading the financial risk of litigation to an investor. An investor provides the funds needed to keep up a litigation fight, risks non-repayment if the case results in a total loss, and shares in the gain if the case results in a favorable settlement or other resolution.

Among the leading commercial litigation funders, the structures of funding deals vary, but all deals have one thing in common—the funding is non-recourse. The party taking the funding owes the funder nothing—not even its money back—unless the litigation is successful and there is a settlement or collected judgment.

OPPORTUNITIES AND CHALLENGES OF CONTINGENCY FEES

Attorneys practicing solo or in small firms are particularly well-suited to benefit from litigation funding. Litigation funding is often used in the context of contingency fee cases, and attorneys practicing solo or in small firms are more likely than those practicing in larger firms to take cases on a contingency basis. In any contingency fee cases they do take on, they are also likely to enjoy more of the upside of any success and more of the downside of any failure, as compared to their big law counterparts. Litigation funding can enable attorneys practicing in small firms or as solos to take on more cases on a contingency or blended/hybrid fee basis, and to share the risk of doing so with a funder.

SINGLE-CASE FUNDING FOR CLIENTS

A typical single-case funding model that works well for attorneys and clients starts from a blended or hybrid fee arrangement and a reasonable budget. The attorney bills the client at 50% of his or her normal realized rates, putting in the other half of his or her time on a contingency fee basis. The funder provides funding to the client to pay the monthly-billed half of the fees, up to an agreed-upon maximum budgeted amount. The client pays only the litigation costs. If the case is successful and there is a recovery, the largest portion typically goes to the client, after the attorney is paid his or her contingency fee, and the funder is paid its contracted return (which may be a multiple of the funded amount or a percentage of the recovery).

The above model is simply one among many possible variations. If the client cannot pay the litigation costs, the funder may provide additional funding to cover them, in exchange for a larger return, to be paid out of the litigation proceeds. If the attorneys prefer to work fully on contingency, the funder may fund just the litigation costs. If the attorneys are working fully on contingency *and* are advancing the litigation costs, the funder may provide funding to the client for business operating or expansion costs, or even for personal expenses. A funder can provide funding for whatever purpose the client needs, *provided* the funder determines that the merits of the case and the solvency of the defendant support the requested funding.

PORTFOLIO FUNDING FOR LAW FIRMS

In addition to providing funding directly to clients in single cases, funders can provide funding to law firms on a "portfolio" basis. In a law firm portfolio deal, the funder invests a fixed dollar amount into a law firm, and the funder's return is secured by a portfolio of cases being handled by the firm on a contingency or partial-contingency (*i.e.*, a blended or hybrid) basis. The amount funded frequently represents a portion of the fee budgets or cost budgets in the same portfolio cases, but the firm can use the funding for any purpose—to hire new associates, expand a practice group by adding new partners, open a new office, advance litigation costs, etc. Again, the funder will need to determine whether the merits of the portfolio cases and the likelihood of collection will support the requested funding.

In a portfolio deal, when the firm collects its contingency fees from any one or more of the cases, it pays the funder its contracted return (usually a multiple of the funding amount). No portion of the funder's return is taken from the client. Like single-case funding, portfolio funding is non-recourse. If the firm is unsuccessful on all the portfolio cases, it owes the funder nothing.

BENEFITS FOR SMALL FIRMS, SOLO PRACTITIONERS, AND THEIR CLIENTS

Litigation funding, either in the form of single-case funding for the client or portfolio funding for the firm, has many benefits for lawyers and clients alike:

- It permits cases to be determined on their true merits, rather than by which party has greater financial resources.
- It reduces litigation risk.
- It alleviates budget pressure.
- It enables clients to work with their preferred counsel.
- It enables clients to preserve capital for core operations.
- It helps firms to establish and strengthen client relationships.
- It demonstrates the firm's sophistication and sensitivity to client business goals.
- It enables firms to manage their cash flow and cover most or all of their fixed costs, and still recover significant contingency fees.
- It maximizes the likelihood of success in the litigation by enabling counsel to prepare cases with top experts.
- It fortifies clients against low-ball settlement offers.

So, when evaluating a client matter, including strategies for how to continue a long and expensive fight, keep litigation financing in mind as a tool in your arsenal.