

From: Campbell Gibson
Sent: Monday, 13 September 2021 5:49 PM
To: [REDACTED]
Cc: Andrew Park <Andrew.Park@fma.govt.nz>
Subject: RE: FMA Acknowledgement CRM:041184862

Hi [REDACTED]

Thanks for the additional context on your story. I've confirmed that we're able to release our submission under the OIA, please find it attached.

Regards,
Campbell

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Greetings.

Just writing about the [Law Commission review into class actions and litigation funding](#). Did the FMA put in a submission? If so, could I see it, please?

It's an interesting area – quite critical in terms of access to justice – and I'd be interested in the FMA's views.

[REDACTED]

From: FMA Customer Service <questions@fma.govt.nz>

Date: Monday, 13 September 2021 at 3:21 PM

To: [REDACTED]

Subject: FMA Acknowledgement CRM:041184862

Dear [REDACTED]

Thank you for contacting the Financial Markets Authority (FMA).

Your enquiry has been referred to the appropriate department.

We aim to provide you with a response as soon as possible, however this may take up to 20 working days once all the relevant information has been received.

Yours sincerely

Financial Markets Authority

Customer Service

T 0800 434 566

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11 March 2021

Catherine Helm
Kaitohutohu Matua | Senior Legal and Policy Adviser
Te Aka Matua o t Ture | Law Commission
cal@lawcom.govt.nz

Delivered by email
Dear Catherine

Class Actions and Litigation Funding

I am writing to you about the Law Commission's review of class actions and litigation funding. The Financial Markets Authority (FMA) is an independent Crown entity. The FMA's purpose under the Financial Markets Authority Act 2011 (FMA Act) is to "promote and facilitate the development of fair, efficient and transparent financial markets". Our role is to strengthen public confidence in New Zealand's financial markets, promote innovation, and support the growth of New Zealand's capital base by providing effective regulation.

We have the following comments on the recommendations set out in the issues paper.

Class Actions

We support the Law Commission's view that a statutory class actions regime is desirable in Aotearoa.

Litigation Funding

In chapter 23 of the issues paper, the Law Commission identifies four key concerns associated with litigation funding: funder control of litigation, excessive funder profits, conflicts of interest, and capital adequacy of funders. The Law Commission sets out five options for the form that regulation and oversight of litigation funders could take, two of which identify the FMA as a potential regulator:

- (b) Managed investment scheme requirements overseen by the Financial Markets Authority (FMA).
- (c) Tailored licensing requirements overseen by the FMA or another regulator.

We do not consider that licensing by the FMA is an effective mechanism to address the regulatory risks sought to be addressed by regulating litigation funders. The role of the FMA under the FMA Act is to promote and facilitate the development of fair, efficient and transparent financial markets. The FMA is funded predominantly by levies imposed on financial markets participants. As per the Council of Financial Regulators [Regulatory Charter](#), the financial markets regulatory regime in Aotearoa is based on a twin peaks model of financial regulation - the FMA is responsible for market conduct regulation and the Reserve Bank is the prudential regulator.

It is outside the FMA's remit to address concerns that a litigation funder takes excessive profits, or undermines the integrity of the court system by controlling the litigation for their own ends. Nor

would regulation by the FMA be appropriate to address the conflicts of interest that arise between plaintiffs, lawyers and litigation funders. These issues do not relate to the financial markets.

In relation to the concern that litigation funders are adequately capitalised, licensing by the FMA would not automatically mean that litigation funders have adequate financial resources to meet adverse costs orders, continue to fund proceedings, or distribute funds to shareholders.

We consider that litigation funding should be regulated as a legal service, as it is more closely aligned with the provision of legal services and the administration of justice, as opposed to financial markets services. Litigation funders typically employ people with legal qualifications and experience as they require legal expertise to consider which lawyers to engage, which clients to support, and what litigation tactics to take.

The issues paper does not identify who other potential regulators might be. We consider that the Ministry of Justice or Department of Internal Affairs are more suitable agencies to regulate litigation funders given the other services they already have oversight of.

Managed investment schemes

The statutory definition of a managed investment scheme (MIS) under section 9 of the Financial Markets Conduct Act 2013 (FMC Act) provides:

managed investment scheme means a scheme to which each of the following applies:

- (a) *the purpose or effect of the scheme is to enable persons taking part in the scheme to contribute money, or to have money contributed on their behalf, to the scheme as consideration to acquire interests in the scheme; and*
- (b) *those interests are rights to participate in, or receive, financial benefits produced principally by the efforts of another person under the scheme (whether those rights are actual, prospective, or contingent, and whether they are enforceable or not); and*
- (c) *the holders of those interests do not have day-to-day control over the operation of the scheme (whether or not they have the right to be consulted or to give directions).*

It is not clear whether litigation funding arrangements come within this MIS definition. In order to be a MIS, plaintiffs must have rights to participate in, or receive, financial benefits. Financial benefits are defined in section 6 of the FMC Act to mean “capital, earnings, or other financial returns”. When considering the litigation funding arrangement between a litigation funder and a plaintiff, we do not consider the features that relate to reducing financial risk, or compensation for loss received from the court, fit the definition of financial benefits.

There is the possibility that a litigation funder raises funds from investors to operate. The arrangement between the litigation funder and investors is more likely to fit the definition of a managed investment scheme and, if so, the FMC Act regulatory MIS regime would apply. If a litigation funder was funded by contributions from retail investors this may well raise issues that intersect with the FMA’s regulatory mandate, and there are good arguments for regulation of these. However, this is not the purpose for which the Law Commission seeks to regulate, and we maintain that the FMA is not the appropriate regulator.

We note that in the Australian case of [Brookfield](#), the court found that the litigation funding scheme in question constituted a MIS. The definition of “benefits” was read widely to mean “anything that is good for a person” so that “financial benefits” produced by the scheme included protection from any adverse cost order and avoidance of a need to give security. As detailed above, the FMC Act definition of “financial benefits” is much narrower so it is unlikely that the same reasoning can be applied in Aotearoa.

Designation as a MIS

In footnote 21 of chapter 23, the issues paper refers to the fact that the FMA is able to designate arrangements as a MIS. This is a discretionary power of the FMA and in order for the FMA to make such a declaration, it must be satisfied that the statutory requirements in sections [562](#), [563](#) and [564](#) of the FMC Act are met. The test focuses on the economic substance of a ‘security’. ‘Security’ is defined in section 6 as “an arrangement or a facility that has, or is intended to have, the effect of a person making an investment or managing a financial risk”. We question whether litigation funding arrangements satisfy the definition of ‘security’ and we are also not satisfied that the arrangement is of a similar economic substance to a MIS.

Under section 563, the FMA cannot not make a declaration unless it is satisfied that the declaration is necessary or desirable in order to promote at least one of the purposes in sections [3](#) and [4](#) of the FMC Act. These purposes focus on the financial markets. We do not consider that the activities of litigation funders ordinarily fit within the financial markets conduct regulatory regime and therefore consider it unlikely that designating litigation funding arrangements as a MIS would be necessary or desirable to promote the FMC Act purposes.

Licensing requirements of a MIS

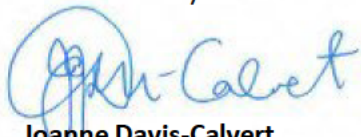
The issues paper does not discuss the suitability or proportionality of the FMC Act regime’s MIS requirements applying to litigation funders, or the potentially significant compliance costs, including FMA licensing fees and annual FMA levies. The MIS requirements - particularly the FMC disclosure and governance settings - would need significant tailoring through regulations and/or FMA exemptions (as has been needed in Australia) in order for them to be appropriate for litigation funders.

Financial service providers

At paragraph 23.37, the issues paper states that a benefit of designating litigation funders as a MIS is that “having all financial service providers covered by the same regime would encourage coherence”. It is not clear that this is correct. Litigation funding would need to first satisfy the definition of ‘financial service’ in [section 5](#) of the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act). The issues paper at 15.60-15.62 notes that it is unclear whether litigation funding is a financial service, and that only two litigation funders are registered as credit contract providers.

Please contact me should you wish to discuss any of our comments.

Yours sincerely



Joanne Davis-Calvert
Head of Policy & Governance