



ASIC
Australian Securities &
Investments Commission

Explanatory Statement

ASIC Corporations (Conditional Costs Schemes) Instrument 2020/38

This is the Explanatory Statement for the *ASIC Corporations (Conditional Costs Schemes) Instrument 2020/38*

The Explanatory Statement is approved by the Australian Securities and Investments Commission (*ASIC*).

Summary

1. A litigation funding scheme or a proof of debt funding scheme that is funded under a conditional costs agreement (an arrangement between the member or members and a lawyer under which the payment of some or all fees is contingent on whether the outcome of the action is successful) may fall within the definition of a “managed investment scheme” within section 9 of the *Corporations Act 2001* (the *Act*) and therefore subject to the requirements in Chapters 5C (managed investment schemes) and 7 (financial services licensing and disclosure) of the Act.
2. The legislative instrument provides temporary relief to enable the operation of these kind of “conditional costs schemes” without having to comply with certain requirements of the Act until 31 January 2023. This is to provide certainty for lawyers and members of conditional costs schemes while the Government considers making regulations in this area.

Background

3. Section 9 of the Act provides that, subject to certain exemptions, a managed investment scheme includes a scheme that has the following features:
 - (a) people contribute money or money's worth as consideration to acquire rights to benefits produced by the scheme;
 - (b) any of the contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the people (members) who hold interests in the scheme; and
 - (c) the members do not have day to day control over the operation of the scheme.

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4. On 20 October 2009, the Full Court of the Federal Court held in *Brookfield Multiplex Ltd v International Litigation Funding Partners Pte Ltd [2009] FCAFC 147* that a funded representative action and solicitors' retainers for two representative proceedings against Brookfield Multiplex Ltd in the Federal Court were a managed investment scheme that should have been registered for the purposes of Chapter 5C of the Act.
 5. A litigation funding scheme or proof of debt scheme that satisfies the definition of a managed investment scheme must comply with the requirements of the Act including:
 - (a) section 601ED of the Act which requires that a managed investment scheme must be registered with ASIC including where it has more than 20 members or is promoted by a professional promoter in certain circumstances;
 - (b) section 601MB of the Act which provides that contracts are voidable at the option of a member of a scheme where an invitation or offer is made and the offeror has failed to comply with section 601ED or Division 2 of Part 7.9 (Product Disclosure Statements);
 - (c) section 911A of the Act which requires that a person carrying on a business of providing financial services must hold an Australian financial services licence (an *AFS licence*) that authorises them to provide that financial service;
 - (d) section 911B of the Act which requires that a person must only provide a financial service on behalf of another person who carries on a financial services business where certain conditions are satisfied;
 - (e) section 992A of the Act which prohibits a person from offering financial products in the course of, or because of, an unsolicited meeting or telephone call. Section 992AA prohibits such conduct in relation to interests in managed investment scheme; and
 - (f) Part 7.9 of the Act which imposes various disclosure obligations on the issuer of a financial product, including the obligation to give a Product Disclosure Statement and provide ongoing disclosure in certain circumstances.
 6. With effect from 12 July 2013, regulation 5C.11.01 of the *Corporations Regulations 2001* declares that a litigation funding scheme is not a managed investment scheme. Regulation 5C.11.01(b) defines a "litigation funding scheme" as a scheme, which amongst other things, has the following features:
 - (a) a person (the *funder*) provides funds, indemnities or both under a funding agreement (including an agreement under which no fee is payable to the funder or lawyer if the scheme is not successful in seeking remedies) to enable the general members of the scheme to seek remedies; and

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- (b) the funder is not a lawyer or legal practice that provides a service for which some or all of the fees, disbursements or both are payable only on success.
 7. As a result, a conditional costs scheme may not be excluded from being a managed investment scheme.
 8. On 11 July 2013, ASIC made ASIC Class Order [CO 13/898] to temporarily exclude conditional costs schemes from the definition of “managed investment scheme” in section 9 of the Act and Parts 7.6, 7.7, 7.8 and 7.9 of the Act.
 9. The objective of [CO 13/898] was to allow the Government time to consider its position on whether to exempt conditional cost schemes under similar terms.
 10. The Class Order had effect until 12 July 2019.

Purpose of the instrument

11. Further time is required for the Government to consider any legislative changes in relation to conditional cost schemes. The legislative instrument provides temporary relief until 31 January 2023 on the same terms as [CO 13/898] with changes to reflect current drafting practice and updated legislative references in the definition of a “conditional cost agreement”.
12. This is to provide certainty for industry that conditional costs schemes are not required to comply with the Act until 31 January 2023.

Consultation

13. ASIC consulted with the Department of the Treasury in relation to making the legislative instrument. ASIC did not undertake wider consultation with respect to the legislative instrument because it is minor and machinery in nature.
14. The full application of Chapters 5C and 7 of the Act to conditional costs schemes could be considered to be an unintended application of consumer protection legislation, subject to the Government reaching a considered and final policy position on how such arrangements ought to be regulated.

Operation of the instrument

15. Section 9 of the Act contains a dictionary of defined terms used in the Act. Paragraph 5(a) of the instrument provides for Chapter 5C of the Act to apply as if a definition of “conditional costs agreement” was inserted into section 9.
16. Paragraph 5(b) of the instrument provides for Chapter 5C of the Act to apply as if the definition of a “managed investment scheme” in section 9 of the Act were varied to exclude conditional cost schemes.
17. Section 6 of the instrument exempts persons from the requirements to hold an AFS licence or act as an authorised representative of a licensee to provide financial services associated with a “conditional cost litigation scheme” and a “conditional cost proof of debt scheme”. This includes a “funding product”

which is defined as an arrangement or an interest in an arrangement that are financial products but not interests in managed investment schemes that are similar to a conditional cost litigation scheme or a conditional cost proof of debt scheme.

18. Section 7 of the instrument exempts persons from the requirement to comply with the hawking prohibitions in subsections 992A and 992AA of the Act in relation to an interest in a conditional cost litigation scheme, a conditional cost proof of debt scheme or a funding product.
19. Section 8 of the instrument exempts persons from the requirement to comply with the disclosure provisions in Part 7.9 of the Act in relation to an interest in a conditional cost litigation scheme, a conditional cost proof of debt scheme or a funding product.
20. Section 9 of the instrument provides that for the avoidance of doubt, the declaration in section 5 of the instrument does not have effect for the purposes of section 601MB of the Act in relation to a contract entered into before the commencement of the Legislative instrument by a person to subscribe for an interest in a conditional cost litigation scheme or a conditional cost proof of debt scheme.
21. The instrument commences on the day after it is registered on the Federal Register of Legislation and continues until 31 January 2023.

Legislative authority

22. Subsections 601QA(1), 926A(2), 992B(1) and 1020F(1) of the Act provides the legislative authority for this instrument.
23. The instrument is a disallowable legislative instrument

Statement of Compatibility with Human Rights

24. The Explanatory Statement for a disallowable legislative instrument must contain a Statement of Compatibility with Human Rights under subsection 9(1) of the *Human Rights (Parliamentary Scrutiny) Act 2011*. A Statement of Compatibility with Human Rights is in the Attachment.

Statement of Compatibility with Human Rights

This Statement of Compatibility with Human Rights is prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

ASIC Corporations (Conditional Costs Schemes) Instrument 2020/38

Overview

1. The legislative instrument provides temporary relief to enable the operation of conditional costs schemes without having to comply with the financial services provisions of the *Corporations Act 2001* until 31 January 2023.
2. A conditional costs scheme is a litigation funding scheme or a proof of debt funding scheme that is funded under an arrangement between the member or members and a lawyer under which the payment of some or all fees is contingent on whether the outcome of the action is successful.
3. The instrument is made so as to provide certainty for lawyers and members of conditional costs schemes while the Government considers making regulations in this area.

Assessment of human rights implications

4. This instrument does not engage any of the applicable rights or freedoms.

Conclusion

5. This instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.