MENZIES RESEARCH CENTRE SUBMISSION

Treasury Laws Amendment (Measures for Consultation) 2021:

Litigation Funders

October 2021

About the Menzies Research Centre

The Menzies Research Centre is a think-tank that champions Liberal principles and advocates for a free, just and prosperous Australia.

It draws inspiration from Sir Robert Menzies, Australia's longest-serving prime minister and an exceptional articulator of Australian Liberalism.

The Centre conducts public policy research, publishes books, hosts live events and maintains an active media presence promoting the values that have made Australia one of the most free and prosperous nations in the world.

The Centre supports freedom, human dignity, personal responsibility, and private enterprise as the mainstays of modern Australian Liberalism.

It is committed to a just and humane society in which every individual has the opportunity to flourish.

The Menzies Research Centre advocates for effective, efficient and democratic government while encouraging independence, innovation and reward for effort.

It supports the institution of the family as the foundation for a strong and dynamic society bound by shared values and mutual obligations in which every individual enjoys equal moral worth.

The Centre is affiliated with the Liberal Party of Australia.

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Submission

Introduction

The Menzies Research Centre is pleased to make a submission to the *Treasury Laws Amendment (Measures for Consultation) Bill 2021: Litigation Funders.* We believe that class actions are an efficient and effective vehicle to bring justice to a class of Australians who have been wronged.

Civil law serves to quench the thirst for justice, not the thirst for profit. Its primary purpose is to compensate citizens whose rights have been infringed. Any remittances that lawyers and funders may make along the way should be reasonable and incidental.

In the field of class actions, however, there is a risk that profit may become the chief motivation for initiating proceedings, if it is not already. Lawyers are shopping for aggrieved clients, not the other way round. Lawyers and third-party litigation funders are shaping proceedings. It is they who are deciding whether justice should be dispensed in the court or settled outside. The decisions frequently appear to be made in their own best interests, favouring the return on their own investment rather than what is best for the client.

The introduction of provisions allowing plaintiffs to litigate collectively in 1992 was well intentioned. It was designed to make justice more affordable by sharing risk and costs. That noble aim has been corrupted by predatory practices by legal companies backed by investors looking for a return on capital.

Forget the heroic narrative of the passionate lawyer acting pro-bono for the marginalised and vulnerable. Three quarters of these are so-called “funded cases”, investment vehicles for financiers, frequently from the US, who bet their money on a successful court finding or settlement and pocket the proceeds.

Awards for damages that are intended to redress the conditions a plaintiff enjoyed before the wrong was committed are being eaten up by the professionals commissioned to help.

In recent times the average amount paid to plaintiffs in such cases was a mere 39 per cent of the settlement proceeds. The average commissions paid to litigation funders increased to 24 per cent and legal fees to 37 per cent. Nearly two thirds of the compensation intended for their clients is being taken by the promoters of class actions.

The damage suffered by injured parties is tangible. They cannot begin to replace a home or business lost in a fire or flood if they receive half or less than half of the replacement cost.

Our justice system has hurtled along the American path and then some. The returns available for investing in litigation in Australia exceed, by a considerable margin, the returns available in nearly every other alternative asset class in the world. Two of the largest litigation funders operating in Australia, Omni Bridgeway and Litigation Lending Services returned ROICs of 154% and 165% respectively. Their success rate is between 89 - 94 per cent.

The returns, in other words, are 17 times larger than those that might be achieved by investing in ASX 200 shares, and nearly 12 times the benchmark returns earned by US Hedge Funds.

The checks and balances that apply to other forms of consumer finance no longer apply. Indeed, since litigation funding was expressly exempted from investment regulation in 2013 by then Labor Minister Chris Bowen, the industry has flourished. The close ties between the Labor Party and Maurice Blackburn, the industry's largest class action player, should be noted.

The submission highlights the advent of common fund orders which allow litigation funders to charge commission on all members of the class whether or not they have consented to the action being undertaken on their behalf. It allows class actions to commence on behalf of hundreds of thousands of class members without their knowledge. All that is required is for one member of the class to consent to their involvement.

Unlike lawyers, litigations funders have no duty to act in the best interests of the plaintiff. Rather their duty is to maximise returns for investors, which may mean a premature out-of-court settlement that may not be in the best interests of the injured party.

This proposed legislation addresses conflicts of interest, the lack of appropriate disclosure and control of proceedings. It seeks to properly regulate foreign funders through the proper application of character and qualification requirements and the same level of prudential supervision that applies to other investment vehicles.

Justice apart, there is a strong economic imperative to prioritise the reform of this area of civil law. The escalating cost of proceedings is significantly adding to the cost of doing business at a time when the economy is still in uncertain territory. Much of the burden of these costs is ultimately carried by ordinary Australians through the loss of jobs or wages or reduced dividends towards their retirement savings.

COVID-19 has demonstrated the need to expand domestic enterprise including manufacturing. Yet legal liabilities are becoming yet another disincentive for companies to operate here.

The series of external shocks we have experienced this year has highlighted the measures we must take to ensure we emerge stronger on the other side. Legal reform of the nature we describe must be high on the list.

There is nothing fair about the system as it currently stands. Its impact is steeply regressive, rewarding some of the richest professionals in the country at the expense of those who can least afford it.

Litigation that delivers private profits for a few at the expense of the many is an injustice that cannot be allowed to stand.

How litigation finance works

Litigation finance operates in a manner very similar to private equity. Litigation funders raise capital from third party investors. That capital is then deployed to fund legal fees to pursue class actions run by plaintiffs' lawyers. In exchange, the litigation funders are entitled to a 'commission' or share of the proceeds that the class recovers, whether by way of settlement or final judgement.

Funding is usually provided on the basis that if the case is lost the funder will be liable to pay the defendant's costs.

Plaintiffs' lawyers are attracted to litigation funding because their fees are effectively underwritten or paid for by the litigation funder.

Litigation finance is not limited to multiparty class actions. It extends to all disputes and modes of resolution including arbitration, traditional corporate litigation, and insolvency matters.[1] In Australia, it appears to be used predominantly in class actions. An investor presentation by Omni Bridgeway (IMF Bentham) from May 2020 reveals that, as of 30 April 2020, 'multi party' matters (i.e. class actions) comprise 27% of its global litigation funding portfolio. However, the same presentation also reveals that 'multi party' matters comprise 70% of its Australian investment portfolio.[2]

Litigation funders investing foreign capital

> *"Litigation financing was 'invented' in Australia [and] Litigation Capital Management, along with IMF Bentham (ASX listed) and Litigation Lending Services (private) were the pioneers."*
>
> *LCM Management Presentation 'LCM IPO on the ASK, November 2016*

There are at least 33 litigation funders operating in Australia.[3] Most of these are foreign entities, or locally created companies investing on behalf of offshore funds.

Similar to private equity funds, these offshore funds are often structured as investment fund vehicles and raise money from external investors – usually sophisticated investors and pension funds. Some funders invest through advantageous tax jurisdictions, including Jersey, the United Kingdom and the Cayman Islands.

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[1] Omni Bridgeway, Investor Presentation, May 2020 (Page 20).
[2] Ibid (Page 20).
[3] Australian Law Reform Commission, An Inquiry into Class Action Proceedings and Third-Party Litigation Funders, January 2019 (appendix G).

Even funders that reside in Australia have restructured their operations to act more like international fund managers to access foreign capital. For example, Omni Bridgeway (formerly known as IMF Bentham)'s Fund 5 is run through a Cayman Island based entity. It has raised investments of up to US$1 billion from foreign investors to deploy into Australia and the region.

ASX disclosures indicate that major investors in this fund include investment firms in Singapore, Europe and North America, including a cornerstone investment from endowment funds associated with Harvard University.[4]

The global litigation fund market is currently valued at US$10.916 billion and is expected to grow to US$22.373 billion by 2027 at a compound annual rate of 8.3 per cent.[5] Some US commentators suggest that the market is potentially as large as US$50 billion - $100 billion. [6] A significant amount of these funds are earmarked for deployment in Australia.

Who do class actions benefit - class members or litigation funders?

The litigation funding industry is generating extraordinary profits for its investors – profits that are paid out of the compensation awarded to their clients, the class members.

Indeed, the point has been reached where even some litigation funders are acknowledging that the returns being generated by the industry are excessive and regulation to protect consumers and class members is required.[7]

In examining this issue two questions must be considered. First, the percentage of the compensation awarded to class members that is taken by the litigation funders and plaintiffs' lawyers. Second, the returns being generated by the funders through their involvement in the proceedings.

Returns to class members

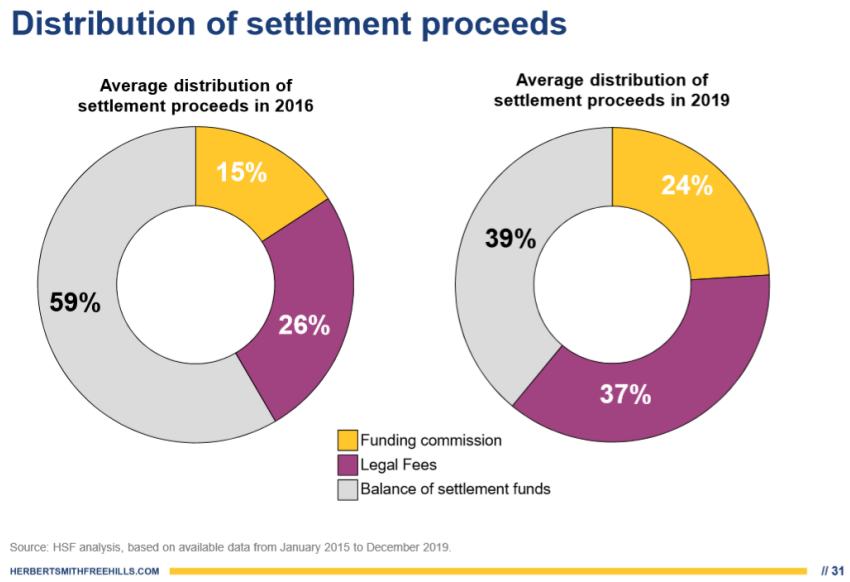
In 2016, on average 59 per cent of settlement[8] proceeds went to class members whilst the average percentage paid out of these damages as a funding commission was just 15 per cent. The balance went to the plaintiffs' lawyers.[9]

By 2019, the average amount paid to plaintiffs had fallen to just 39 per cent of the settlement proceeds, whilst commissions paid to litigation funders increased to 24 per cent and legal fees

[4] IMF Bentham, ASX Disclosure, 20 June 2019.
[5] Absolute Market Insights, global litigation funding investment market, yahoo finance, 18 February. 2020.
[6] https://www.marketwatch.com/story/in-low-yield-environment-litigation-finance-booms-2018-08-17
[7] Omni Bridgeway (IMF Bentham) ASX release – 14 May 2020
[8] While class members may receive compensation following a judgement or the settlement of their claim, most class actions settle before judgement. Accordingly, we have used the term 'settlement' to refer to both modes of resolution.
[9] HSF Analysis, Based on available data from January 2015 to December 2019.

to 37 per cent.[10] Nearly two thirds of the compensation intended for their clients is being taken by the promoters of class actions.

Figure 1: Decreasing Returns to Class Members



The Australian Law Reform Commission (ALRC) reached a similar conclusion. It reported that in actions settled between 2013 and 2018 class members in actions without a third-party litigation funder received a median return of 85 per cent. When a funder was involved that amount fell to just 51 per cent.[11]

Figure 2: Median Return to Class Members

Median funder commission rate	**30%**
Median return to class member (funded)	**51%**
Median return to class member (un-funded)	**85%**

Clearly this is both unacceptable and unsustainable.

In many cases class actions are commenced seeking compensation for significant losses. The class actions commenced following the major Victorian bushfires or the Brisbane floods are good examples. If class members are forced to surrender fifty per cent or more of the compensation they receive to litigation funders and lawyers, any success they may achieve is

[10] Ibid.
[11] Australian Law Reform Commission, *An Inquiry into Class Action Proceedings and Third-Party Litigation Funders*, January 2019, (Page 83).

illusory. Class members cannot begin to replace a home or business lost in a fire or flood if they receive half or less than half of the replacement cost.

If nothing else, the returns being delivered to class members starkly demonstrates how the class action system has been corrupted for the benefit of the promoters of class actions, the litigation funders and plaintiffs' lawyers, at the expense of class members themselves.

As law firm Allens Linklaters observed:

> *There is […] growing evidence that recent experience has us fast approaching a 'tail wagging the dog' scenario – by which we mean that the promoters' pursuit of profits has become an end in itself and is no longer supporting the objectives of the class action regime.*[12]

Returns to Litigation Funders

Litigation funders earn commissions which are generally expressed as a simple percentage of the compensation awarded to class members. However, like private equity and hedge funds, funders measure their profit using the metric of 'Return on Invested Capital' (**ROIC**). This is a measure of the profit that a funder has made from its investments after the return of the funds it has deployed to run a case.

The returns available to investors in funded litigation are, quite frankly, astonishing. When benchmarked against other asset classes, litigation funders in Australia are generating ROIC returns around seventeen (17) times more than investors in ASX 200 stocks and more than ten (10) times the average global hedge fund and private equity performance.

Even when benchmarked against exceptionally high risk / high return investments such as biotech, the returns of funds are still nearly six (6) times higher.

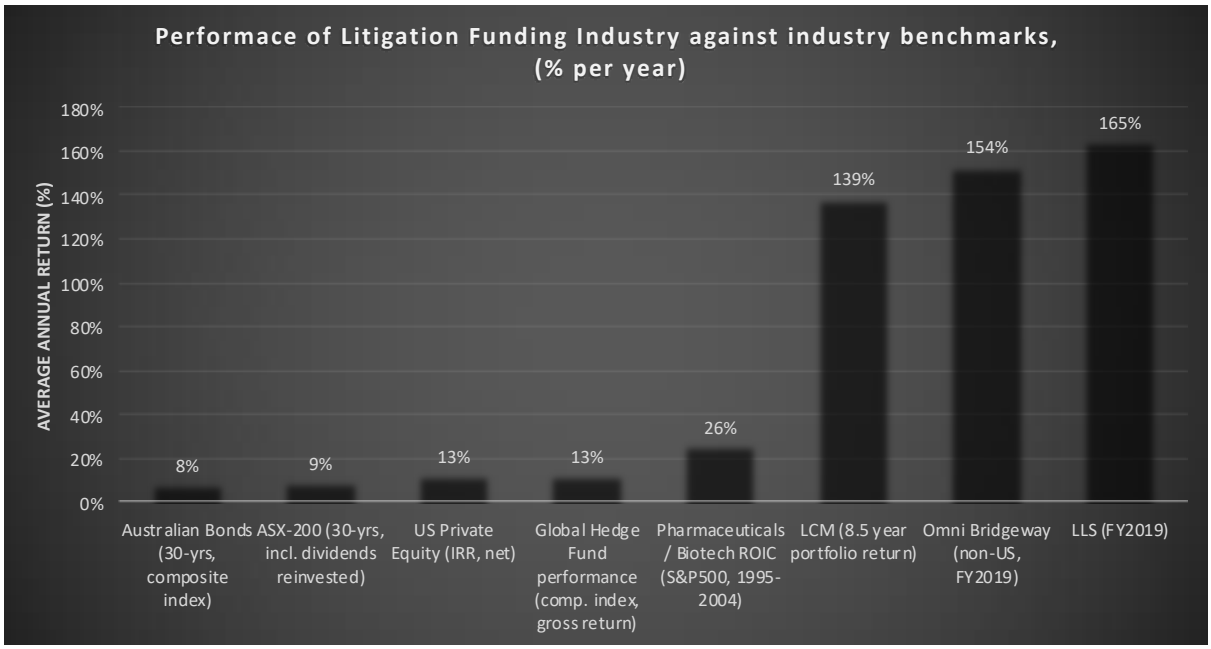
Consider the returns generated by three Australian funders which have disclosed their results:

- LCM disclosed a return of 139% based on an 8.5-year portfolio return.
- Omni Bridgeway's non-US (predominantly Australian) return in FY 2019 was 154%.
- Litigation Lending Services returned 165% in 2019.

These returns are benchmarked against other asset classes in Figure 3.

[12] Allens Linklaters, Class Action Risk, 2018, (Page 6) – emphasis added.

Figure 3: Benchmarked Performance of Australian Litigation Funds



The high returns and low risk of litigation funding make this a tantalising investment class for investors in the current climate of low returns on more traditional forms of investment.

The litigation funding industry seeks to justify these returns by arguing that they are necessary given the risks associated with funding class actions in the event of losing a case and the funder becoming liable for adverse cost orders. However, as demonstrated in Figure 4, the success rate for third-party funded class actions in Australia is between 87 and 94 per cent.

The low risk associated with these investments does not justify the returns generated by Australian litigation funders on any sensible interpretation of corporate finance principles.

Figure 4: Disclosed Success Rate for Litigation Funders

Funder	Investment Duration	Success Rate
Omni Bridgeway (ASX Investor Presentation - Sep 2019)	2.6 Years	89%
Litigation Capital Management (AIM Presentation - Sep 2019)	2.1 Years	87%
Litigation Lending Services (ASIC Annual Report 2018)	2.5 years	94%

The returns in Australia significantly exceed those generated by litigation funders in other jurisdictions, including the United States. Globally, it is estimated that the litigation funding

industry generates annual returns between 29.4 and 43.2 per cent, with average annual returns of about 36 per cent.[13]

Omni Bridgeway (IMF Bentham) has confirmed the lucrative nature of the Australian market as compared to the US in an investor presentation. It revealed that its ROIC for non-US, predominantly Australian litigation investments are currently 3.7 times more profitable than the ROIC for its US litigation operations.[14]

Furthermore, the performance of litigation funding investments are not corelated to other investment classes. Even during times of pandemics such as COVID-19, there is no expectation that stock prices for listed litigation funders should fall. In a recent briefing to investors, Omni Bridgeway (IMF Bentham) has disclosed expert analysis that revealed that its share price is not correlated to the ASX 300 Diversified Financials Index, and that history has shown "Omni Bridgeway's share price has not suffered in the longer term".[15] The analysis also revealed that in times of crisis, rather than its share price dropping Omni has seen its share price increase, first during SARS by 164 per cent and second during the Swine flu outbreak by 26 per cent.[16]

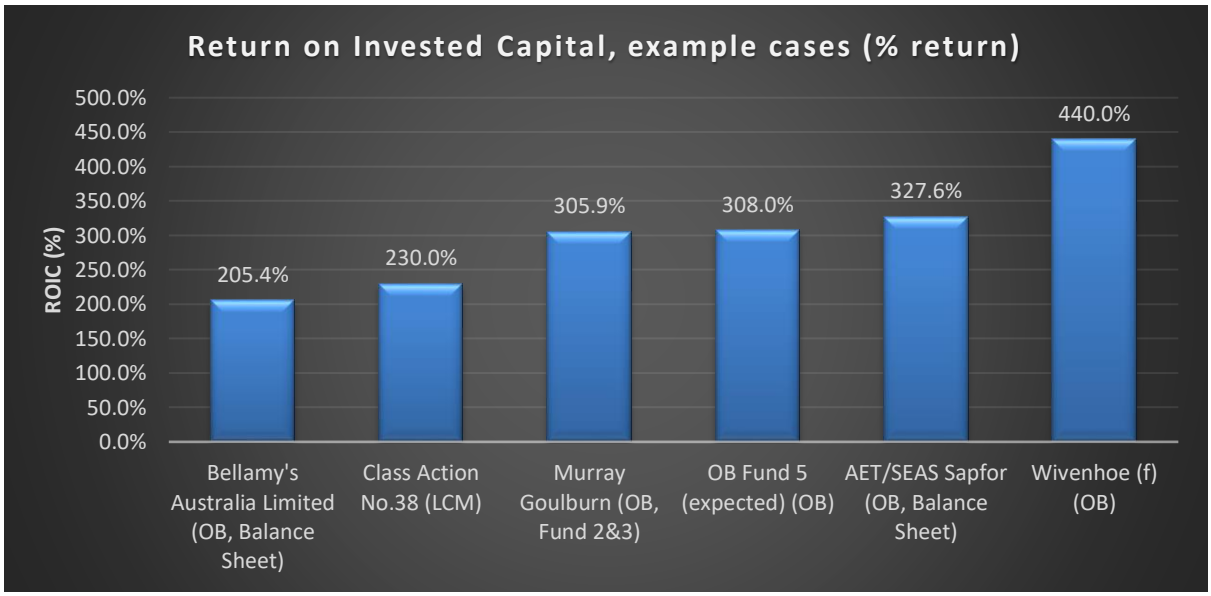
Given these returns, coupled with the fact that the barriers to commencing a class action in Australia are lower than those in the United States[17], it is not surprising that Australia is now the second most attractive class action jurisdiction globally.[18]

[13] Michael McDonald, Finance and Law: Returns to Litigation Finance Investments, above the law.com, July 2016.
[14] Omni Bridgeway, Investor Presentation, March 2020 (Page 13).
[15] Omni Bridgeway, Euroz Conference, March 2020 (page 2)
[16] Ibid.
[17] Samuel Issaharoff and Thad Eagles, *The Australian Alternative: A view from abroad of Recent Developments in Securities Class Actions*, UNSW Law Journal 179, 2015
[18] Herbert Smith Freehills, Litigation Funding on the Rise, 23 May 2018.

Case-by-case Returns of Litigation Funders

Several recent cases funded by Omni Bridgeway (IMF Bentham) correlate to an increasing ROIC well beyond its historic average listed in Figure 5.

Figure 5: ROIC - recent case examples



The current legislative regime for class actions does not contemplate the role of litigation funders. Indeed, litigation funding in its current form didn't exist at the time the relevant legislation was enacted. As the Australian Law Reform Commission observed in its report in 2018 -

> "*It is unlikely that in 1988 the Australian Law Reform Commission could have foreseen the developments in the law relating to class actions that have occurred since then. It certainly would not have foreseen the growth in the involvement of litigation funders.*"[19]

It is even less likely that the ALRC would have foreseen the extent to which the litigation funders have become the beneficiaries of the compensation awarded to class members.

Judges Focus on Percentage Commissions, Not Funder Returns

The litigation funding industry is largely unregulated and there are no statutory or other criteria for determining how litigation funding agreements operate or a funders remuneration should be determined. As a general rule, a litigation funding agreement will provide for the funder to receive a commission determined by reference to a percentage of the compensation the class members receive from the defendant. The litigation funding agreement may also provide for

[19] *ALRC Report – An inquiry into Class Action Proceedings and Third-Party Litigation Funders, January 2019*

the funder to charge a range of other fees and charges in addition to the commission. In some cases, the percentage payable to the funder may increase the longer the case runs.

Similarly, the legislation governing class actions in Australia makes no provision for dealing with the role of litigation funders in class action proceedings. Rather, the courts have been forced to try and develop an appropriate response with very limited assistance.

When a court is hearing an application for the approval of a class action settlement the judge considers a range of issues to determine whether it is 'fair and reasonable'. As part of that process, the court will review the commission and charges sought by the funder and the legal fees charged by the plaintiffs' lawyer. However, instead of considering the profit measures used by funders, such as ROIC, judges instead focus on the commission as a percentage of the compensation awarded to class members with no benchmark or legislative guidance as to what the term 'fair and reasonable' should be interpreted as. Given this, the approach taken by the court in relation to the funders' remuneration is haphazard and undertaken without regard to principles of corporate finance or benchmarks for risk-adjusted rates of return.

The task is made more difficult by the fact that, once a settlement has been reached, the defendant has no interest in delaying approval and thus the final resolution of the matter. For their part, both the litigation funder and the plaintiffs' lawyer representing the class are hopelessly conflicted and unlikely to do anything to jeopardise the approval or delay receiving their often significant remuneration. Unless a class member is willing to appear at the approval hearing with independent lawyers at their own expense to oppose or question the settlement costs or remuneration, nobody will be independently representing the class members.

In most cases, the judge will take a fairly arbitrary view as to an appropriate percentage which is at least in part informed by the overall quantum of the settlement. In other words, the larger the settlement the more likely the court will balk at approving a high percentage. But in each of these approaches, the courts focus entirely on the commission measured as a percentage of the class members' compensation and has no regard to the ROIC profitability measure used by litigation funders.

Consequently, the commission paid to the litigation funder, expressed as a percentage of the compensation awarded to class members, can be reduced by the court while still delivering extraordinary levels of returns when benchmarked against alternative investments.

The Impact of Common Fund Orders

Common Fund Orders

A common fund order is an order made by the court on the application of a litigation funder to require all class members to pay the funder a commission in the absence of any agreement on their part to make such a payment.

Common fund orders enable litigation funders to take a percentage of every class member's compensation regardless of whether the class members have signed a funding agreement, agrees to the payment or is even aware that such an application has been made by the funder.

This is particularly egregious in the context of the Australian opt-out class action system where a funder can commence a class action on behalf of hundreds of thousands of class members in circumstances where no more than one member of the class need consent to their involvement or even be aware that the proceedings have been commenced.

This has huge advantages for litigation funders. They no longer need to go to the trouble of identifying clients and seeking their agreement to join the action and pay the funder a fee or commission. It makes it much easier and quicker to commence a class action and describe a class that is really only limited by the imagination of the person drafting the class description. This mechanism, first approved by the Federal Court in the 2016 'Money Max' decision[20], has enabled funders and plaintiff lawyers to bring larger claims for larger classes without the additional work required to sign up individual class members – the so called 'bookbuild'.

The mechanism has allowed funders to both expand the damages pool, and, by extension, exponentially increase the commissions they can make from a class action.

The class action involving Takata airbags in BMWs is a prime example. In this case only 33 of the potential 200,000 class members had entered into a litigation funding agreement and agreed to the funder's terms. Despite this, the funder sought to have the entire class pay it a commission. In this instance, when the application finally came before the High Court it held that the provision under which the application had been made did not extend to the making of the order.

How Common Fund Orders magnify claim sizes

The use of the common fund mechanism has increased both the number and size of class actions in Australia and the ease with which they are commenced.

20 Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited [2016] FCAFC 148

Given the lack of regulatory oversight, it is difficult to determine the exact size of the litigation funding market in Australia and the impact that the advent of common fund orders has had on the sector. However, some insight is provided into claim sizes through portfolio updates filed by Omni Bridgeway (IMF Bentham) with the ASX.

Omni Bridgeway (IMF Bentham) measures the size of its pipeline of active funded litigation by 'EPV', which it defines as follows:

> "*EPV for an investment where the IMF funding entity earns a percentage of the resolution proceeds as a funding commission is* ***IMF's current estimate of the claim's recoverable amount after considering the perceived capacity of the defendant to meet the claim****.*"[21] (our emphasis)

It is from this amount, once recovered, that Omni Bridgeway (IMF Bentham) derive its commissions. It discloses that:

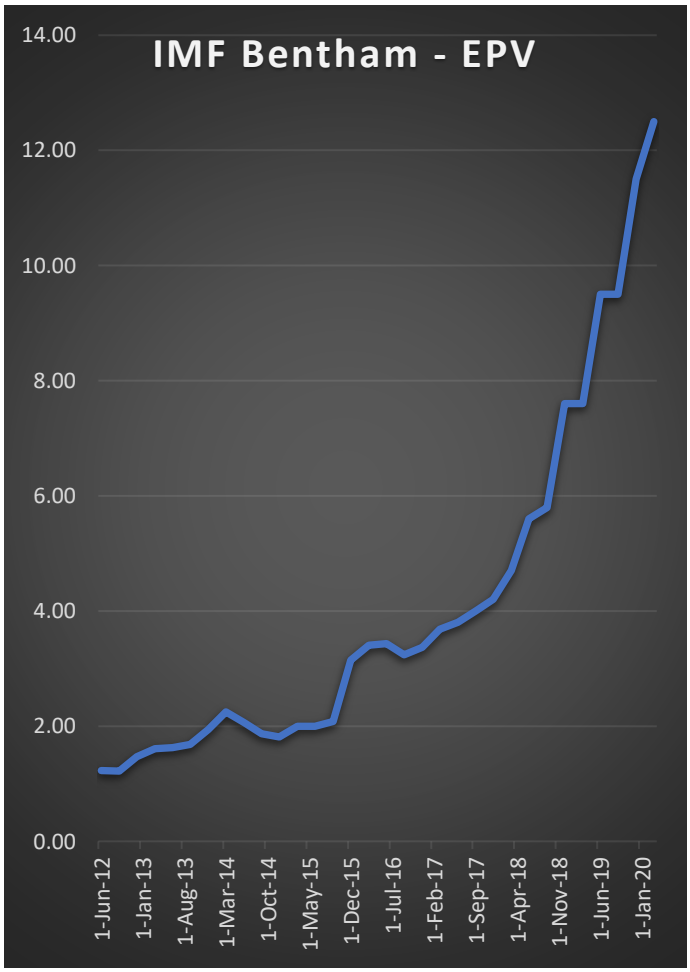
> *"Past performance indicates that OBL's litigation funding investments (excluding OBE investments) have generated average gross income of approximately 15% of the EPV of an investment at the time it is completed (****Long Term Conversion Rate****)."*[22]

The total amount of Omni Bridgeway (IMF Bentham)'s EPV[23], expected funded litigation recoveries, increased by 600% from the date Common Fund Orders were first proposed in the Federal Court's 'Money Max' case in September, and increased by 385% since the date that Common Fund Orders were approved by the Federal Court in October 2016 to March 2020.[24]

Omni Bridgeway discloses that its total EPV as of 31 March 2020 is $12.5 billion.[25] Assuming that its Long-Term Conversion Rate holds, it would potentially recognise average gross income of $1.87 billion on this portfolio.

[21] Omni Bridgeway (IMF Bentham) Investor Portfolio Report at 30 September 2019
[22] Omni Bridgeway (IMF Bentham) Investor Portfolio Report at 31 March 2020
[23] It is noted that the EPV figures disclosed in portfolio reports include global returns. However, regional based breakdowns of the data are not disclosed.
[24] Omni Bridgeway (IMF Bentham) Investor Portfolio Report at 30 September 2019
[25] Omni Bridgeway (IMF Bentham) Investor Portfolio Report at 31 March 2020

Figure 6: Omni Bridgeway (IMF Bentham) EPV 2012 to 2020



Claim sizes for Omni Bridgeway (IMF Bentham)

The funds raised by litigation funders produce enormous leverage in terms of the size of the claims they can bring with these funds. For example, Omni Bridgeway (IMF Bentham)'s Funds 2 & 3, which invest into Australia and the region, have just $180 million of committed capital. According to a portfolio report released by Omni Bridgeway (IMF Bentham) as of March 2020, Funds 2 & 3 are currently funding litigation where the total expected recovery measured by 'EPV' is $3.2 billion.[26] That means the fund can bring claims where expected recoveries are nearly eighteen (18) times larger than the fund value itself.

Certainty needed over the continued use of common fund orders

The High Court decisions involving BMW and Westpac (the *Brewster* case) held that courts may not have the power to make common fund orders at the outset of class action

[26] Omni Bridgeway (IMF Bentham) Investor Portfolio Report at 31 March 2020

proceedings. However, the Federal Court quickly issued a practice note stating that the Court would make alternative orders at the end of proceedings providing the same economic benefits to litigation funders, and imposing obligations to pay the funder's commission on class members regardless of whether or not they consent to, or are even aware of, class action proceedings being run in their name.

The position on common fund orders is currently a point of contention between judges in the Federal Court. Several judges have approved common fund orders following the *Brewster* decision. However, Justice Foster delivered a powerful condemnation of the concept in his decision in the Volkswagen Diesel Emissions Class action. He said:

> *"Unfunded group members have no contractual or other relationship with the litigation funder. Nor have they any liability to the funder. The funder has no right to the proceeds of a settlement or judgment under contractual or equitable principles… [It] is clear that the [High Court] rejected the idea that, upon some free-standing independent basis, equitable principles could support the [CFO] under consideration in Brewster," Justice Foster wrote.*
>
> *"In my judgment, the making of a CFO, whether at an early stage of a group proceeding or at the conclusion of such a proceeding, cannot be supported by the equitable principles … which addressed the sharing of reasonable legal costs expended in the creation of a court ordered trust fund and did not concern spreading the burden of a litigation funder's profits amongst all the beneficiaries of the trust fund thereby created, or by notions of unjust enrichment."*
>
> *"It is apparent [that Justices Murphy, Beach and Lee] are of the opinion that this court has power to make a CFO at the conclusion of a representative proceeding and should ordinarily do so, keeping a close eye, of course, upon the approved rate of commission and overall quantum of the particular funder's remuneration. Their Honours are of the opinion that the judgments of the majority in Brewster did not go so far as to decide that this court has no power to make a CFO at any time. With great respect to my colleagues, I do not think that the position is so clear."*[27]

Without this legislation the legal position on common fund orders will remain unclear. However, what is crystal clear is that common fund orders have played a large part in allowing offshore litigation funders and plaintiffs' lawyers to bring claims where very few claimants are actively engaged and bring class actions on behalf of large groups, for large amounts of money, potentially without the group members' knowledge or consent.

[27] Dalton & Anor v Volkswagen AG & Anor (No.2) [2020] FCA 661.

Somewhat surprisingly Omni Bridgeway (IMF Bentham) signalled its support for the abolition of common fund orders stating:

> *"The company advocates for a number of measures … including … introducing legislation to end the use of common fund orders and prevent the introduction of contingency fees for lawyers, as proposed by the Victorian government. This would ensure that only claims which are genuinely supported by enough engaged claimants, rather than funders or lawyers alone, are commenced."*[28]

Omni Bridgeway (IMF Bentham) is of course already well placed in terms of its infrastructure to bookbuild for major class actions.

Court Approvals are No Safeguard

Litigation funders and their supporters point to the fact that the commissions they receive are 'approved' by the court as part of the settlement process. This is intended to leave class members and the public with the impression that the approval process has involved a careful assessment of the commission and other fees and charges claimed by the funder by an independent entity seized with all of the relevant facts. On this basis they argue that regulation and independent oversight is unnecessary.

As demonstrated above, this belief is simply not true.

The judges do not have the experience and training in corporate finance to properly assess the risks and returns. Nor does the legislation require them to. They are not provided with the data required to undertake the exercise and receive no assistance from the parties. Even the appointment of an independent contradictor is currently a laboured exercise.

Consequently, courts are left as unwitting accomplices in what is unconscionable conduct on the part of the litigation funding industry. The litigation funding industry operates without any true 'market'. The returns are only possible because they are approved and enabled by a judge. Most concerningly, the levels of these returns defy all understood corporate finance principles of risk-adjusted return and escape all meaningful scrutiny.

28 Omni Bridgeway (IMF Bentham) ASX Announcement, 14 May 2020

Regulating the Industry

Regulation needed in this Booming Industry

There have been repeated calls for the regulation of the litigation funding industry.

They have come from groups as diverse as the Productivity Commission, law reform commissions, trade unions, consumers caught up in class actions and even litigation funders themselves.

The vices that attend the litigation funding industry, the lack of oversight and the failure of the few mechanisms for consumer protection that may apply to the industry are well documented. See for example the report of the Victorian Law Reform Commission published in 2018 and the Australian Law Reform Commission's Discussion Paper of the same year.

This exposure draft and any subsequent legislation is a positive step in the right direction to regulate the litigation funding industry.

By clearly defining what is 'fair and reasonable' judges are given the legislative guidance to determine what the term means and that ultimately this is overseen by an independent assessor or contradictor. By legislating these two measures, ultimately greater guidance and understanding is given to the courts in approving any settlement and this removes the complicated process by which if someone is not happy with the settlement approved, they have to sue their own lawyer.

Likewise, the removal of a common fund order is a significant advancement. It is logical, and more so only fair, that an individual has to provide consent to be a party to a class action and not the other way around where if they just so happen to be made aware that a funder has grouped them into a class, take active steps to opt out.

The reforms outlined in the *Treasury Laws Amendment (Measures for Consultation) Bill 2021: Litigation funders* address for the first time since class actions were established in 1992, a regulated model for how the courts deal with third party litigation funding and enforce a set of guidelines that class them properly as a Managed Investment Scheme (MIS), as they should already have been.

There is nothing fair about the system as it currently stands. Its impact is steeply regressive, rewarding some of the richest professionals in the country at the expense of those who can least afford it.

Litigation that delivers private profits for a few at the expense of the many is an injustice that cannot be allowed to stand.

We commend this bill and its passage through the Parliament.