

Bottom of the class?

By **Edward Machin** - 22 August, 2012

When Australia's embryonic litigation funding industry was granted a statutory exception to the common law prohibition against maintenance and champerty, in 1995, few could have predicted how significant the decision would turn out to be.

Less than two decades later, however, and Australia is home to the world's most prominent funding market, with both corporate and public interest in the industry yet to abate. Unsurprisingly, much of it focuses on what has long been the funders' calling card: bankrolling class-action lawsuits.

The Australian government has also been quick to endorse both class-actions and the companies that fund them – so much so that, on 12 July, funders were told they could invest in class-actions without a financial services licence, because they were not a “managed investment scheme” under the Corporation Act. (The amendments, which also include a duty to manage conflicts of interest, take effect on 13 January 2013.)

“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,” Canberra said in an explanatory statement accompanying its Corporations Amendment Regulation 2012 (No 6) (<http://www.comlaw.gov.au/Details/F2012L01549>). “The government's main objective is therefore to ensure that consumers do not lose this important means of obtaining access to the justice system.”

But here's the funny thing about funders: they actually *want* regulation. Which is why **Wayne Attrill**, an investment manager at **IMF (Australia)**, the country's largest funder, says the business community, academia and funding firms alike don't think the regulations will change things for the better. (They also overturn in statute the 2009 Federal Court ruling in *Multiplex*, which found that a litigation funding arrangement was a managed investment scheme.)

“The Australian government had an opportunity to mandate the on-going, principled development of the industry by requiring all funders to be licensed, but they missed it,” says Attrill, whose firm recently recouped AUD 60 million (<http://www.cdr-news.com/categories/litigation/australian-court-approves-record-settlement-in-centro-pwc-class-action>) in the record Centro PwC class-action settlement.

And though the regulations exclude litigation funding arrangements from managed investment schemes, there's a potential defect in such thinking, he says.

“While the regulations only cover certain types of funding arrangements – i.e. those where the funder and lawyers are not members of the scheme – in Australian multi-party litigation the funder and lawyers are *always* members of a scheme,” Attrill explains. “So the regulations will have little, if any, impact.”

Even if effective, “they do not go far enough,” he adds. “They do not require funders to be licenced, as IMF is, or impose any capital adequacy requirements on funders.”

In other words, just about anyone can set themselves as a litigation funder, whether they have sufficient capital to meet their financing obligations or not.

What's in a name?

That these “inadequately resourced subsidiaries” may come from abroad simply compounds the problem, says **Michael Legg**, an associate professor at the **University of New South Wales** law faculty, because such ‘funders’ would be beyond the reach of Australia’s courts.

“The only partial protection against this is an order for security for costs by the courts, which requires that a bank guarantee or other form of security is provided to meet the costs of a defendant if the proceedings are unsuccessful,” Legg says.

“However, it is common practice that the amount of security that a court generally requires to be posted is substantially lower than the costs actually incurred by the defendant,” he adds. “As a result, the representative party in a class-action may be liable for those costs if the litigation funder is insolvent. Where those people have inadequate resources, which is highly likely as they required litigation funding to commence the proceedings, they may become bankrupt.”

Australia’s funders are similarly concerned that wanton disregard for good funding practice is liable to sully their good name, with disastrous reputational results for the industry as a whole.

“The risk is that a rogue operator might decide to fund a major piece of litigation here, lose it and then go into liquidation rather than pay adverse costs,” Attrill says. “So far this hasn’t happened, and we don’t want it to. This is why we endorse licencing for all funders.”

The **Law Council of Australia** – the country’s largest representative body for the legal profession, with some 56,000 practitioners on its books – likewise says “all funders” should be required to hold an Australian Financial Services Licence (AFSL), thereby enabling the Australian Securities and Investments Commission to supervise potential conflicts of interest.

It would, however, “remain necessary for the Corporations Regulations to exempt litigation funders from the managed investments scheme provisions of the Corporations Act,” says the organisation’s president, **Catherine Gale**.

“Litigation funders have facilitated the development of large-scale class-actions in Australia, [and] without litigation funders many representative proceedings could not proceed due to the high costs and risk involved,” Gale adds. “There is a strong public policy rationale in favour of representative proceedings, which are the most efficient means of ensuring access to justice where there are a large number of parties whose complaints arise out of a common incident or set of circumstances.”

So Australians back class-actions – that much is clear. But with the High Court currently deliberating whether funders need an AFSL in single-party litigation, as a lower court ruled in *Chameleon Mining*, there may still be trouble ahead for an industry accused of being little more than high-class ambulance chasers.

Indeed, Attrill says recent developments, despite their limited reach, will almost certainly lead to a more heavy-handed approach down the line.

“These amendments reflect the government’s desire to foster litigation funding as a means of improving access to justice and not to burden the sector with over-regulation,” he says.

“However, the government is likely to insist on more stringent regulation of funders in the future as the sector grows and as more foreign-based funders operate in Australia.”

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