

30 July 2018

Australian Law Reform Commission  
GPO Box 3708  
Sydney NSW 2001

via email: [class-actions@alrc.gov.au](mailto:class-actions@alrc.gov.au)

Dear Sir or Madam

## Inquiry into Class Action Proceedings and Third-Party Litigation Funders

Chartered Accountants Australia and New Zealand welcomes the opportunity to provide a submission to the Australian Law Reform Commission on the Inquiry into Class Action Proceedings and Third-Party Litigation Funders. Appendix A includes our responses to some of the discussion paper proposals and questions and Appendix B provides more information about Chartered Accountants Australia and New Zealand.

### Key points

- We support the proposed review of the legal and economic impact of the continuous disclosure obligations of entities and recommend that further consideration is given to the economic cost of class actions.
- We support the proposed regulation of litigation funders and the proposed requirement for third-party funders to obtain and maintain a 'litigation funding licence.'
- The discussion paper largely focuses on 'class action' cases, however we note that litigation funding is also a useful model for the insolvency industry. We recommend that the Inquiry recommendations distinguish between the two to avoid any unintended consequences.
- We encourage the Commission to propose that base level financial requirements are held within Australia to protect defendants in the event that adverse costs arise against the applicant.

Should you have any queries concerning the matters raised in the following questionnaire or wish to discuss them in further detail, please contact Karen McWilliams via email at [karen.mcwilliams@charteredaccountantsanz.com](mailto:karen.mcwilliams@charteredaccountantsanz.com) or phone (612) 8078 5451.

Yours sincerely

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# Appendix A – Detailed Comments on Discussion Paper

## General comments

We are pleased to note that submissions made during the Victorian Law Reform Commission (VLRC) “Access to Justice – Litigation Funding and Group Proceedings” consultation have been considered within this discussion paper. In particular, our submission called for regulation to protect the validity of the legal process and the legitimate interests of plaintiffs and defendants, which has been addressed as a part of Proposals 3-1 and 3-2.

The discussion paper largely focuses on ‘class action’ cases, however we note that litigation funding is also a useful model for the insolvency industry. It allows liquidators/trustees in bankruptcy to commence legal action in certain matters, where ordinarily they may not have commenced such action due to no funds being available. Some of our members are also concerned that the proposed changes could inadvertently affect funding advanced by creditors of insolvent administrations for litigation purposes, including funding by the ATO or under the Fair Entitlements Guarantee Recovery (FEG) Program. We recommend that the Inquiry recommendations distinguish between third party funding for class actions and the funding of professionals, such as insolvency practitioners.

## 1: Introduction to the Inquiry

### Proposal 1-1:

We support the review of the legal and economic impact of continuous disclosure obligations of entities. We recommend that such a review should include all applicable continuous disclosure requirements including the ASX Listing Rules (chapter 3) and the ASX Corporate Governance Council’s principles and recommendations.

We recommend that further consideration is given to understanding the economic cost of class actions related to continuous disclosure obligations. This would allow for a proper evaluation to be carried out on the impacts to entities and the overall industry. The economic cost extends beyond the direct cost to the corporate entity. As the paper notes, the increase in the cost of D&O insurance (increased more than 200% in the last 12 to 18 months as mentioned in the discussion paper) has had a significant impact on operating costs in business and placing additional pressures on professional services fees.

Further, some of our members have expressed concern about the additional cost burden that could possibly flow onto other professions such as auditors in public practice. Shareholder class actions may also target the auditor if there has been a breach of continuous disclosure requirements. Auditors may be targeted at the same time as the class action or after the action if unsuccessful in pursuing the corporate entity resulting in additional costs to the auditor. Additionally, audit firms can also incur significant costs in relation to the compulsory orders for the production of documents, even in circumstances when they are not named as defendants in the case.

It is important to note the value that audits bring to the economy, building trust in investment markets and companies. Audits help enhance confidence by providing an independent assessment about the accuracy and reliability of financial statements. These additional cost burdens on the assurance profession may ultimately feed into the cost of performing an audit.

## 3: Regulating Litigation Funders

### Proposal 3-1:

We support proposal 3-1 that will require third-party litigation funders to obtain and maintain a 'litigation funding licence' to operate in Australia.

Consideration needs to be given to who will be responsible for the licencing regime. As noted in the discussion paper ASIC has been identified as the appropriate body to administer and regulate a fit for purpose compliance regime. However continued advocating for the group needs to also be considered and the Association of Litigation Funders of England and Wales model mentioned within the discussion paper could be a viable option that will complement ASICs role

As noted in our VLRC submission, we also consider it important to take into account that additional regulation on litigation funders is likely to increase the cost to consumers of pursuing court proceedings.

### Proposal 3-2:

We agree with the ALRC's conclusion not to require litigation funders to hold an AFS License and instead set up a new licensing regime for litigation funders. We support the proposed licensing obligations. We consider the five options within section 3.38, table 1 to be appropriate requirements for skills and qualifications to provide the services and products under the licence.

We support the proposed requirement for litigation funders to be audited annually. We note that paragraph 3.10 of the discussion paper states:

*"A key part of the proposed licence regime for litigation funders is an annual audit. That audit will not only provide an independent assessment of the funder's finances but would include compliance audit to assess whether the funder has met, and continues to meet, the conditions of its licence. This will provide oversight of the litigation funder's compliance and provide a key plank of the licensing scheme's integrity."*

We encourage the commission to consider auditor independence when outlining annual audit requirements. We note that challenges to independence could arise if an auditor is named as a defendant in a funded class action as well as carrying out the litigation funding licence audit requirements.

### **Question 3-1: What should be the minimum requirements for obtaining a litigation funding licence, in terms of the character and qualifications of responsible officers?**

We consider that the requirements for lawyers and AFS Licensees are adequate models to determine a licensees character and skill requirements. We recommend a combination of both models to provide a minimum threshold for entry into the industry.

### **Question 3-2: What ongoing financial standards should apply to third-party litigation funders? For example, standards could be set in relation to capital adequacy and adequate buffers for cash flow**

We encourage the commission to propose that base level financial requirements are held within Australia. We understand that many funders are based offshore and "they hold little to no capital here in Australia" as noted in section 3.61. Although proposed regulation and ongoing financial standards may result in overseas funders exiting the Australian market, defendants would be protected in the event that adverse costs arise against the applicant.

We recommend that the current ASIC regulation of AFS Licensees, which includes base level financial requirements as well as additional tailored financial requirements which are dependent on specific industries, is used as a guide for the financial standards.

If deemed appropriate, the commission could also consider exemptions to Australian based financial requirements (but would be held overseas) if a litigation funder has an appropriate level of Australian insurance to cover any adverse costs for After the Event ('ATE' insurance).

### **Question 3-3: Should third-party litigation funders be required to join the Australian Financial Complaints Authority Scheme?**

We support third-party funders joining the Australian Financial Complaints Authority Scheme as the scheme would act as a safeguard to protect plaintiffs and class action members. It would ensure that an independent assessor was available if internal dispute resolution was not possible.

## 5: Commission Rates and Legal Fees

We note that some of our members have expressed concerns at the potential conflict of interest which may arise by allowing lawyers to charge on a contingency basis (i.e. on a % of recoveries) rather than the current model of an hourly rate plus an uplift (25% maximum).

## 6: Competing Class Actions

### **Proposal 6-1:**

We support the proposal that where there are two or more competing class actions that the court will determine which one of the proceedings will progress. This will improve efficiency, reduce court assignments and reduce costs associated with class actions.

We recommend that when reviewing overlapping or duplicate cases that a 'race to judgement' and 'first-to-file' situations are avoided. These situations have been seen in the US where lawyers are competing to secure work and claimants and the outcome of settlements have been impacted negatively.

## About Chartered Accountants Australia and New Zealand

Chartered Accountants Australia and New Zealand is a professional body comprised of over 120,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgment, financial discipline and a forward-looking approach to business which contributes to the prosperity of our nations.

We focus on the education and lifelong learning of our members, and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international markets.

We are a member of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

We also have a strategic alliance with the Association of Chartered Certified Accountants. The alliance represents 788,000 current and next generation professional accountants across 181 countries and is one of the largest accounting alliances in the world providing the full range of accounting qualifications to students and business.