

Burford

Litigation Finance: An Introduction

About Burford

Burford is the world's largest specialty provider of investment capital and risk solutions for litigation. We provide litigation-related corporate finance to businesses and law firms.

Burford is a \$300 million investment fund publicly traded on the London Stock Exchange, committing more than \$150 million annually to a diversified portfolio of matters. Investment capital is available immediately. Burford also owns and operates the UK's leading litigation insurance provider.

Burford has worked with more than half of the AmLaw 50 (and most of the UK's leading law firms) and with a wide variety of businesses – from small start-ups to large public companies – all over the world.

Burford supplies corporate finance solutions to enable meritorious commercial cases to proceed with high quality counsel. Burford's capital can be used to pay some or all of the costs of litigation, to finance insurance arrangements or to monetize a claim to provide immediate capital for other business purposes.

Businesses use Burford's capital to alleviate liquidity or budget constraints, to assist with the accounting treatment of litigation matters, or simply for prudent financial or risk management. Law firms rely on Burford to facilitate alternative fee arrangements and other risk transfer solutions.

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Christopher Bogart, Chief Executive Officer at Burford Capital LLC

Christopher Bogart co-founded Burford and serves as Chief Executive Officer at Burford Group Limited.

Mr. Bogart's background includes a wide variety of legal, executive management and investment experience. In recent years, he has served as Chief Executive Officer of Churchill Ventures Limited, a publicly traded investment vehicle; Managing Director of Glenavy Capital LLC, a global media and technology investment firm; and General Partner of the Glenavy Arbitration Investment Fund LP, a dispute financing firm.

Previously, Mr. Bogart held a number of senior executive positions with Time Warner Inc. He served as Executive Vice President & General Counsel of Time Warner Inc., managing one of the largest legal functions in the world with more than 350 lawyers. He also served as Chief Executive Officer of Time Warner Cable Ventures and one of four senior executives operating Time Warner Cable, Time Warner's largest business, with \$9 billion in revenue and 30,000 employees.

In the course of his work with Time Warner, Mr. Bogart played a significant role in a number of major transactions and litigation matters, including: the \$350 billion merger with America Online; the acquisition of Turner Broadcasting Systems, including CNN and its other media properties; antitrust litigation with News Corporation; the attempted acquisition of EMI Music; a joint venture with Microsoft and Compaq to create a major national broadband business; a constitutional challenge of the federal Cable Act; and a \$550 million litigation over the Six Flags theme park.

Mr. Bogart came to Time Warner from the New York law firm of Cravath, Swaine & Moore where he was a trial lawyer representing companies such as IBM, GE and Time Warner. He was the gold medallist and graduated with distinction from the Faculty of Law of the University of Western Ontario, and served as a law clerk to the Chief Justice of Ontario.

Litigation Finance: An Introduction

Over the last few years, many have heard of litigation finance for the first time. Despite extensive press coverage of this rapidly growing practice, litigation finance remains a subject of some mystery even to sophisticated lawyers and corporate executives. We hope to dispel much of that mystery here, and to highlight the advantages that litigation finance offers to both corporate clients and their lawyers.

I. What Litigation Finance Is

Litigation finance, which can take many different forms, generally refers to any transaction through which the asset value of a litigation claim is used to secure financing.

In the simplest variation of the practice, commonly referred to as "litigation funding," a provider of finance covers the expenses of bringing a legal proceeding in exchange for a return tied to the outcome of the case (e.g., a portion of the damages or the settlement received).

Because the litigation funder's return is tied to the success of the case, there is a strong motivation for financial providers to fund only the most meritorious actions.

In a sense, litigation financing transactions are entirely unremarkable, sharing much in common with the financing that businesses obtain every day by collateralizing their real estate, equipment, or inventory.

In contrast to those assets, however, litigation claims have not routinely been viewed as a potential source of financing. Much of the excitement over litigation finance revolves around its innovative effect of "unlocking" the often-substantial value buried in unresolved litigation claims.

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In addition to the simple provision of funds for a given case, there are a growing number of other ways in which the advantages of finance are being applied to litigation. These advanced forms of the practice can involve variations in the interest taken by the financier, the purposes to which the capital is put, or the party to which the financing is provided.

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The Need for Litigation Finance

Today's growing litigation finance market would not have arisen if it did not serve a need. Those familiar with the practice of litigation, especially complex commercial litigation, know that the cost of prosecuting claims can be extraordinary. And indeed, there are many situations in which a party would not be able to pursue a claim – or at least not pursue it as effectively – without litigation financing.

In some instances, a client simply cannot afford to bring the proceeding. A business with its major asset tied up in the litigation – for instance, a pharmaceutical start-up with a breakthrough drug subject to a legal dispute – may find itself in this position.

In other instances, although a client may have the resources to pay for the litigation, it chooses to invest them elsewhere. Corporate counsel frequently decline to pursue valuable claims because the expensive, prolonged, and unpredictable nature of litigation makes senior management – or the corporate balance sheet – reluctant to support the effort.

In Depth: Innovative Forms of Litigation Finance

Litigation finance can take many forms beyond the prototypical "litigation funding" example in which the financier funds a single case in exchange for a return on its results.

- Litigation finance can be employed to fund portfolios of cases in addition to individual suits. Portfolio financing, which can be done for law firms as well as clients, distributes risk across multiple actions and thus allows the financier to offer better pricing.
- Litigation finance can be used to fund activities other than prosecuting the underlying claim. High-value claims can facilitate the financing of business operations.
- Litigation finance can provide an immediate, discounted payment on an uncollected judgment.
- Litigation finance can be employed to cover premiums on an insurance policy against the risk of an award being overturned on appeal.
- Litigation financing can serve as a financial tool for defense-side actions as well as offensive actions.

In still other instances, a client may have pursued a piece of litigation, only to reach the limit of its budget before the case is resolved. In all three situations, a litigation financier can provide critical assistance in realizing the value of the claims.

In theory, the needs of such clients could be served by providers other than litigation financiers, most obviously law firms willing to operate on a contingency-fee basis. In practice, however, the firms that are often best situated to bring complex commercial claims and most desired by clients are often not comfortable – given their compensation models and institutional reluctance – to undertake substantial and lengthy litigation without a known return.

Banks, insurance companies, and investment funds could also fill the market demand, though historically, most have been unwilling to provide funding for litigation – which features protracted timelines, and requires significant legal knowledge to underwrite the risks associated with any particular case.

What Litigation Finance Is Not

Having established what litigation finance is, it is equally important to emphasize what it is *not*. First, as discussed here, “litigation finance” does not refer to the funding of consumer lawsuits (e.g., individual personal injury suits).

As the ABA has stated, the market for consumer legal funding, in which the funder typically pays an amount used to cover a plaintiff’s living expenses while pursuing a personal injury lawsuit, is highly differentiated from that of commercial litigation financing.¹

In contrast to the consumer context, commercial litigation financing involves sophisticated corporate parties, typically represented by major law firms, with the financier investing millions of dollars – sometimes up to \$15 million and beyond. Such substantial transactions are highly negotiated, bespoke arrangements.

Second, litigation finance is not an engine for frivolous litigation. Because the success of the litigation financier depends on the success of the case it has financed, it is a business imperative for the litigation financier to select only the most meritorious claims. Those who invest in frivolous lawsuits will quickly find themselves out of business.

Third, litigation finance does not violate any legal or ethical guidelines. The increased popularity of litigation finance has led to questions regarding the extent to which the practice is legally permissible, as well as its impact on evidentiary protections given to confidential information of clients and their lawyers.

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It is not surprising to find those players unhappy about the loss of their historical – and unfair – advantage. These questions have been answered favorably by courts and in examinations conducted by the American Bar Association and the New York City Bar, each of which has found litigation finance to be perfectly acceptable, and many of the very largest law firms use litigation finance without concern.

¹ American Bar Association Commission on Ethics 20/20, White Paper on Alternative Litigation Finance (“ABA White Paper”) at 7-9.

Often these questions are posed by clients and lawyers just familiarizing themselves with litigation finance, who naturally seek assurance that any financing arrangement they undertake complies with the law and will not undermine their case.

A second group, which has been more vocal in attaching ethical concerns to litigation finance, consists of repeat players in the judicial system who often possess greater financial resources than their litigation opponents, and who may be unsettled by litigation finance's effect of leveling the playing field. It is not surprising to find those players unhappy about the loss of their historical – and unfair – advantage.

Lastly, there is nothing novel at the core of a litigation finance transaction. All litigation, after all, requires some form of financing. Although Burford and others are among the first to dedicate themselves to the business, they merely represent an alternative to other methods of financing litigation – borrowing from a bank, raising financing from investors, or self-financing – that are not only well-accepted, but necessary. Litigation funding, the prototypical form of litigation finance, facilitates what is from the perspective of the client a contingency fee, which has long been endorsed by the judicial system in the US and which will soon enter the UK market in the form of Damages Based Agreements.

II. The Positive Impact of Litigation Finance

Litigation finance often serves to connect claimants with good cases to lawyers at great law firms in an arrangement that wouldn't otherwise be economically feasible for either party. It offers substantial additional benefits, too, not just to clients and their counsel, but to the justice system as a whole.

Benefits to Corporate Clients

Much has been written about the increasing pressure on corporate legal departments to limit expenditures on outside legal services, to demand alternative forms of billing for those services, and to cultivate a perception as a corporate profit center rather than a profit drain. Under such conditions, engaging an elite law firm to bring a significant piece of litigation can prove difficult, if not impossible. The substantial fees required by such firms reduce corporate profits and tie up cash during the pendency of the suit, and the return on the expense is so distant and unpredictable – given the vagaries of litigation – that corporate clients are often reluctant to pursue even the strongest cases.

Litigation finance allows corporate legal departments to avoid making the difficult choice between pursuing strong claims and other corporate priorities.

In Depth: Accounting Considerations

The disincentives to litigate valid claims are only enhanced by the accounting treatment of litigation, under which legal expenses paid directly are immediately recorded as expenses. That is, any legal fees paid result in a reduction from profits – a reduction likely to be substantial and last for years in a commercial case of any complexity.

To make matters worse, if and when the client receives a recovery, it is often recorded “below the line” as a non-recurring or extraordinary item. That is an unhappy result for many businesses, and it is particularly unpleasant for EBITDA-based businesses, as the accounting result of pursuing a successful claim can perversely be a permanent reduction in EBITDA (because legal fees paid reduce EBITDA but recoveries occur below the EBITDA line).

Clients can avoid these negative accounting effects by pursuing claims through litigation financing.

Litigation finance allows corporate legal departments to avoid making the difficult choice between pursuing strong claims and other corporate priorities.

With funds supplied by a third-party financier, in-house counsel have an elegant alternative to paying hourly fees to top tier counsel, while at the same time pursuing profit-enhancing claims with little or no downside risk if those claims are unsuccessful.

Benefits to Law Firms

Law firms unwilling to undertake contingency work can only serve those clients able to pay their fees, an obvious constraint that prevents many law firms from accepting interesting and worthy cases that they would otherwise be eager to take on.

Litigation finance allows these firms to accept such cases by ensuring that potential clients are properly resourced.

For firms willing to accept contingency engagements for complex corporate matters, litigation finance can play a critical role in helping such firms expand their practices. In one scenario, the financier can provide working capital directly to the firm itself, allowing it to take on additional cases and/or hire new resources. In another, the financier can help the firm manage risk (from either its current portfolio or potential new cases) by off-loading some of that risk.

Law firms are also discovering that simply raising the possibility of litigation finance can have a positive effect on client relations. When negotiating engagement fees, the attorney-client dynamic can often become tense and focused exclusively on the percentage discount a firm is willing to offer. The availability of litigation finance allows a firm to offer its client an entirely different alternative to its hourly rate structure. Even when the client does not ultimately pursue litigation financing, the simple suggestion of an alternative approach – and the entrance of a third party – often releases much of the negotiating tension. On a related note, in the United Kingdom there is a growing consensus that lawyers are ethically obligated to discuss financing options with their clients at the outset of a case¹.

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Benefits to the Judicial System

The benefits of litigation financing flow not just to the parties and firms that employ it, but also our judicial system as a whole. Open access to the civil justice system –

¹ CDR – Don’t ask, don’t tell: a duty to discuss litigation funding? By Edward Machin – July 9, 2012

In Depth: Burford's Story

Christopher Bogart, CEO of Burford and the former general counsel of Time Warner, structured what may be the largest corporate contingency fee in history: a \$35 million fee paid to Cravath, Swaine & Moore for its work on the AOL/Time Warner merger. He had observed the frustrations of both law firms and their clients with the economics of modern legal practice, and in the Time Warner merger demonstrated his desire to find a satisfactory alternative for both.

Separately, Jonathan Molot, Burford's Chief Investment Officer and a professor at the Georgetown University Law Center, had been researching the troubling impact on litigation outcomes of situations in which parties to litigation possess disparate levels of financial resources. His writings had investigated the question of whether a market solution, rather than procedural reforms, could most effectively level the playing field for litigants with inferior financial resources.

The two met at a RAND/UCLA conference on litigation finance, a meeting that ultimately led to the formation of Burford Group and the raising of a fund, Burford Capital, dedicated to helping clients and lawyers manage the financial burdens and risks of litigation. Since then, Burford has become the largest player in the world and continues to pioneer new advancements in litigation finance worldwide.

not just in theory, but in practice as well – is a fundamental characteristic of any meaningful legal system. While all would agree with this statement, they would likely also agree that the onerous costs associated with modern legal practice, particularly in complex commercial matters, places the courts out of reach for many.

By making it economically feasible to bring worthy claims, litigation finance allows parties to overcome the prohibitive expense, prolonged duration, and other disincentives associated with modern litigation, with greater efficiency than any court reform.

Importantly, in easing the path to the courthouse, litigation finance also selects out meritless cases. While some wrongly suggest that the availability of financing indiscriminately promotes litigation, the truth, as noted earlier, is that business necessity requires litigation finance providers to back winning cases. Litigation finance providers, therefore, provide a vetting function that is valuable to overburdened courts.

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Litigation finance also has the fairness-enhancing effect of leveling the playing field between those parties that have ample litigation budgets and those that do not.

An imbalance in litigation resources can have a significant effect on litigation outcomes, despite the fact that it has no relation to the merits of the case. Rare is the litigator who has not observed, for instance, aggressive motion work from a resource-rich party designed to sap the budget of its adversary and pressure it into settlement. This negative phenomenon, once the subject of academic study by Burford Group Chief Investment Officer, Jonathan Molot, is corrected through litigation finance. It gives the party that uses litigation finance the necessary resources to conduct the litigation and allows the case to be decided, as it should be, on the merits alone.

III. What Burford Offers

The considerable appetite for litigation finance has attracted a number of providers into the market. None, however, can claim the level of resources and talent for innovation possessed by Burford, which *Litigation Finance* magazine has called the “giant” in the field. Burford began in 2009 and is the largest fund in the world dedicated to litigation finance by a significant margin, with more than \$300 million in capital. In its lifetime, Burford has committed more than \$280 million in capital to investments involving US commercial litigation, international arbitrations, and most recently, litigation in the UK. The fund is publically traded on the London Stock Exchange.

The size of Burford’s fund provides it with a distinct competitive advantage over others in the market. While some “funders” assemble financing on a deal-by-deal basis, Burford’s superior resources position it to act immediately on any deal it considers, and without any risk that it will fail to raise the necessary capital.

Its large pool of assets has also allowed Burford to diversify its portfolio. In contrast to some litigation finance providers that deal exclusively in narrow legal issue areas, Burford believes it is smarter to spread its investments across a broad range of legal issues, law firms, jurisdictions, and other metrics.

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Fundamental to Burford’s approach to investing is a deep respect for the lawyer-client relationship, and on principle, it does not interfere with strategic decisions made between clients and their attorneys. This principle provides an important differentiation for Burford from some other funders in the market. While Burford conducts extensive due diligence on each opportunity it considers, and while clients and their lawyers have come to rely on the analysis and insights of Burford’s experienced litigators, Burford assumes no control over litigation strategy, settlement decisions, or any other matters properly falling within the domain of the lawyer-client relationship.

Burford’s greatest asset, however, lies in the innovative and skillful approach taken by its senior management. CEO and co-founder Christopher Bogart is the former general counsel of Time Warner, Inc., where he managed a department of 350 lawyers, and also formerly practiced as a litigator at Cravath Swaine & Moore.

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Jonathan Molot, co-founder and Chief Investment Officer of Burford, previously clerked for US Supreme Court Justice Stephen Breyer and served as counsel to the economic policy team on the Obama-Biden Presidential Transition.

Burford's management team includes a former general counsel within Dow Jones, a former chair of Latham & Watkins's national litigation department, and others with similar leadership experience. Its investment staff includes litigators with decades of experience at top law firms and in senior in-house positions at major corporations. Many if not most of the innovations in the industry beyond standard litigation funding are the work of this talented team.

Moving forward, Burford will continue to expand. Early in 2012, it extended its focus from the US to the UK through the acquisition of Firstassist, the largest provider of litigation expense insurance in the UK market. This step not only provided a logical geographic expansion for Burford's core offerings, but extended Burford's business model into insurance-related products that can further assist both clients and law firms.

As the legal industry looks to lessen the financial pressures on litigants and law firms, it increasingly appears that litigation finance may provide some of the best and most efficient tools for the task.

As the services of litigation financiers are better understood and appreciated by those in the legal practice and their clients, interest only continues to grow. Indeed, it seems inevitable that both Burford and the litigation finance industry as a whole will continue to innovate and evolve, providing valuable opportunities for those involved in commercial litigation.

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