ILFA | INTERNATIONAL LEGAL FINANCE ASSOCIATION

5 July 2021

Manager
Market Conduct Division
The Treasury
Langton Crescent
Parkes ACT 2600

By email: MCDLitigationFunding@treasury.gov.au

Dear Manager,

Re: ILFA submission responding to consultation by Treasury and the Attorney General's Department: Guaranteeing a minimum return of class action proceeds to class members

The International Legal Finance Association (**ILFA**)[1] is the only global association of commercial legal finance companies. It is an independent, non-profit trade association promoting the highest standards of operation and service for the commercial legal finance sector.

A number of ILFA members, including the largest legal finance companies in the world, have made submissions responding to a consultation paper from the Australian Government on guaranteeing a statutory minimum return of gross proceeds in class actions to group members (**Consultation Paper**) - effectively a cap on litigation costs and litigation funding fees in Australian class actions - and arguing why there is no basis or justification for such a cap. ILFA provides this submission to emphasize some key common arguments against the imposition of any cap and also to push back against this proposal which would be to the detriment of everyday Australians.

As a threshold matter, whilst the Consultation Paper is framed in terms of "guaranteeing a minimum return of class action proceeds to class members", scrutiny must be directed towards which stakeholders are calling for a cap on litigation costs and funder fees in class actions. Contrary to some assertions, no law firm or funder of which we are aware has supported a 30% cap on returns (which appear to include reimbursement of the legal fees and disbursements as well as the funder's commission) in class actions. Likewise, no consumer or shareholder group, which includes some of the world's largest institutional investors, have called for a 30% cap.

Furthermore, no Australian court has requested that a 30% cap be imposed. The Australian courts have oversight of litigation funding fees, which they exercise when determining whether to approve a class action settlement. By contrast, major corporate interests, vocally supported by like-minded interest groups, have been pushing relentlessly for a suite of reforms that make the prosecution and funding of class actions in Australia more difficult and expensive. In that light,

[1] https://www.ilfa.com/

one must seriously question whether this proposal—driven as it is by lobbying interests – is really in the best interests of Australians.

Further skepticism of the proposed cap is warranted given that absolutely no data or analysis has been provided to show why a 30% cap should be imposed on law firms and funders in Australian class actions as representing a fair and proportionate return for the assumed risks. Likewise, no case law has been cited to justify why a 30% cap is warranted. Rather, references to "windfall profits" and a purported "feeding frenzy" absent any empirical data demonstrating that there is a problem that requires such heavy-handed intervention seems to have formed the basis of the proposals. Recent studies by Australian law firms, Allens and King & Wood Mallesons, both found that, although there was a small increase in class actions filed in the past year, the proportion of class actions funded by litigation funders is actually in substantial decline.[2]

It is worth noting that the proposed cap is the most recent of many class action reforms where attempts have been made during a global pandemic to make changes absent any consultation or analysis. In 2020, funder licensing and managed investment scheme regulation were imposed on funders prior to any consultation with stakeholders (or ASIC). In recent days, the Senate Economics Reference Committee released a report denouncing attempts to permanently weaken Australian continuous disclosure laws. The Committee found that no cogent or evidence-based reasons were provided for these reforms; there was a complete failure to identify even one example of an "opportunistic class action" being brought by a funder and no effort to define what that moniker means; there was no evidence to support claims that D&O policy costs will be reduced at all by these reforms; and there was no analysis of the impact such reforms would have on Australians. The Committee concluded that "numerous claims [that] have not withstood even the slightest degree of scrutiny" and "[i]nstead of broad consultation and sober analysis, the government opted for a process that was, from a public policy perspective, indefensible." This pattern of trying to force through baseless class action reforms without consultation, during a global pandemic to appease lobbying interests at the expense of Australians must end.

This proposed cap is arbitrary. It is clear that, in accordance with the Australian Government's own internal processes, a thorough cost-benefit analysis of the impacts on all relevant stakeholders should be undertaken before any cap is considered.

What is also clear is that no consideration has been afforded in the Consultation Paper to the significant costs and risks that funders assume, including funder exposure to adverse cost orders and cases that lose or settle for an amount less than the amount of legal fees expended on a class action. Funders' internal costs, which are not passed on to group members, have also not been taken into account.

When those costs and risks are properly considered, it is evident that funders provide non-recourse funding from the outset of a class action with a potential risk of losing 165 - 200 % of their investment whilst group members assume no downside risk. The nature of that risk makes this type of finance very different from other types of investments that various parties opposing class

[2] Allens, *Class Action Risk 2021,* March 2021 and King & Wood Mallesons, *Winter is coming: Class action battles surge to new record,* 24 May 2021.

actions in the recent Australian parliamentary committee inquiry tried to use in an attempt to draw analogies and conclusions about what profits are, and are not, reasonable in this sector.

There has also been no consideration of the barriers and cost that flow from new funder regulations that were imposed in mid-2020. According to a recent article in Law.com International:

> *"The Australian Securities and Investments Commission, which issues the licenses, told Law.com International that litigation funding licenses have so far been issued to six entities—only a fraction of the 25 litigation funders active in Australia identified in a government-commissioned inquiry into class actions and litigation funding in December 2018.*"[3]

Furthermore, a separate unintended consequence that appears to have not been considered in the Consultation Paper is its differential treatment of law firms and funders. In a complete reversal of the approach taken by the Australian Law Reform Commission (ALRC), the recent regulation of the funding of class actions has focused entirely on funders notwithstanding that law firms can run class actions on a "no win no fee" basis as well as on a contingency fee basis for class actions filed in Victoria (following the Victorian legislative reform that came into effect in July 2020).

To date, no justification has been provided as to why funders are subject to one set of rules regarding licensing, funder reporting and disclosures, whilst those rules do not apply to law firms funding the class actions that they run or fund.

Whilst the proposed 30% cap has been painted as simply an initiative to further regulate funders and limit any profits they can achieve in successful cases, this proposal seems to be an attempt to dry up funding for Australian class actions and place strong downward pressure on the settlements that group members will receive in Australian class actions. Those pushing for these baseless reforms are well-aware that a cap will reduce the number of Australian class actions and the amounts that defendants need to pay to settle such class actions. Indeed, a number of ILFA's members have drawn attention to the fact that many class actions will become uneconomic to fund in the event of the imposition of a 30% cap.

In March 2021, PwC published a report that analyzed the impact of imposing a statutory minimum return to group members using historic publicly available class action outcomes.[4] PwC found that a statutory minimum return of 70% to group members (that is, a 30% cap on fees) would mean 36% of cases would not have proceeded as the 30% cap would not have covered the litigation costs alone and the funder would have received no commission) and a further 55% of cases would have been impacted as the funder's commission would have been reduced.

[3] *Only a Handful of Litigation Funders Obtain Licenses Under New Australia Law*, Law.com International, 8 June 2021.

[4] PwC, *Models for the regulation of returns to litigation funders*, 16 March 2021. Omni Bridgeway commissioned the report to analyze the impact of imposing a statutory minimum return to group members.

It would be unwise for Australians, whom the class action regime is supposed to protect, in their capacity as employees, consumers, shareholders and citizens, to think this proposal is in their best interests.

Sincerely,

Leslie Perrin

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Chairman

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