Blurred Lines between Third-Party Funders and Law Firms

The line between third-party funders and law firms is blurring. Originally, there were only two traditional types of third-party funding arrangements. In the first type, the third-party funder makes an agreement to finance the legal expenses of the claimant or respondent in a case in exchange for a portion of the claimant's awarded amount, if the claimant wins, or a predetermined payment from the respondent. In the second type, a third-party funder makes an agreement to finance a law firm's single case or portfolio of cases in exchange for a negotiated rate of return. In both types of traditional third-party funding, the third-party funder remains a separate legal entity from both the funded party and the law firm. Therefore, the traditional third-party funding transaction is often depicted as a triangle with the three corners representing the party, attorney and funder. Now there is new evidence that third-party funders are transitioning from being external investors in parties or law firms to becoming internal partners or owners of parties and law firms. This brief essay focuses specifically on third-party funders partnering with law firms.

The classic relationship between third-party funders and law firms arose in response to a lack of availability of traditional business loans to law firms. Many business loans from traditional banks are secured by tangible collateral owned by the business, such as equipment. Due to the nature of their industry, law firms typically do not own enough equipment to serve as collateral for their business loans. Law firms do have significant accounts receivable, outstanding invoices, or expected contingent fee payments; however, most traditional banks are not willing to accept those intangibles as collateral for traditional loans. The law firm lending segment of the third-party funding industry thus arose because litigation funders are willing to accept future expected payments essentially as "collateral" in exchange for lending cash to law firms. Thus, third-party funders lending to law firms are filling a crucial market need.

The next iteration of this transition is that third-party funders are moving from lending to law firms to investing in law firms. For example, in November 2015, Bentham IMF, a United States-based third-party funder affiliated with IMF Bentham in Australia, issued a press release announcing that it is forming strategic partnerships with law firms, rather than providing only capital under the traditional approach described above. The press release quotes Ralph Sutton, Bentham's chief investment officer, as saying

> *"…[W]e've established close relationships with a number of smaller, top-tier firms with whom we are partnering. We view our portfolio approach as a way of providing strategic capital to elite litigation specialists. We help them recruit talent, launch a promising new litigation specialty, or provide a safety net for their own risks, allowing them to pursue new cases. In short, we help incubate firms and practice groups." (Bentham IMF Unveils New Portfolio Model for Litigation Funding, BENTHAM IMF (Nov. 16, 2015))*

Bentham also provides case referrals to firms with which it partners. This is evidence of the relationship between law firms and third-party funders growing one step closer to resembling a venture capital investment.

The final iteration of this transition illustrates the future of the third-party funder/law firm relationship: merger. This Author predicts that third-party funders will take equity stakes in law firms, that law firms will create their own third-party funders, and that third-party funders will even create their own law firms. The latter of these arrangements –

a third-party funder creating its own law firm – has already occurred. For example, in October 2016, U.S.-based third-party funder, Burford, which is publicly traded on the United Kingdom stock exchange, "has launched a new legal arm dedicated to helping clients enforce their arbitral awards" called "Burford Law." (See Lacey Yong, [Burford launches new firm with former Akin Gump counsel](), GLOBAL ARB. REV. (Oct. 5, 2016)) Burford Law is licensed as an "alternative business structure" under the Legal Services Act 2007 in the United Kingdom. (Legal Services Act 2007, c. 29 (Eng.) This law allows nonlawyer individuals and entities – like third-party funders – to have partial ownership of law firms. Burford Law will "handle English enforcement proceedings and act as a legal advisor to international counsel in enforcement proceedings where other jurisdictions are involved." (See Yong article.) Chris Bogart, CEO of third-party funder Burford, told Global Arbitration Review that "'Burford has added the ability to be a law firm and to provide a more integrated service'" and "that clients may retain Burford Law for advice on enforcement even if they are not receiving third-party funding or using the funder's judgment enforcement services." (See Yong article.) This new development is an example of a truly blurred line between a law firm and a third-party funder.

The investments of third-party funders in law firms are highly controversial, and the consequences of such close collaboration and ownership remain to be seen. For now, careful observation and analysis of these experiments is crucial to understanding the benefits and drawbacks of funder-law firm partnerships.

For a detailed analysis of the benefits and drawbacks of third-party funders becoming internal partners of law firms or parties, see Victoria Shannon Sahani, Reshaping Third-Party Funding, 91 TUL. L. REV. (forthcoming 2017), current draft available here.