EXPLANATORY STATEMENT

Issued by authority of the Assistant Treasurer and Minister for Financial Services

Corporations Act 2001

Corporations Amendment (Litigation Funding) Regulations 2022

The *Corporations Act 2001* (the Act) provides for the regulation of corporations and financial services.

Section 1364 of the Act provides that the Governor-General may make regulations prescribing matters required or permitted by the Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the Act.

The purpose of the *Corporations Amendment (Litigation Funding) Regulations 2022* (the Regulations) is to provide litigation funding schemes with an explicit exemption from the Act's managed investment scheme (MIS) regime, Australian Financial Services Licence (AFSL) requirements, product disclosure regime and anti-hawking provisions (i.e. unsolicited sales of financial products).

Litigation funding schemes and arrangements involve an entity that is not a party to the litigation (a third-party litigation funder) paying the costs of litigation or indemnifying parties from adverse costs orders in return for a percentage share of the proceeds if the litigation is successful.

The Act's MIS and ASFL regimes were not designed or intended to regulate the litigation funding industry. The amendments also clarify the status of the law in the *Corporations Regulations 2001* (the Corporations Regulations) following the Full Federal Court's decision in *LCM Funding Pty Ltd v Stanwell Corporation Limited* [2022] FCAFC 103 (the LCM case). In the LCM case, the Full Federal Court found the Court's earlier decision in *Brookfield Multiplex Ltd v International Litigation Funding Partners Pte Ltd* (2009) 180 FCR 11, that litigation funding schemes are subject to the MIS regime, was fundamentally wrong.

The Regulations bring arrangements for litigation funding schemes in line with arrangements for other types of litigation funding schemes (i.e. insolvency litigation funding schemes) or litigation funding arrangements defined in the Corporations Regulations, which are already exempt from the Act's MIS regime, AFSL requirements, Part 7.9 product disclosure requirements and anti-hawking provisions. This also brings the arrangements in line with the law before 22 August 2020 (in effect reversing the effect of amendments made by the *Corporations Amendment (Litigation Funding) Regulations 2020).*

The Act does not specify any conditions that need to be met before the power to make the Regulations is exercised.

An exposure draft of the Regulations was released for public consultation between 2 September 2022 to 30 September 2022 and eighteen submissions were received. Consultation did not result in any changes to the Regulations.

Details of the Regulations are set out in Attachment A.

The Regulations are a legislative instrument for the purposes of the *Legislation Act 2003*.

The Regulations commence on the day after the instrument is registered on the Federal Register of Legislation.

The Office of Best Practice Regulation has assessed the Regulations as having no more than a minor regulatory impact (OBPR Reference Number OBPR22-02113). Accordingly, a Regulation Impact Statement has not been prepared.

A statement of Compatibility with Human Rights is at Attachment B.

ATTACHMENT A

Details of the *Corporations Amendment (Litigation Funding) Regulations 2022*

Section 1 – Name of the Regulations

This section provides that the name of the Regulations is the *Corporations Amendment (Litigation Funding) Regulations 2002* (the Regulations).

Section 2 – Commencement

Schedule 1 to the Regulations commences on the day after the instrument is registered on the Federal Register of Legislation.

Section 3 – Authority

The Regulations are made under the *Corporations Act 2001* (the Act).

Section 4 – Schedule

This section provides that each instrument that is specified in the Schedule to this instrument will be amended or repealed as set out in the applicable items in the Schedule, and any other item in the Schedule to this instrument has effect according to its terms.

Schedule 1 – Amendments *Corporations Amendment (Litigation Funding) Regulations 2022*

Item 1 (Subregulation 5C.11.01(2A)) – Adding an exemption from the Managed Investment Scheme (MIS) regime for litigation funding schemes

Item 1 provides an explicit exemption for litigation funding schemes from meeting the definition of a managed investment scheme (MIS) in section 9 of the Act.

The exemption ensures the *Corporations Regulations 2001* (the Corporations Regulations) reflect the status of the law following the Full Court of the Federal Court's decision in *LCM Funding Pty Ltd v Stanwell Corporation Limited* [2022] FCAFC 103 (the LCM case). In the LCM case, the Full Federal Court found the earlier decision in *Brookfield Multiplex Ltd v International Litigation Funding Partners Pte Ltd* (2009) 180 FCR 11 (the Brookfield case) that litigation funding schemes are subject to the MIS regime, was fundamentally wrong.

The explicit exemption provides greater certainty for industry, as well as implementing the Government's policy that litigation funding schemes should not be subject to the MIS regime.

Providing an explicit exemption is also consistent with the existing approach for other litigation funding schemes (labelled 'insolvency litigation funding schemes' prior to the Regulations) and litigation funding arrangements (defined in regulation 5C.11.01 of the Corporations Regulations). This approach is also consistent for class actions

and proof of debt arrangements that are funded by conditional costs agreements (such as an agreement under which a lawyer agrees to act on a no win, no fee basis).

Class actions and proof of debt arrangements that are funded by conditional costs agreements are afforded explicit exemptions from the MIS regime under the *ASIC Corporations (Conditional Costs Schemes) Instrument 2020/38*). That legislative instrument also provides exemptions from other legislative requirements in the Act, such as the need to hold an Australian Financial Services Licence (AFSL), the anti-hawking provisions and product disclosure requirements.

Item 2 (Subregulation 5C.11.01(3)) – Removing the separate label for 'insolvency litigation funding schemes'

Item 2 removes the separate label for insolvency litigation funding schemes, as such schemes are to be treated the same as other litigation funding schemes.

Prior to the Regulations, litigation funding schemes were not exempt from MIS regime requirements, whereas insolvency litigation funding schemes were exempt. As both litigation funding schemes and insolvency litigation funding schemes are now subject to the same rules and obligations under the Act, it is unnecessary for them to have separate labels (i.e. to be labelled as either a litigation funding scheme or an insolvency litigation funding scheme). This item simplifies the law by removing an unnecessary term.

Items 8 and 9 (Paragraph 7.1.04N(2)(a) and subregulations 7.1.04N(3) and (4)) – Ensuring interests in litigation funding schemes continue to be 'financial products'

Item 9 would remove subregulations 7.1.04N(3) and (4) (which provide that an interest in a litigation funding scheme is a financial product). Subregulations 7.1.04N(3) and (4) would no longer be necessary as item 8 maintains the status of interests in litigation funding schemes as financial products by ensuring that this is achieved instead by subregulation 7.1.04N(2). It is necessary for such interests to be declared financial products so they can be provided with explicit exemptions from the Act's AFSL requirements, product disclosure requirements and anti-hawking provisions. This item is required because item 2 removes the distinction between litigation funding schemes and insolvency litigation funding schemes.

Item 13 (Paragraph 7.6.01(1)(x)) – Adding exemption from AFSL requirements for services in relation to litigation funding schemes

Item 13 provides an explicit exemption for litigation funding schemes from the Act's requirement to hold an AFSL. This brings the treatment for all litigation funding schemes in line with requirements for litigation funding arrangements with respect to AFSL requirements.

Items 14, 15, 16, 18 and 19 (Subregulation 7.6.01AB(1) (paragraph 911A(5C)(a) of the *Corporations Act 2001*); Paragraph 7.6.01AB(2)(a); Subregulation 7.6.01AB(2) (note); Paragraph 7.6.04(1)(l);

Subregulation 7.6.04(2A)) – Changing the way bespoke conflict of interest requirements apply in relation to AFSLs

The combined effect of items 14, 15, 16, 18 and 19 is to remove the bespoke conflict of interest requirements that attached to AFSLs for litigation funding schemes.

As litigation funding schemes are now expressly exempt from the requirement to hold an AFSL, attaching the bespoke conflict of interest requirements to AFSLs is no longer an appropriate means of imposing these requirements.

However, similar bespoke conflict of interest requirements will continue to apply to litigation funding schemes through subregulation 7.6.01AB(2).

Subregulation 7.6.01AB(2) requires persons providing financial services to comply with similar conflict of interest requirements as a condition of their exemption from holding an AFSL under paragraph 7.6.01(1)(x).

Items 20 and 21 (Paragraph 7.8.21A(g) and subparagraphs 7.8.21A(g)(i) and (ii)) – Adding an exemption from the anti-hawking provisions for litigation funding schemes

Item 20 exempts litigation funding schemes from the Act's anti-hawking provisions. This means all litigation funding schemes and litigation funding arrangements are treated the same for the purposes of the Act's anti-hawking provisions. The amendment is required because item 2 removes the separate label for insolvency litigation funding schemes, meaning litigation funding schemes and insolvency litigation funding schemes are no longer subject to different requirements.

Item 21 is a consequential amendment to repeal provisions which are now unnecessary due to the changes made by item 20.

Item 22 (Subparagraphs 7.9.98A(a)(i), (b)(i), (c)(i) and (d)(i)) – Adding an exemption from Part 7.9 of the Act for litigation funding schemes

Item 22 exempts litigation funding schemes from the Act's Part 7.9 disclosure obligations. This means all litigation funding schemes and litigation funding arrangements are treated the same for the purposes of the Act's Part 7.9 disclosure obligations. The amendment is required because item 2 removes the separate label for insolvency litigation funding schemes, meaning litigation funding schemes and insolvency litigation funding schemes are no longer subject to different requirements.

Item 23 (Part 10.48—Application provisions relating to the *Corporations Amendment (Litigation Funding) Regulations 2022*) – Application of the amendments to litigation funding schemes

Item 23 provides for the application of the Regulations to litigation funding schemes.

- Litigation funding schemes entered into on, or after, the commencement of the Regulations, are explicitly exempt from meeting the definition of a MIS, AFSL requirements, the Act's Part 7.9 product disclosure requirements and anti-hawking provisions.

- Litigation funding schemes entered into prior to the commencement of the Regulations are explicitly exempt from meeting the definition of a MIS, AFSL requirements, the Act's Part 7.9 product disclosure requirements and anti-hawking provisions for the duration of the scheme that occurs on or after the Regulations commence.

The Australian Securities and Investments Commission (ASIC) may need to consider whether it is appropriate to extend or amend any existing exemptions or modifications to support the Regulations.

For example, ASIC may need to consider whether modifications granted under instruments, such as the *ASIC Corporations (Litigation Funding Schemes) Instrument 2020/787*, are appropriate to retain or whether they could now be revoked.

Instrument 2020/787 provides exemptions to litigation funding schemes from certain requirements in the Act. That instrument was originally made to facilitate litigation funders complying with the MIS regime.

Items 3, 4, 5, 6, 7, 8, 10, 11 and 17 (Paragraphs 5C.11.01(4)(e) and (5)(e), Subregulation 5C.11.01(6) (definition of *general member*), heading of regulation 7.1.04N, heading of subregulation 7.1.04N(2) and paragraph 7.1.04N(2)(a), paragraph 7.1.06(2A)(a), paragraph 7.1.06(2A)(b) and sub-subparagraph 7.6.04(1)(k)(ii)(B)) – Consequential amendments due to the removal of the 'insolvency litigation funding scheme' label

Items 3, 4, 5, 6, 7, 8 and 10 are consequential amendments required because item 2 removes the distinction between litigation funding schemes and insolvency litigation funding schemes.

Items 11 and 17 are consequential amendments to punctuation required because item 2 removes of the insolvency litigation funding scheme label.

Item 12 (Paragraph 7.1.06(2A(c)) – Consequential amendment due to the repeal of subregulation 7.1.04N(3)

Item 12 is a consequential amendment required because subregulation 7.1.04N(3) is repealed. The repeal of subregulation 7.1.04N(3) is itself required because item 2 removes the 'insolvency litigation funding scheme' label.

ATTACHMENT B

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Corporations Amendment (Litigation Funding) Regulations 2022

This Legislative 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*.

Overview of the Legislative Instrument

The purpose of the *Corporations Amendment (Litigation Funding) Regulations 2022* (the Regulations) is to provide litigation funding schemes with an explicit exemption from the *Corporations Act 2001* (the Act) managed investment scheme (MIS) regime, Australian Financial Services Licence (AFSL) requirements, product disclosure regime and anti-hawking provisions (i.e. unsolicited sales of financial products).

Litigation funding schemes and arrangements involve an entity that is not a party to the litigation (a third-party litigation funder) paying the costs of litigation or indemnifying parties from adverse costs orders in return for a percentage share of the proceeds if the litigation is successful.

The Act's MIS and ASFL regimes were not designed or intended to regulate the litigation funding industry. The amendments clarify the status of the law in the *Corporations Regulations 2001* (the Corporations Regulations) following the Full Federal Court's decision in *LCM Funding Pty Ltd v Stanwell Corporation Limited* [2022] FCAFC 103 (the LCM case). In the LCM case, the Full Federal Court found the Court's earlier decision in *Brookfield Multiplex Ltd v International Litigation Funding Partners Pte Ltd* (2009) 180 FCR 11 (the Brookfield case), that litigation funding schemes are subject to the MIS regime, was fundamentally wrong.

The Regulations bring arrangements for litigation funding schemes in line with arrangements for other types of litigation funding schemes (i.e. insolvency litigation funding schemes) or litigation funding arrangements defined in the Corporations Regulations, which are already exempt from the Act's MIS regime, AFSL requirements, Part 7.9 product disclosure requirements and anti-hawking provisions. This also brings the arrangements in line with the law before 22 August 2020 (in effect reversing the effect of amendments made by the *Corporations Amendment (Litigation Funding) Regulations 2020).*

Human rights implications

The Regulations engage the right to a fair trial and hearing contained in Article 14 of the International Covenant on Civil and Political Rights (ICCPR).

The right to a fair trial and hearing

Article 14 of the ICCPR recognises the right to a fair trial and hearing. This is a fundamental part of the rule of law and the proper administration of justice. Article 14 further provides that all persons are equal before the courts and tribunals and have access to justice. This right applies to both criminal and civil proceedings.

Under this right, all people are to have equal access to courts. No one should be barred from accessing courts or tribunals (except in limited exceptions). The United National Human Rights Committee (UNHRC) has stated the right to a fair trial and fair hearing rights may only be limited in strict circumstances.

The Regulations promote access to justice by reducing compliance costs for litigation funders, potentially allowing claims to be brought that might not otherwise have been. Prior to the Regulations and the decision of the Full Federal Court in the LCM case, third party litigation funders were required to comply with the MIS regime in Chapter 5C of the Corporations Act and hold an AFSL to deal in, or provide, financial product advice in relation to an interest in a litigation funding scheme.

Under Article 14(1), the UNHRC has noted the imposition of fees on parties to proceedings that would de facto prevent their access to justice might give rise to issues.[1] Reinstating the exemptions from AFSL and other Corporations Act requirements, and the subsequent reduction in compliance costs for litigation funders, improves their ability to affordably provide services that facilitate access to justice for claimants.

Conclusion

The Regulations are consistent with Article 14 of the UNHRC as the Regulations reduce compliance costs for litigation funders, improving their ability to facilitate access to justice for claimants.

[1] Human Rights Committee, General Comment No. 32, Article 14: Right to equality before courts and tribunals and to a fair trial, U.N. Doc. CCPR/C/GC/32 (2007).