

Association of Litigation Funders of Australia

Submission to Treasury

**Consultation on the Draft *Corporations Amendment (Litigation
Funding) Regulations 2022***

About the Association of Litigation Funders of Australia

ALFA is a professional body established in April 2018 to enhance the Australian litigation funding industry by:

- providing education, training and information about litigation funding and the litigation funding industry;
- engaging with government, legislators, regulators and other policy makers to help shape the legal and regulatory framework of litigation funding in Australia; and
- promoting best practice and ethical behaviour amongst litigation funders in Australia.

ALFA Funder members are Augusta Ventures, Balance Legal Capital, CASL, Court House Capital, Investor Claim Partner, Ironbark Funding, Litigation Lending Services, Premier Litigation Funding, Southern Cross Litigation Finance and Vannin Capital.

Associate members of ALFA are Banton Group, Cornwalls, Epiq, Johnson Winter & Slattery, KordaMentha, Mayweathers, McGrath Nicol, Piper Alderman and William Roberts Lawyers.

This submission is made on behalf of the members of the Association and represents their collective views, but it does not necessarily represent the individual views of each member.

Summary

- 1 ALFA welcomes the opportunity to make this submission in response to Treasury's consultation on the draft Corporations Amendment (Litigation Funding) Regulations 2022 (**Draft Regulations**). ALFA supports the introduction of the Draft Regulations and agrees with the Explanatory Statement that the current regulatory regime for litigation funding schemes is not fit for purpose.
- 2 The Draft Regulations will amend the *Corporations Regulations 2001* (**Corporations Regulations**) to reinstate the previously longstanding exemptions for litigation funding schemes from the managed investment scheme (**MIS**), Australian Financial Services Licence (**AFSL**), product disclosure and anti-hawking provisions of the *Corporations Act 2001 (Cth)* (**Corporations Act**).
- 3 The reintroduction of these explicit exemptions is consistent with the views expressed by the Australian Law Reform Commission (**ALRC**), the Australian Securities & Investments Commission (**ASIC**), and numerous other stakeholders, that the AFSL and MIS regimes are unsuitable for the regulation of litigation funding arrangements.
- 4 Further, ALFA requests that the Government take two additional steps to ensure the regulation of litigation funding in Australia is fit for purpose and consistent with the Draft Regulations and the Government's stated policy to facilitate access to justice through funded class actions:
 - (a) The Corporations Regulations should be amended to include an explicit exemption for conditional costs schemes from the MIS, AFSL, product disclosure and anti-hawking provisions of the Corporations Act. There is uncertainty about whether conditional costs schemes fall within the scope of these provisions, and since 2013 ASIC has granted temporary relief to address this uncertainty. However, the current ASIC instrument granting this relief is due to expire on 31 January 2023 and ASIC has advised it is considering whether to extend the instrument. An exemption for conditional costs schemes is consistent with the purposes of the Draft Regulations and should be introduced as part of the Draft Regulations.
 - (b) The Government should make further regulations to exclude litigation funding arrangements generally from the application of the National Credit Code¹. The regulatory requirements of the National Credit Code are similarly unsuited to litigation funding and there is uncertainty as to which funding arrangements those requirements apply. As a result, in 2013, ASIC granted temporary relief from these requirements and has maintained this relief to date, by extending it on multiple occasions. However, this relief is also due to expire on 31 January 2023 and the Government should make that relief permanent by regulation.
- 5 If these further regulatory changes are not able to be implemented by 31 January 2023, when the ASIC instruments granting temporary relief are due to expire, ALFA requests that the Government engage with ASIC to ensure that these instruments are extended to maintain the status quo position in the interim.

¹ The National Credit Code is Schedule 1 to the *National Consumer Credit Protection Act 2009* (Cth)

Background

- 6 Between 2009 and 2012, three appellate court decisions held that certain litigation funding arrangements:
- (a) were subject to the MIS provisions of the Corporations Act - *Brookfield Multiplex Limited v International Litigation Funding Partners Pte Ltd* (2009) 180 FCR 11 (**Brookfield**);
 - (b) were 'financial products' within the meaning of s 763A of the Corporations Act, and that the relevant litigation funder was therefore required to hold an AFSL - *International Litigation Partners Pte Ltd v Chameleon Mining NL* [2011] NSWCA 50; and
 - (c) constituted a 'credit facility' within the meaning of reg 7.1.06 of the then Corporations Regulations, meaning that the National Credit Code could apply to litigation funding arrangements - *International Litigation Partners Pte Ltd v Chameleon Mining NL (Receivers and Managers Appointed)* (2012) 246 CLR 455.
- 7 These decisions caused significant disruption and uncertainty in the litigation funding industry, as the AFSL and MIS regimes impose a suite of registration, licensing, disclosure and conduct requirements unsuited to litigation funding arrangements. As Justice Lee recently observed, 'the characterisation of litigation funding arrangements as managed investment schemes is a case of placing a square peg into a round hole'.²
- 8 In response, in 2013, the then Federal Government introduced regulations exempting litigation funders from the requirement to hold an AFSL and the requirements of the MIS regime, subject to funders maintaining appropriate conflict of interest policies. The Explanatory Statement to the exempting regulations stated:³
- The Federal Court's decision would have imposed a wide range of requirements that apply to MIS, such as registration, licensing, conduct and disclosure requirements on litigation funders and their arrangements with their clients. The Government considers that these requirements are not appropriate for litigation funding schemes. The Government supports class actions and litigation funders as they can provide access to justice for a large number of consumers who may otherwise have difficulties in resolving disputes. The Government's main objective is therefore to ensure that consumers do not lose this important means of obtaining access to the justice system.
- 9 Further, to address remaining concerns that some aspects of litigation funding were not covered by the exemption regulations, in 2013 ASIC also granted temporary relief:
- (a) to litigation funding arrangements generally from the application of the National Credit Code;⁴ and
 - (b) to litigation funding arrangements funded by conditional costs agreements ('conditional costs schemes') relief from the requirements of the MIS, AFSL, product disclosure and anti-hawking regulatory regimes.⁵
- 10 The instruments granting this relief were remade in January 2020 – ASIC Credit (Litigation Funding - Exclusion) Instrument 2020/37 (**Credit Code Instrument**) and ASIC Corporations

² *LCM Funding Pty Ltd v Stanwell Corporation Limited* [2022] FCAFC 103, [7].

³ Explanatory Statement, Select Legislative Instrument 2012 No 172, 1.

⁴ Class Order [CO 13/18] *Funded representative proceedings and funded proof of debt arrangements exclusion from the National Consumer Credit Protection Act 2009* (Cth).

⁵ Class Order [CO 13/898] *Representative proceedings and proof of debt arrangements funded by conditional costs agreements*.

(Conditional Costs Schemes) Instrument 2020/38 (**Conditional Costs Instrument**) – and these instruments are now due to expire on 31 January 2023.

- 11 In its 2018 Report on Class Action Proceedings and Third-Party Litigation Funders, the ALRC concluded that improved court oversight of litigation funding, rather than the application of the AFSL and MIS regulatory framework, was the better approach to regulating litigation funding in Australia.⁶ This also reflected the views of ASIC, which considered the courts to be ‘better placed to regulate litigation funders, through court rules and procedure, oversight and security for costs’,⁷ than the application of a regulatory regime not intended or designed for litigation funding.
- 12 Despite the ALRC’s recommendations, and opposition from a wide range of stakeholders, in July 2020 the previous Federal Coalition Government amended the Corporations Regulations to require litigation funders operating in Australia to hold an AFSL and to subject litigation funding arrangements for class actions to the requirements of the MIS regulatory framework.⁸ These requirements have applied since 22 August 2020, subject to certain temporary relief granted by ASIC to manage the transition to the new regime. They formed part of a suite of reforms sought to be introduced by the previous Government (opposed by ALFA at the time) aimed at restricting third-party funding of class actions, for the benefit of narrow sectional interests at the expense of greater access to justice.
- 13 In May 2022, a new Federal Government was elected with the stated intention of taking a markedly different approach to the regulation of litigation funding and class actions to that of its predecessor.⁹ ALFA welcomes this change in approach, which is reflected in the Draft Regulations.
- 14 Further, in June 2022, the Federal Court in *LCM Funding Pty Ltd v Stanwell Corporation Limited* [2022] FCAFC 103 (**LCM**) held that the decision in *Brookfield* was ‘plainly wrong’, and that a litigation funding scheme relating to a class action does not fall within the description of a MIS.
- 15 Prior to these events, in July 2021 ASIC issued a consultation paper in which it indicated that it was ‘not currently minded’ to extend the operation of the Credit Code and Conditional Costs Instruments.¹⁰ It would appear this was a response to the policy position of the former Coalition Government and concerns expressed by the Senate Standing Committee for the Scrutiny of Delegated Legislation that exemptions from primary legislation should not continue indefinitely.¹¹
- 16 ALFA understands that ASIC is now reconsidering its position in light of the decision in *LCM* and the different policy position of the new Federal Government on funded class actions. ALFA is not aware whether ASIC has reached a new position on these matters or by when it may do so. ALFA remains concerned that there would be significant disruption to the availability of litigation funding in Australia if these exemptions were permitted to lapse.

Draft Corporations Amendment (Litigation Funding) Regulations 2022

- 17 ALFA supports the introduction of the Draft Regulations, which will bring the law back in line with the position prior to August 2020, and notes the following key features:

⁶ ALRC Report 134 on Integrity, Fairness and Efficiency – An Inquiry into Class Action Proceedings and Third-Party Litigation Funders, 161-2 [6.37].

⁷ Ibid.

⁸ Corporations Amendment (Litigation Funding) Regulations 2020.

⁹ ‘Labor to scrap class action funding regulations’, Australian Financial Review, 20 June 2022.

¹⁰ ASIC Consultation Paper 345, *Litigation funding schemes: guidance and relief*, 7 July 2021, [116].

¹¹ ASIC Consultation Paper 345, [109]-[111].

- (a) The Draft Regulations provide that litigation funding schemes are outside the definition of a MIS, and that the MIS provisions of the Corporations Act do not apply to these arrangements, making explicit in the Corporations Regulations the position following the decision in *LCM*;
 - (b) Interests in litigation funding schemes will continue to be classified as ‘financial products’. This allows for such interests to be subject to the further explicit exemptions in the Draft Regulations referred to below;
 - (c) The Draft Regulations provide an explicit exemption for all litigation funding schemes from the Corporations Act’s requirement to hold an AFSL. This brings litigation funding schemes for class actions in line with the current requirements for other litigation funding arrangements with respect to AFSL requirements; and
 - (d) The Draft Regulations exempt litigation funding schemes from the Corporations Act’s anti-hawking and product disclosure provisions, meaning that all litigation funding arrangements are now treated the same for the purposes of these provisions.
- 18 While the decision in *LCM* clarified that the MIS requirements do not apply to litigation funding arrangements, ALFA welcomes the certainty provided by making the position explicit in the Corporations Regulations. ALFA also welcomes the introduction of the further exemptions to the AFSL, anti-hawking and product disclosure requirements.
- 19 The Draft Regulations are also in accordance with the views expressed by the ALRC, ASIC and numerous other stakeholders, that the current AFSL and MIS regulatory regimes are unsuited to the regulation of litigation funding. They return the regulation of litigation funding to the position pre-August 2020, a period when litigation funding of class actions operated efficiently to promote access to justice in Australia.
- 20 Finally, the Draft Regulations obviate the need for ASIC to continue to grant temporary relief from certain aspects of the MIS and AFSL regulatory regimes and provide stakeholders with the certainty required to invest in the litigation funding industry in Australia. Further regulatory changes required to remove the remaining uncertainty in relation to conditional costs schemes and the application of the National Credit Code are addressed below.

Exemptions for conditional costs schemes

- 21 Since 2013, ASIC has provided temporary relief for conditional costs schemes from the MIS, AFSL, and product disclosure anti-hawking requirements of the Corporations Act, in response to industry concerns that they were not covered by the 2013 exemption regulations.¹² Those concerns will continue under the proposed definition of ‘litigation funding scheme’ in the Draft Regulations.
- 22 Under ASIC’s Conditional Costs Instrument, a ‘conditional cost litigation scheme’ is defined as a MIS for participating in and conducting legal proceedings where members fund their legal costs under a ‘conditional costs agreement’.¹³ A conditional costs agreement is a costs agreement where ‘the payment of some or all of the legal costs is conditional on the successful outcome of the matter to which those costs relate’.¹⁴

¹² ASIC Consultation Paper 345, [4].

¹³ ASIC Corporations (Conditional Costs Schemes) Instrument 2020/38, cl 6.

¹⁴ ASIC Corporations (Conditional Costs Schemes) Instrument 2020/38, cl 5; *Legal Professional Uniform Law Application Act 2014* (Vic), s 181.

- 23 As with litigation funding arrangements generally, the requirements of the MIS and AFSL regimes are entirely unsuited to conditional costs schemes, particularly where they would capture conditional costs arrangements entered into directly between a lawyer and participants in a class action.
- 24 The Explanatory Statement to the Draft Regulations specifically identifies that they are intended to bring the regulation of litigation funding schemes into line with the regulation of conditional costs schemes, as provided by the Conditional Costs Instrument. It would be a perverse outcome if, after the introduction of the Draft Regulations, the Conditional Costs Instrument was permitted to lapse, creating an inconsistency between the regulation of litigation funding schemes and conditional costs schemes, and exposing funders and scheme members to unsuitable and expensive regulatory requirements.
- 25 In its recent consultation paper, ASIC indicated that it was considering not extending the Conditional Costs Instrument, in part due to the concerns expressed by the Senate Committee that temporary relief should not become a de facto amendment of the primary legislation.¹⁵ However, allowing the instrument to lapse would have precisely that effect, by removing the exemptions that have been in place since 2013. This would also be contrary to the new Federal Government's stated policy to remove inappropriate impediments to funded class actions.
- 26 Rather than ASIC remaking the Instrument, however, ALFA considers that the Government should instead amend the Corporations Regulations to incorporate the exemptions currently contained in the Conditional Costs Instrument. This could be achieved by amending the Draft Regulations to incorporate the operative parts of Parts 2 and 3 of the Conditional Costs Instrument (with appropriate textual amendments).
- 27 This approach would address the Senate Committee's concern about ASIC's temporary relief being extended indefinitely. It also would ensure that the Draft Regulations achieve their stated purpose of bringing litigation funding schemes into line with how other litigation funding arrangements, including conditional costs schemes, are regulated.

Exemption from the National Credit Code

- 28 As set out above, since 2013, ASIC has provided temporary relief excluding litigation funding arrangements generally from the application of the National Credit Code (Schedule 1 to the *National Consumer Credit Protection Act 2009* (Cth)).
- 29 ALFA supports the continuation of this exemption, given the unsuitability of the requirements of the National Credit Code to litigation funding arrangements. However, ASIC has indicated that it may not extend the Credit Code Instrument beyond 31 January 2023, due to the concerns raised by the Senate Committee, referred to above.¹⁶
- 30 If ASIC fails to extend the instrument, it will have the effect of disrupting the status quo as it has stood since 2013, exposing litigation funders and their clients to unnecessary and ill-suited regulatory requirements. Litigation funders would have to implement a raft of changes to comply with these requirements. These changes would be expensive to implement, likely driving up the costs of litigation financing for consumers and creating artificial barriers to access to justice.
- 31 ALFA will continue to engage with ASIC to seek an extension to the Credit Code Instrument. However, we consider the best course is for the Government to make permanent the

¹⁵ ASIC Consultation Paper 345, [109]-[111].

¹⁶ *Ibid.*

exemptions for litigation funding arrangements by regulation, pursuant to section 6(13) of the National Credit Code. This would avoid the need for ASIC to continually extend the Credit Code Instrument and provide certainty for the litigation funding industry and market.

Conclusion

- 32 ALFA supports the new Federal Government's policy to ensure the regulation of litigation funding in Australia is fit for purpose, as reflected in the Draft Regulations. Consistent with that policy and the purpose of the Draft Regulations, the Government should also enact regulations to make permanent the temporary exemptions for conditional costs schemes and relief from the application of the National Credit Code to litigation funding arrangements generally.
- 33 If these regulatory changes are not able to be implemented by 31 January 2023, when ASIC's temporary relief is due to expire, the Government should engage with ASIC to ensure this relief is extended pending further regulatory change.

Association of Litigation Funders of Australia

30 September 2022