

Burford

Guide to

LEGAL FINANCE PRICING





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Burford Capital is a leading global finance and investment management firm focused on law. Its businesses include litigation finance and risk management, asset recovery and a wide range of legal finance and advisory activities. Burford is publicly traded on the London Stock Exchange, and it works with law firms and clients around the world from its principal offices in New York, London, Chicago, Washington, Singapore and Sydney.

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Pricing risk, structuring agreements and the cost of legal finance capital

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Craig Arnott is Managing Director responsible for Burford's underwriting and investment activities in the UK, continental Europe, Asia and Australia. He was previously a barrister at Sixth Floor Selborne and Wentworth Chambers in Sydney, and Head of Competition/Antitrust at Fried Frank Harris Shriver & Jacobson in London.

Since joining Burford, one of the most common questions posed to me by lawyers is this: How much does Burford’s capital cost? It’s a sensible and understandable question—but one that lacks a simple or one-size-fits-all answer.

It should be no surprise that answering the question of legal finance capital cost is complicated—of course it is. Lawyers and corporate executives call on Burford to provide capital for commercial litigation and arbitration—which is by definition highly complex, expensive and risky.

In this article I’d like to address three topics that shed light on this question. First, I will provide an overview of the various factors that affect the cost of legal finance capital, and the various ways lawyers and litigants can work with Burford to arrive at the best solution.

Second, I will address head-on the notion that legal finance capital is “expensive”. It’s not quantitatively wrong that legal finance typically costs more than transactional forms of financing—but that is not the whole story. The more fruitful way in which we engage clients around the cost of capital is to explain the various ways in which we can structure agreements to deliver what matters most to them. To that end, I’ll provide an overview of some of the most common structures we offer.

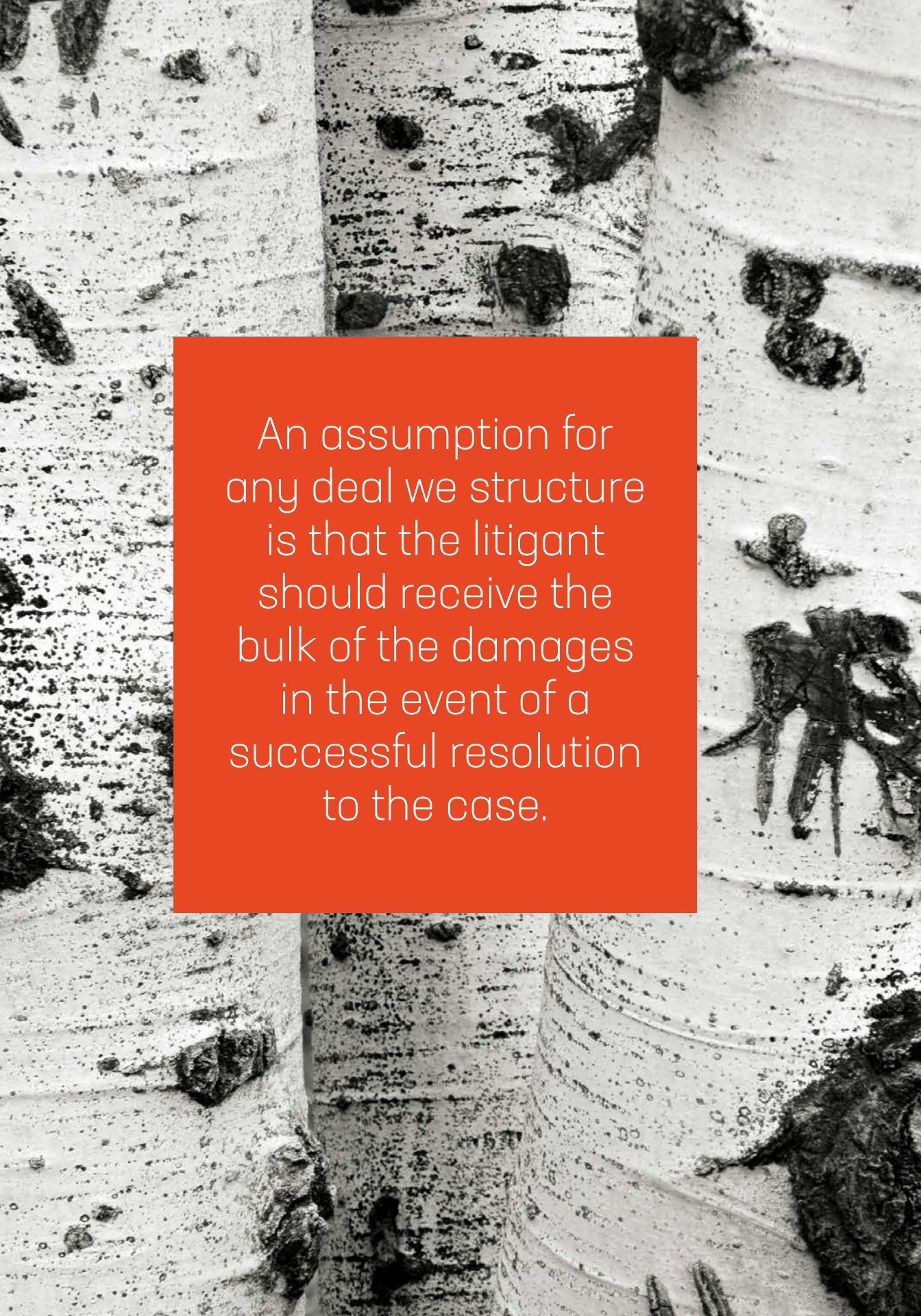
Third, I will provide some guidance on legal finance term sheets—how Burford structures them relative to others in the industry, and how law firm and in-house lawyers should think about them.

How risk impacts pricing

Any lawyer who has spoken to a litigation financier has heard some version of this simple truth: Legal finance pricing is based on risk. Let’s unpack what that means.

When Burford finances matters, we assume an extraordinary degree of risk. Typically, legal finance is provided on a non-recourse basis meaning that we lose our capital if the underlying matters are unsuccessful—and there are very few capital providers with the expertise needed to assess and assume that risk. We take on that risk and the inherent uncertainty of matters that may take years to resolve. When considering an expensive, protracted legal matter, our clients accept the notion of forgoing a portion of their recoveries or fees once their matters have resolved because they know that Burford’s capital not only provided them the means to pursue the matters in the first place but also because our agreement gave them “downside cover” and shifted risk from their business to ours.

So how do we price risk? In many ways we act just like lawyers considering matters to take on contingency. Lawyers recognize that every case is different—understanding the particular client, the circumstances of the matter and the jurisdiction is crucial. The cost of our capital ranges, but ultimately it’s priced competitively according to the risks of the individual matter.

A black and white photograph of a tree trunk with a large red rectangular overlay containing white text. The tree trunk is covered in dark, irregular spots and marks, possibly from insects or weathering. The red overlay is positioned in the center of the image, and the text is centered within it.

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When assessing and pricing risk, we consider a number of factors:

1) TIMING

If a case is about to be filed or has only recently been filed, we don't have the full story of the case—so the case will be considered higher risk.

2) DAMAGES

The damages must be realistic and supported by evidence.

3) RISK DIVERSIFICATION

A single-case investment will by definition have a binary risk—versus a matter that is part of a portfolio, where risk is diversified across numerous matters.

In these terms, the highest-risk investment is a single matter financed in the early stages of the case where Burford is paying all fees and expenses. Because there is only one case, the risk is binary (meaning the finance provider would lose its entire investment if the case loses); and because the case has not progressed, it's difficult to understand the entire story and fully assess the potential risk. Such a case represents the upper limits of Burford's pricing, at about 30-40% of the recoveries.

Burford can also work with our counterparties to finance multi-case portfolios, which have significantly less risk than single-case investments. Portfolios—which can include as few as two matters—are cross-collateralized so that if we invest in case A, but case B returns proceeds, we can return our investment dollars for case A from case B. Because portfolio financing arrangements diversify risk of loss for both Burford and our counterparties, they create better economic structures where claimants can have better pricing than our single cases would ordinarily have.

Most lawyers first work with Burford to finance a single case. Under the right circumstances, we work hard to offer them opportunities to transition to larger financing arrangements that can result in additional savings down the road.

Creating economic structures to match client needs

Setting aside the question of cost, we can also structure deals to reflect specific client needs. For example, some clients value certainty and so we structure deals accordingly. The starting point for any engagement is listening to our clients to understand their needs so that we can offer the right economic structure. An assumption for any deal we structure is that the litigant should receive the bulk of the damages in the event of a successful resolution to the case.

We frequently gravitate to a few consistent structures. These structures exist on a spectrum, with variable returns on one end, and fixed returns on the other.

1) VARIABLE RETURNS

A variable return is comparable to a contingency fee arrangement, where a law firm will advance the cost of litigation out of pocket, and then recoup those costs “first-dollar” out of the return, in addition to taking a percentage such as 30-40% of the net remaining proceeds. In other words, the firm's repayment will vary depending on the ultimate recoveries. In such an arrangement, that percentage of damages recouped represents the risk the firm takes in forgoing all of its fees and advancing costs.

Burford can similarly structure a variable return consisting of our investment back, plus a percentage of the settlement or award. This structure is most attractive to our clients (whether law firms or litigants) when the potential for recovery isn't inordinately large in relation to Burford's investment commitment. That's understandable: If the expected recovery is especially large, you would be less happy to give up a percentage of the upside and would prefer instead a fixed return structure.

2) FIXED RETURNS

At the opposite end of the spectrum is a fixed return structure, where the finance provider's return consists of an investment back, plus a multiple (or fixed) return of that investment, as opposed to a percent of the net proceeds.

3) HYBRID STRUCTURES

In most cases, the needs of our counterparties are such that the return structure falls somewhere in the middle of the spectrum, resulting in a hybrid structure. Burford will get its investment back, then some fixed return—albeit a smaller multiple than if we were relying on that entirely—and then also a percent of the net proceeds—again, likely a lesser amount, given that we have both a fixed return and a variable return element.

4) RETURN WATERFALL

In addition to working with clients to find structures that meet their needs and match our view of the risk, we also work to structure an appropriate return waterfall—in other words, to lay out the order in which and the increments by which we and our counterparties earn returns from matters in which we invest. Again, each matter is unique and we work hard to adjust waterfalls to clients’ needs—but the important point to appreciate is that while Burford may earn its investment back on a first-dollar basis, further recoveries are often split on an incremental basis. In essence, Burford and its counterparties “take turns” earning returns.

Understanding term sheets

A critical step in the process of finalizing a legal finance investment is the term sheet, which is the medium in which Burford expresses our proposed structure and terms. We have a unique view on term sheets which bears some explanation.

After nearly ten years in business, Burford’s team has reviewed thousands of cases, and we’ve concluded that we can best meet the needs of our counterparties if we complete a substantial amount of diligence before we provide term sheets. This gives us an opportunity to listen to our counterparties’ needs and offer realistic terms informed by our understanding of the risk. During this initial period, we do not seek exclusivity.

Some other finance providers take a different approach, preferring to propose term sheets along with a 60-day exclusivity period at the beginning of the process, before they’ve invested in a significant amount of diligence. While other funders’ intentions may be good, we caution (and it will not be a surprise) that often their initial proposed terms ultimately change during the diligence process to something that is more appropriate for the case.

Conclusion

In the end, how we price an investment is flexible to meet the needs of our counterparties. The cost depends on the risk appetite of the claimant and the law firm, in addition to all the circumstances of the merits of the case. When we make an investment decision, we’re not just investing in the underlying merits of the litigation, we’re investing in and trusting the litigation counsel the claimant has chosen to execute a strong legal strategy—we’re investing in the entire potential of that case and the people who are going to run it. It’s crucial that we have discussions with the claimant’s legal team to understand what they think is likely to happen, what they want to happen, and what they don’t want to happen so that we can price our capital accordingly.



Do the math: The cost of self-finance vs. outside finance of litigation

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Aviva Will is Senior Managing Director in charge of Burford's underwriting and investment team and has reviewed many hundreds of billions of dollars' worth of commercial litigation. She has particular expertise in antitrust and international arbitration matters, and in financing through bespoke portfolio models. Previously, she was senior litigation manager and Assistant General Counsel at Time Warner, Inc. and a senior litigator at Cravath, Swaine & Moore LLP.

Before joining Burford in 2010, I was the Assistant GC at Time Warner. In the nearly 10 years since, in-house legal departments have undergone an evolution: What was once an overly siloed business function has become increasingly integrated and strategic, with responsibilities not only for risk management but also for value generation.

Given the need to pursue significant value for their businesses—often achieved through affirmative recovery programs—while managing risk and controlling costs, legal finance is fast becoming an evermore critical tool for in-house leaders.

To illustrate the myriad benefits and applications of legal finance for in-house leaders, we’ve “done the math” on some hypothetical examples of the types of matters we routinely encounter and finance. These case studies demonstrate different use scenarios for our capital and the associated quantitative benefits. These examples by no means provide an exhaustive list of all of the ways in which Burford can help solve business challenges, but they help illustrate how legal finance works and why it is a financial game-changer for the modern legal department.

Legal department adds certainty to its legal spend while demonstrating value

Corporate challenge

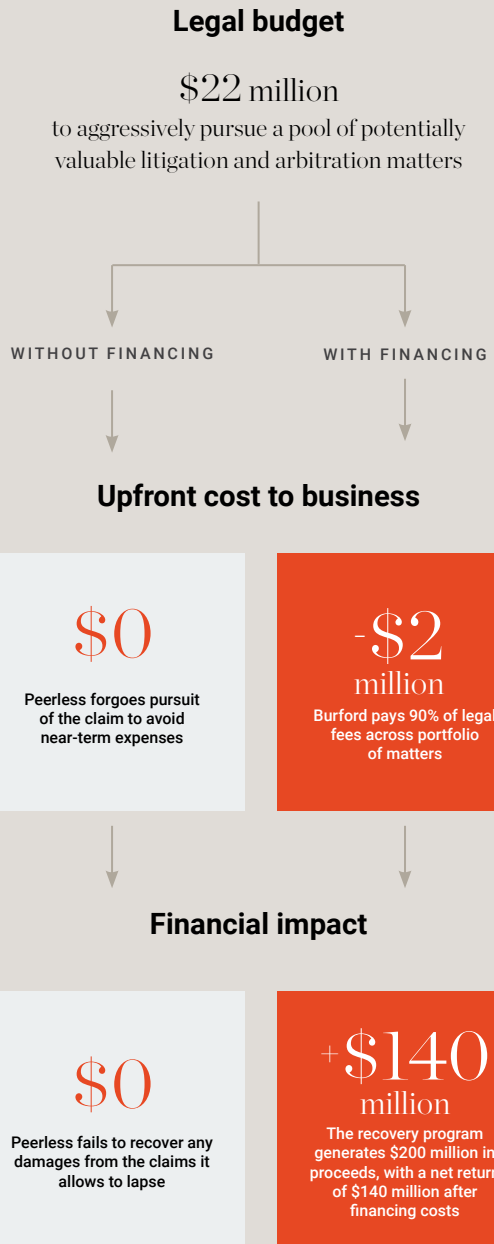
Peerless Inc. is a mid-sized publicly traded company that is facing significant margin pressure and has asked its corporate departments to manage costs accordingly. The company's GC has identified a number of commercial litigation and arbitration matters which could result in aggregate proceeds over \$200 million, but the CFO has pushed back: It's unclear when the matters will resolve, and the GC's counsel of choice are not willing to share risk or reduce their hourly fees beyond a token discount for good clients—creating undesirable uncertainty in Peerless's litigation spend.

Burford solution

Burford provides \$20 million of portfolio financing to offset Peerless's legal fees across the pool of matters, enabling Peerless to pursue its recovery program without significant out-of-pocket spend. Under the terms of the agreement, Burford's investment is returned on a first-dollar basis, plus a multiple of the invested amount. Because the investment is non-recourse, Peerless bears no risk of loss in an unsuccessful outcome. The portfolio financing arrangement allows Peerless to pursue its recovery program without adding significant cost or risk to the corporate balance sheet.

Impact

Over the following years, Peerless recovers \$200 million across its pool of matters, remitting a portion to Burford according to the negotiated investment terms. By the end of the investment, Burford has earned \$60 million—meaning that the portfolio has generated \$140 million in proceeds to Peerless, with minimal downside risk and without adding materially to Peerless's legal budget.



Financing affirmative and defense matters

Corporate challenge

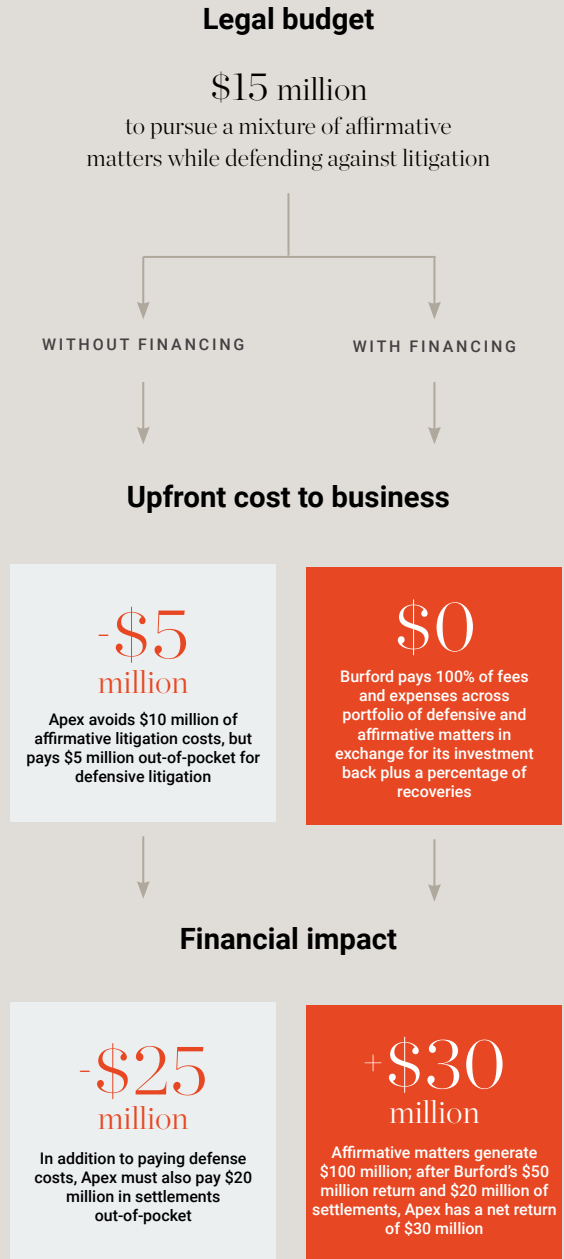
The legal department at Apex Corporation has expanded rapidly to handle a growing slate of offensive and defensive litigation matters. Its increase has drawn the scrutiny of the CFO, who is anxious to keep expenses in check. Apex’s law firm of choice will consider a discount to fees with a corresponding uplift but will not take material contingency risk. The GC has now identified an additional slate of affirmative litigation to pursue, but despite the realistic expectation of significant recoveries, the company’s CFO lacks the risk tolerance to support the plan, preferring to allocate resources solely to defense matters, which are viewed as necessary expenses.

Burford solution

Burford diligences the portfolio and confirms a path to \$100 million in recoveries—a number that dwarfs projected settlements from Apex’s defense matters. Burford offers a \$15 million blended portfolio to cover the \$5 million budget for defensive litigation costs and an additional \$10 million of affirmative litigation costs, in exchange for its investment back plus a percentage return of the eventual recovery net of its investment. This return structure resembles the contingency arrangement with which Apex is familiar: Burford receives a defined entitlement from affirmative recoveries only, and Apex will owe nothing if the affirmative matters are unsuccessful.

Impact

With financing in hand, the GC secures the CFO’s approval to pursue the meritorious cases. Over the next several years, the portfolio generates \$100 million of recoveries. Meanwhile, the defense matters financed through Burford settle for \$20 million. When the investment concludes, Burford has earned \$50 million. Ultimately, Apex nets \$30 million in proceeds, transforming the legal department from a cost center to a revenue generator.



Helping a company assess and pursue claims

Corporate challenge

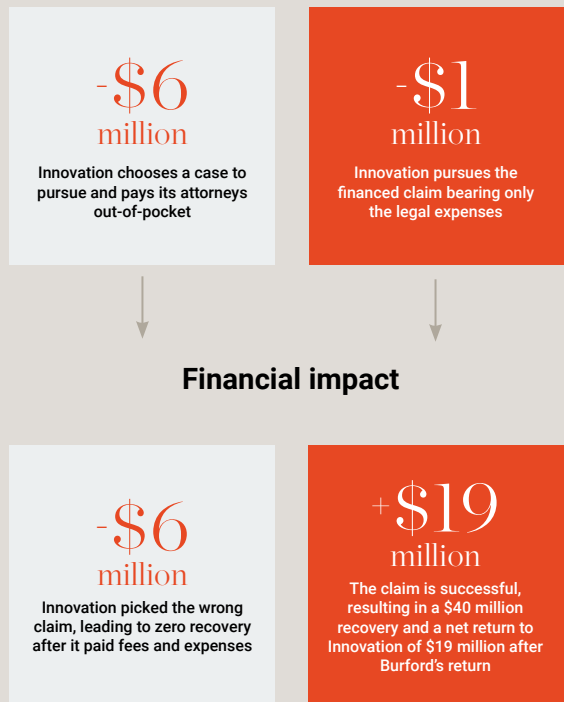
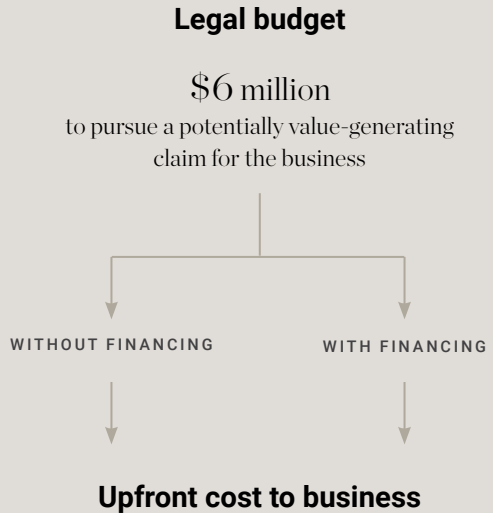
Innovation Inc. has identified numerous affirmative claims that it would like to pursue, and the company’s external law firms have done sufficient initial diligence to support bringing the claims, though all of the lawyers are on hourly fee arrangements and have not expressed a strong opinion that any of the claims will be successful. The combined cost of pursuing all the claims is significantly more than the legal department’s budget, and the GC is faced with the choice of which (if any) cases to pursue to maximize return on litigation cost. As an alternative, the GC approaches Burford for potential financing of all its claims.

Burford solution

Burford performs preliminary diligence on the claims and determines that one of the potential cases meets its investment criteria though it presents significant risk. Burford agrees to finance the \$5 million legal budget for that case in exchange for its investment back, plus a multiple on the investment with Innovation responsible for expenses anticipated at \$1 million. The arrangement is similar to the contingency fee arrangements with which Innovation is familiar. The capital is provided on a non-recourse basis, meaning that Innovation must repay Burford only if the underlying matter is successful. The availability of financing makes the GC’s decision clear: Pursue the financed case and abandon the rest, which an independent third party has declined to fund.

Impact

The case financed by Burford results in a \$40 million settlement in just under two years, offering the company a speedy path to a \$19 million recovery, after it returns Burford’s initial investment and pre-defined multiple.



A company in restructuring finds hidden value

Corporate challenge

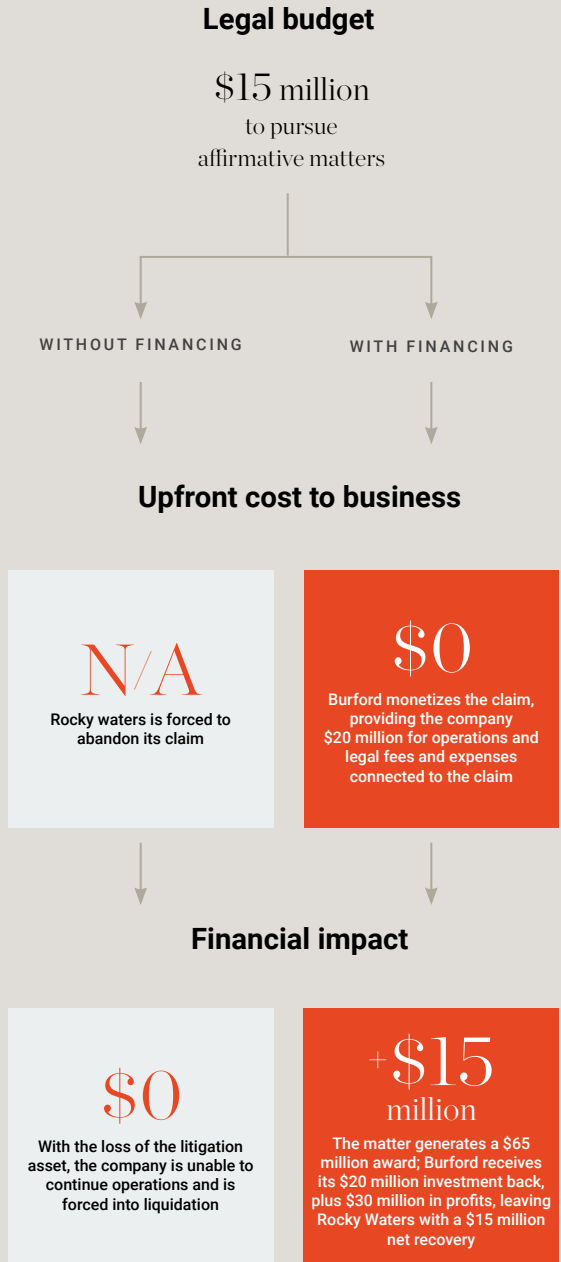
Rocky Waters Rafting is undergoing voluntary Chapter 11 reorganization. It is also in the middle of a preexisting legal proceeding that likely will return \$80 million in damages to the business—but that will take at least two years to resolve, as it is unlikely to settle before appeals. The company recognizes that litigation will be critical to its reorganization plan, but it has been unable to obtain debtor-in-possession (DIP) financing to fund the continued prosecution of the claim. The company’s attorneys are unwilling to go on contingency and switching attorneys at this late stage will be costly.

Burford solution

Burford agrees to monetize 25 percent of the claim, or \$20 million, enabling Rocky Waters to immediately free up liquidity to satisfy its creditors and to pay legal expenses. The capital is provided on a non-recourse basis in exchange for its investment back and a pre-defined percentage of the recovery net of the return of investment. Given the dire need for liquidity, management presents Burford’s financing to the bankruptcy court as part of the reorganization plan, and the monetization is approved.

Impact

With financing from Burford, Rocky Waters gains immediate access to \$20 million, some of which it uses to repay creditors as part of a court-approved reorganization plan. Its legal matter concludes in three years for \$65 million. The company repays Burford its investment back plus a return, leaving a \$15 million recovery for the once-imperiled company.



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