News & Analysis

Litigation finance offers a lucrative opportunity

There's profit in court cases, as law firms turn to investors to fund legal claims.

Christopher Faille - 3 June 2024

A white paper from New York-based investment firm Corbin Capital hails the market for litigation finance as an "inefficient and fragmented market [that] offers excellent risk/reward opportunities today".

Cesar Bello, a partner at Corbin, says sourcing of opportunities is key to success in this space. "I've been with the litigation finance operation as part of Corbin's investment team for six years now," he says. "That operation was an outgrowth of our broader private credit programme."

Sometimes, Bello says, a law firm will "come to us and make a pitch". But, more generally, sourcing opportunities will arise from the network of ongoing relationships with law firms that Corbin maintains.

As the white paper observes, litigation finance – loans to law firms pursuing legal claims in exchange for a portion of the proceeds of litigation – is a lucrative market. Annual costs and compensation paid within the US tort system amounts to roughly 2.3 percent of gross domestic product. Only 2

… of all lawsuits involve any litigation funding. These two facts allow a … om for growth.

Corbin says "the global litigation funding investment market is expected to experience a double-digit annual growth rate through 2035".

The regulatory environment is also improving for investors. The suspicion of non-lawyers' financing role has come from wariness they will get too involved and end up exerting malevolent control over legal work. Caution is lessening, however, and Corbin is on the lookout for new opportunities that more permissive attitudes are creating.

Returns from litigation finance are both high and uncorrelated, making it a valuable differentiator for many investors with an otherwise conventional portfolio.

Bello says Corbin has invested about $500 million in litigation finance since 2019, with about half that on the books now. There are, of course, risks. There is the operational challenge of lending to the right law firm. The white paper raises the questions: "How well capitalised is a firm? What is their operational infrastructure/case management system like? Where does the law firm sit in the ecosystem [ie, where several firms may be involved in a mass tort litigation and some may take a leading role, while others are serving just to bring in new members]?"

Those are questions about the law firm. There are also questions about the lawsuit. Is it speculative or well grounded in the law and facts? How long will proceedings take, even assuming the case is meritorious, before a judgment or settlement?

David and Goliath

As the Corbin paper indicates, borrowing for litigation is not only for the slingshot-wielding Davids of the economy. Large corporate Goliaths have good reason to finance their litigation. "Many Fortune 500 companies are s[illegible] on valuable legal claims but often need to make hard budgeting [illegible]ns. Third-party financing allows them to monetise those claims in a way that is most accretive to their bottom lines."

There are also accounting considerations. If a company finances a lawsuit with balance sheet cash, it will lower the numbers for cashflow and projections. Also, the report says "any positive outcome is likely to be disregarded as a one-time event and thus excluded from any forward-looking EBITDA/valuation projections. In short, they will get penalised for spending the money and not get much valuation benefit for a positive outcome".

As for timing, Bello says it is not necessary to adopt a case in its early days. "We like to get involved in the seventh or eighth inning. There are other firms that take on the early innings challenge, when of course the risks are greater. We don't do a lot of that."