

The Art Of The Litigation Funding Deal

By **Julia Gewolb** (February 8, 2018, 6:01 PM EST)

As litigation funding becomes more widespread, greater complexity and variability in funding deals are to be expected. Creative deal terms can be a great asset to claimants and lawyers in need of unusual funding solutions, but they also run the risk of muddying the economics of funding transactions. This article outlines a set of key questions on the economics of single-case funding that all claimants should keep in mind when considering or comparing funding terms.



Julia Gewolb

Case Budget & Investment

First, how much funding is needed to see the case to conclusion, and how will it be divided among the funder, lawyers and claimant? This is the first and most essential question because all the economics of the deal will flow from how much each participant is contributing. Specific questions to consider here are:

- What is the cost of bringing the case through trial and appeal? While it's impossible to estimate litigation costs with absolute certainty — unexpected events can and usually do arise in litigation — it's important to establish a realistic and experience-based budget to guide funding negotiations. Because a funder's investment is usually capped, every budget should include some cushion to cover the unknown and to prevent claimants from having to seek additional funding midway through the case — but not so much that the case will not support a healthy return for each of the funder, claimant and lawyers (more on that below).
- Is the funder seeking to recover any due diligence fees? In addition to the funding requested by the claimant, some funders seek to recover the costs of their due diligence on the matter, and perhaps even to earn a return on the amount. An apples-to-apples comparison of funding proposals should take any such fees or charges into account.
- Who will bear the risk of covering fees and costs that exceed the case budget? It's also important to consider whether the claimants or lawyers will bear the responsibility of covering any spending in excess of the case budget and / or the funder's capped commitment.

- Does the claimant need or want any working capital during the pendency of the litigation? In addition to covering litigation fees and costs, claimants might use litigation funding to cover business or personal costs. Or, perhaps a claimant simply wants funding up front to defray the risks of litigation. Either way, it's helpful to have a number in mind when approaching a funder.

Litigation Recovery & Returns

Second, what is the realistic value of the case, and does that value support a healthy return for each of the claimant, lawyers and funder? Simply put, if pursuing the litigation costs as much or nearly as much as the case is expected to yield in damages or settlement, it will not be a good candidate for litigation funding. Even where the expected damages clearly exceed the funding required, a case may not be right for funding if the lawyers' contingency fee and the funder's return combined eat up the lion's share of proceeds. In considering these issues, claimants should ask themselves:

- What is a reasonable estimate of the damages or settlement value of the case? Claimants should work with their lawyers to establish a reasonable, relatively conservative estimate of the value of the case to guide discussions with litigation funders. While funders will conduct their own due diligence into the case's value, such estimates are needed early on to establish a basic framework for discussion.
- What is the claimant willing to settle the case for? Likewise, it's helpful for everyone when a claimant has considered, and comes to some understanding, of what settlement range he or she would be likely to find acceptable.
- Is a non-cash settlement or relief likely? While litigation funders may be willing to consider investing in a case that includes a likely non-cash settlement component (i.e., a settlement where the claimant receives some rights or continuing business interest, as opposed to a lump sum), such components can be more difficult to value for funding purposes.
- What returns will the lawyers and the funder receive? This, of course, is the key question in any funding deal. As a starting point, a good rule of thumb — and one that Bentham follows — is that every deal should aim to secure the claimant in the case a healthy return after the funder's and lawyers' interests are paid out. To accomplish that, Bentham typically looks for a significant amount of realistic expected damages that far exceed the amount of litigation funding sought.

How much is a "significant amount" of damages? As an example, let's assume the funder and the claimant's counsel equally split attorneys' fees: the funder pays the lawyers an agreed upon percentage of hourly fees as incurred, while the lawyers take the remaining portion of their hourly fees on contingency. The claimant pays any out-of-pocket costs in the case. (If, instead, the funder assumes the additional burden of paying costs, its share of the return might rise relative to the lawyers' or claimant's share.) In return, the funder and the lawyers split a contingency interest down the middle, and the claimant keeps the remaining case proceeds.

Under this basic funding model, the calculation of the damages needed to sustain a healthy return for all parties resembles the calculation most contingency lawyers are already familiar with: what damages are needed to sustain a fee that fairly rewards the lawyer's work (and the funder's contribution), while also

ensuring a fair outcome for the client? If the realistic expected damages are so low that the lawyer and the funder are very likely to receive a zero return on their invested capital and time, the case likely is not suitable for funding.

While this basic model is often tweaked — for example, the claimant may want operating capital; the lawyers may not be willing to take on a significant contingency risk; the funder’s return may include a “floor,” or minimum return, that might exceed the funder’s percentage-based return in a low-recovery scenario; or the funder’s return may vary over time as the litigation progresses — the basic concept of aiming for fair and proportionate returns for all parties should hold in every deal. As always, a best practice for evaluating proposals is to choose a range of likely litigation recovery scenarios based on best-case and worst-case damages scenarios and to model out the returns for the claimant, lawyers (including any hourly fees paid as incurred by the funder) and funder.

The entry of new litigation funders and increased complexity in funding terms means that claimants and lawyers are likely to see radically different (and far less straightforward) deal terms. No matter the terms proposed, these questions should provide a useful roadmap for evaluating funding proposals.

Julia Gewolb is legal counsel in Bentham IMF's New York office.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.