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Monday Monday

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Volume 12, Issue 4 | February 12, 2018

Using Litigation Funding for Practice Building

This is part of a series on the importance of litigation funding. We asked Lee Drucker, the founder of litigation funder Lake Whillans which recently raised a new fund of 125 million dollars, for his perspective.

Rainmakers in major law firms have traditionally built high-end business litigation practices by cultivating relationships with the largest corporations and their general counsel. These clients have had the financial resources to accept an hourly rate billing structure over the long course of complex litigation. With the advent of litigation finance, and firms like Lake Whillans, entrepreneurial litigators at large firms have a new path to building sustainable high-end litigation business with a much broader range of clients, not limited to clients with big litigation budgets and strong balance sheets. Entrepreneurial litigators can now also serve companies which have financial constraints, but also have meritorious claims.

Litigation finance also allows enterprising lawyers to overcome the common practical constraints that have made their firms resistant to contingency fee arrangements, reduced or capped fees with success premiums. There have been three major constraints on large law firms:

- **Financial Management.** Law firms cannot access the capital markets to raise equity (due to professional rules of conduct which prohibit lawyers from sharing fees with a non-lawyer). This has created a limiting capital structure. Law firms must generally rely on business revenues and debt facilities (which typically require regular payments) to fund daily operations and capitalize on growth opportunities. Even a relatively small portfolio of contingent fee cases, which does not produce regularly recurring revenues, may be problematic for firms that require monthly income to continue operations.

- **Compensation.** Another challenge is setting fair compensation for partners working on contingent matters that is accepted firmwide. For example, how does a firm compensate two partners if the first one, a transactional lawyer, accounts for $5 million in annual net income and the second one, a litigator working on one contingent fee case, accounts for $5 million in paper losses but might produce $30 million in net income in three years?

- **Investment Selection.** The financial management of large firms does not usually analyze the merits of cases rigorously in the intake process. Because litigation services are invoiced on an hourly rate basis, the ultimate outcome of the litigation does not materially affect the firm's financial position, at least in the short run. By contrast, a successful contingent fee practice requires careful selection of a portfolio of cases that rationally spreads the risk of loss from any one case. When millions of dollars can be invested in a single case, contingent fee arrangements present significant risk to the financial stability of the firm. The law firm's ability to select profitable claims is paramount to the success of this practice but large firms frequently do not have mechanisms or processes for managing and promoting effective case selection, let alone a portfolio of such cases.

Litigation finance addresses these challenges while permitting the law firms to maintain their traditional financial management, partner compensation system, and fee structures. Third party funding also enables firms to mitigate or avoid the risks inherent in selecting cases for investment. In this way, litigation finance empowers entrepreneurial litigators to build their practices without having to rely solely on representing large corporations.

Lake Whillans is pleased to have the opportunity to provide funding to entrepreneurial lawyers to represent a wide range of clients including small and start-up enterprises in emerging industries and technologies that have been sidelined by unfair business dealings.

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