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# **DRAFT REPORT**

with recommendations to the Commission on Responsible private funding of  
litigation  
(2020/2130(INL))

Committee on Legal Affairs

Rapporteur: Axel Voss

(Initiative – Rule 47 of the Rules of Procedure)

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## MOTION FOR A EUROPEAN PARLIAMENT RESOLUTION

### with recommendations to the Commission on Responsible private funding of litigation (2020/2130(INL))

*The European Parliament,*

- having regard to Article 225 of the Treaty on the Functioning of the European Union,
  - having regard to Article 5 of the Decision of the European Parliament of 28 September 2005 adopting the Statute for Members of the European Parliament<sup>1</sup>,
  - having regard to Rules 47 and 54 of its Rules of Procedure,
  - having regard to Directive (EU) 2020/1828 of the European Parliament and of the Council of 25 November 2020 on representative actions for the protection of the collective interests of consumers and repealing Directive 2009/22/EC<sup>2</sup>,
  - having regard to Commission Recommendation of 11 June 2013 on common principles for injunctive and compensatory collective redress mechanisms in the Member States concerning violations of rights granted under Union Law,
  - having regard to the Study conducted by the European Parliament Research Service ‘Responsible Private Funding of Litigation’ of March 2021,
  - having regard to the report of the Committee on Legal Affairs (A9-0000/2021),
- A. whereas third party litigation funding (TPLF) is a growing practice whereby commercial investors (‘litigation funders’) who are not a party to a dispute invest in legal proceedings and pay legal and other expenses, in exchange for a share of any eventual award; whereas TPLF does not only occur in collective redress cases but also in arbitration and insolvency proceedings;
- B. whereas litigation funders involved in legal proceedings act in their own economic interest, rather than in the interest of claimants; whereas they can seek to control the litigation and demand an outcome that pays them the greatest return<sup>3</sup>;
- C. whereas litigation funders often demand a disproportionate share of the proceeds that exceed the typical returns of other types of investments; whereas the rates of returns for

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<sup>1</sup> OJ L 262, 7.10.2005, p. 1.

<sup>2</sup> OJ L 409, 4.12.2020, p. 1.

<sup>3</sup> The Australian Parliament concluded “the level of power and influence litigation funders have in class actions gives rise to situations where their financial interests trump those of the representative plaintiff and class members”, see Australian Law Reform Commission (2019): An Inquiry into Class Action Proceedings and Third-Party Litigation funders, p 19.

litigation funders can be up to 300% or in some cases even 3 000%<sup>4</sup>, directly taking from the compensation available for claimants<sup>5</sup>;

- D. whereas litigation funders seem to argue that only they can provide access to justice, there are in fact other ways to seek redress, such as mediation, ADR/ODR, the Ombudsman or through grievance systems managed by companies; whereas, those solutions could result in faster and more adequate compensation for claimants;
- E. whereas, although TPLF is widespread in Australia, it has not had a positive impact on the administration of justice in that jurisdiction; whereas, empirical data<sup>6</sup> show that litigation funders typically pick and choose between cases to find the best returns, and would not invest in cases they regard as too risky or not profitable enough;
- F. whereas the number of litigation funders is increasing with currently more than 45 known to operate in the EU; whereas, the practice of TPLF however remains largely unregulated in the Union, despite presenting material risks to the administration of justice;
- G. whereas the current regulatory vacuum enables litigation funders to operate in secrecy, with the result that courts can, on occasion, make awards to claimants without realising that a large majority of the award will subsequently be redirected to litigation funders; whereas the lack of transparency can also mean that even the potential beneficiaries have little or no knowledge about the distribution of awards or the funding agreements, in particular in Members States with an opt-out system;
- H. whereas Directive (EU) 2020/1828 identifies certain safeguards relating to litigation funding, which are, however, limited to representative actions on behalf of consumers taken under that Directive, and therefore exclude many other types of action or categories of claimants; whereas, effective safeguards should apply to all types of claims;

### *Introduction*

1. Observes that third party litigation funding is a rapidly expanding commercial practice in the Union, which has a significant impact on justice systems as well as on European citizens. Notes that litigation funding is so far largely unregulated in the Union;
2. Firmly believes that in order to ensure that justice systems prioritise redress for victims of injustice, and not the interests of investors who may seek commercial opportunity

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<sup>4</sup> See Bentham(2014): Submission to the Ministry of Security and Justice. Dutch Draft Bill on Redress of Mass Damages in a Collective Action, par. 2.15 on page 5 as well as 1266/7/7/16 Walter Hugh Merricks CBE v MasterCard Incorporated and Others – Judgment (CPO Application) [2017] CAT 16 | 21 Jul 2017 in section 99 and 100 on page 37 and 38.

<sup>5</sup> In Australia, the median return for claimants of collective redress proceedings involving TPLF is 51% while claimants of legal proceedings without the involvement of litigation funders get 85%. See Australian Law Reform Commission (2019): An Inquiry into Class Action Proceedings and Third-Party Litigation Litigation funders, p 83.

<sup>6</sup> See Australian Law Reform Commission (2019): An Inquiry into Class Action Proceedings and Third-Party Litigation funders, p 34.

from disputes, a regulatory regime addressing key issues relevant to litigation funding, including transparency, fairness, and proportionality, is necessary;

3. Strongly believes that only the regulation of litigation funders will allow regulators to exercise effective oversight and adequately ensure that the interests of claimants are protected. Points out that voluntary regulatory mechanisms and codes of conduct have not been subscribed to by the large majority of funders, leaving claimants significantly exposed;

#### *Regulation and supervision of litigation funders*

4. Recommends the establishment of a system of authorisation for litigation funders, permitting the introduction of corporate governance requirements and supervisory powers to protect claimants, and to ensure that funding is only provided by entities that are committed to complying with minimum standards in terms of transparency, governance and capital adequacy, and observing a fiduciary relationship vis-à-vis claimants and intended beneficiaries;

#### *Ethical issues*

5. Recommends that litigation funders be obliged to respect a fiduciary duty of care requiring them to act in the best interests of a claimant. Believes that litigation funders should be prevented from exercising control over the legal proceedings they fund, which should be the sole responsibility of the claimant and their legal representatives. Points out that such control over the legal proceedings they fund can consist both of formal control, such as a contractual power to make decisions, and informal control, such as the threat to withdraw the funding;
6. Underlines that conflicts of interest may arise where there are relationships between litigation funders, qualified entities, law firms, aggregators, including claims-collection and award-distribution-platforms, and other actors who may be involved in claims. Notes that there is a trend of an increasingly close cooperation, with, for example, litigation funders agreeing to finance law firms across a series of future cases (portfolio funding)<sup>7</sup>. Recommends that safeguards are adopted to prevent such conflicts, set out claimants' rights and to require that details of relationships between litigation funders and the other involved parties are disclosed;
7. Believes that litigation funders should not be permitted to abandon funded parties in litigation, except in restricted and well-defined circumstances, leaving claimants solely responsible for all costs of the litigation, which may have only been pursued due to the involvement of the funder;
8. Believes that, just like claimants, litigation funders should be responsible for the defendants' costs arising from unsuccessful litigation (such as an adverse cost award). Is of the opinion that regulation should prevent litigation funders from limiting their liability to costs in the event of an unsuccessful outcome;

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<sup>7</sup> EPRS Study (2021): Responsible litigation funding. State of play on the EU private litigation funding landscape and on the current EU rules applicable to private litigation funding, p. 28 -29.

### *Incentives and limits on recovery*

9. Considers that legislation should impose limits on the proportion of the award that litigation funders are entitled to by virtue of a funding agreement. Believes that only under exceptional circumstances arrangements between litigation funders and claimants should vary from the rule that a minimum of 60% of the gross settlement or damages is paid to the claimants;

### *Disclosure and transparency*

10. Considers that there should be transparency regarding the involvement of litigation funding in legal proceedings, including obligations for claimants and their lawyers to disclose funding agreements to courts and defendants. Notes that, currently, courts or administrative authorities and defendants are often not aware that a claim is funded by a commercial actor. Points out that this can also hinder a court or administrative authority in properly considering costs issues and in ensuring that awards compensate claimants adequately;

### *Powers of supervisory authorities and review by courts and administrative authorities*

11. Is of the opinion that supervisory authorities, and courts and administrative authorities were appropriate in accordance with national procedural law, should have the powers to facilitate the enforcement of legislation adopted to achieve the goals set out above; recommends the establishment of a complaints system. Considers that supervisory authorities, and courts and administrative authorities where appropriate in accordance with national procedural law, should have the powers to address abusive practices by authorised litigation funders;

### *Final aspects*

12. Requests the Commission to submit a proposal for a directive to regulate third party litigation funding, following the recommendations set out in the Annex hereto;
13. Considers that the requested proposal will not have financial implications;
14. Instructs its President to forward this resolution and the accompanying recommendations to the Commission and the Council;

**ANNEX TO THE MOTION FOR A RESOLUTION:  
RECOMMENDATIONS AS TO THE CONTENT OF THE PROPOSAL REQUESTED**

Proposal for a

**DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL  
on the regulation of third-party litigation funding**

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Economic and Social Committee,<sup>1</sup>

Acting in accordance with the ordinary legislative procedure,<sup>2</sup>

Whereas:

- (1) Third-party litigation funding is a commercial practice which is quickly developing into a litigation services market without any proper legislative framework being in place at Union level. Despite the fact that litigation funders are regularly established and operating in various Member States, domestically or across borders, they have so far been subject to different national rules and practices. Diverging rules and practices in Member States are likely to constitute an obstacle to the functioning of the internal market. A lack of clarity on the terms on which commercial third party litigation funders (“litigation funders”) may operate, in particular taking into account that litigation funders can easily be attracted by cross-border cases, is not compatible with the proper functioning of the internal market. Divergences in the legal framework applicable in each Member State entail a risk of forum shopping by litigation funders, which could be influenced by the favourability of certain national rules concerning their establishment, the law applicable to funding agreements and national procedural rules.
- (2) Union law seeks to ensure a balance between access to justice and providing appropriate safeguards to those engaged in proceedings, to prevent their wish to access justice from being unjustly exploited. When litigation funders provide financing for legal proceedings in exchange for a share of any compensation awarded, a material risk of injustice can arise. That risk includes litigation funders being able to take advantage of claimants, or those they represent, including where relevant consumers whose interests are represented by qualified entities, to serve their own purposes and to maximise their own return, thus leaving claimants or intended beneficiaries materially disadvantaged. The risks can be particularly acute where those expecting to benefit from litigation are consumers, who might welcome the involvement of a litigation funder ready to pay for

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<sup>1</sup> OJ [...]

<sup>2</sup> OJ [...]

proceedings, without appreciating that their interests could be subverted in favour of the litigation funder's own interests.

- (3) As the internal market facilitates increasing cross-border trade, as disputes are increasingly cross-border, and as the activities of litigation funders are global in nature, the risk of material divergences in Member State approaches to safeguards and the protections necessary with regard to third party funding is acute. Voluntary approaches have not been successful or subscribed to by the majority of the industry, and, in any event, non-legislative measures would not be appropriate in light of such material risks, including to consumers.
- (4) This Directive aims to regulate third-party litigation funding, a commercial practice whereby third-party entities not directly involved in a dispute invest for profit in legal proceedings, typically in exchange for a percentage of any settlement or award. Third-party litigation funding does not include provision of funds to sponsor litigation on a charitable or donated basis, or similar activities carried out on a pro bono publico basis. This Directive also aims to lay down safeguards to prevent conflicts of interest, abusive litigation as well as the disproportionate allocation of monetary awards to litigation funders.
- (5) The term 'litigation funder' should be understood to refer to any undertaking that is not a party to proceedings, but enters into a third-party litigation funding agreement ('third-party funding agreement') in relation to those proceedings. In line with the case-law of the Court of Justice of the European Union, the concept of 'undertaking' includes any entity engaged in an economic activity, regardless of its legal status and the way in which it is financed, and therefore includes any legal person, including its parents, subsidiaries or affiliates and could include professional litigation-funding providers, financial services providers, claims management firms or other service providers. The concept of litigation funder is not intended to include lawyers representing a party in legal proceedings, or regulated providers of insurance services to such a party.
- (6) In accordance with the legal traditions and autonomy of the Member States, it is for each Member State to determine whether, and to what extent, the provision of litigation funding should be permitted within its own legal system. Where Member States choose to permit such third party litigation funding, this Directive provides for minimum standards for the protection of funded claimants, so that those who might have recourse to litigation funding in the Union are covered by a minimum level of protection, which is consistent across the Union.
- (7) Where third party litigation funding activity is permitted, a system for the authorisation and supervision of litigation funders by independent administrative bodies in the Member States is necessary to ensure that such litigation funders meet the minimum criteria and standards laid down in this Directive. Litigation funders should be subject to oversight in a manner similar to that of the existing prudential supervision system applicable to financial services providers.
- (8) Litigation funders active in the Union should be required to conduct their business from within the Union, be authorised within the Union, and to conclude their third-party funding agreements subject to the laws of the Member State of the proceedings or, if different, the Member State of the claimant or intended beneficiaries, in order to ensure

that supervision under Union and national law is adequate.

- (9) Supervisory authorities within the Union granting authorisations to conduct third-party litigation funding activities should be empowered to require that litigation funders comply with minimum criteria laid down by this Directive. Such criteria should include provisions relating to governance, transparency, capital adequacy, and observance of a fiduciary duty to claimants and intended beneficiaries. Supervisory authorities should be empowered to make any necessary orders, including the power to receive from litigation funders applications for authorisation and to decide upon them, to gather any necessary information, grant, deny or withdraw any authorisation or to impose any condition, restriction or penalty upon any litigation funder, as well as to investigate any complaint against any litigation funder conducting activities within their jurisdiction.
- (10) Among other authorisation criteria, Member States should require litigation funders to demonstrate that they have sufficient capital to satisfy their financial obligations. The absence of capital adequacy requirements creates a risk that an undercapitalised litigation funder enters into a third-party funding agreement and is not willing or able subsequently to cover the costs of the litigation it had agreed to support, including the costs or fees necessary to allow the proceedings to reach their conclusion, or any adverse cost award. This can expose claimants who rely on litigation funders to a risk of material unforeseen economic loss, and to the risk of the abandonment of otherwise viable proceedings due to the business circumstances or decisions of the litigation funder.
- (11) Litigation funders should be required to commit to being bound to a duty to act fairly, transparently and in the best interests of claimants and intended beneficiaries of claims. A lack of a requirement to place the interests of claimants and intended beneficiaries ahead of a litigation funder's own interests creates the risk of proceedings being directed in a manner that ultimately serves the interests of the litigation funder, rather than those of the claimant.
- (12) To prevent circumvention of the requirements of this Directive, agreements entered into with third party funders not having the necessary authorisation should have no legal effect. The burden to acquire the necessary authorisations should be on litigation funders themselves, and therefore claimants and intended beneficiaries should be indemnified in respect of any harm caused by a litigation funder not having the necessary authorisation.
- (13) This Directive should regulate the activities of litigation funders, but should be without prejudice to any other regulatory obligations or regimes that may apply.
- (14) To facilitate the consistent application of this Directive, Member States should ensure that their supervisory authorities apply this Directive in close cooperation with the supervisory authorities of other Member States. Coordination between supervisory authorities should be organised at Union level to avoid the divergence of supervisory standards, which could jeopardise the proper functioning of the internal market.
- (15) The Commission should coordinate the activities of supervisory authorities and facilitate the creation of a suitable cooperation network for this purpose. Supervisory authorities should be enabled to consult the Commission as necessary, and the Commission should be allowed to issue guidelines, recommendations, best practice

notices or advisory opinions to supervisory authorities on the application of this Directive, and in relation to any apparent inconsistency with regard to the implementation of this Directive. Supervisory authorities should share details of their activities with the Commission to facilitate coordination, including sharing details of all decisions taken and litigation funders they authorise.

- (16) To facilitate the provision of cross border litigation funding services in those Member States where it is permitted under national law, Member States should be able to cooperate, share information, and should be required to take full account of each other's authorisation decisions.
- (17) Member States should ensure that decisions regarding the relevant legal proceedings, including decisions on settlement, are not unduly influenced by the litigation funder in a manner that would be detrimental to the interests of the claimants concerned by that action.
- (18) Courts or administrative authorities should be empowered to ensure the provision of sufficient disclosure of relevant information on all third-party litigation funding activity relevant to the legal proceedings under their responsibility.
- (19) Courts or administrative authorities should be empowered, where a third-party funding agreement is relevant to the case before them, either upon request by a party to the proceedings to review the agreement, or following an action brought before them against the administrative decision of a supervisory authority which has become final, to deal with such a case in a way which allows them to assess whether this Directive is complied with.
- (20) To redress any knowledge or resource imbalance between a litigation funder and a claimant, in assessing the suitability of a third-party funding agreement, courts or administrative authorities should take into account the level of clarity and transparency of such agreements, and the degree to which any risks and benefits were transparently presented to and knowingly undertaken by claimants or those represented by claimants.
- (21) Third party funding agreements should be presented to claimants in a language they understand, and should set out clearly and in appropriate terms the range of possible outcomes, as well as any risks and relevant limitations.
- (22) The adequacy of supervision of litigation funders and third-party funding agreements cannot be ensured absent obligations on litigation funders to be transparent regarding their activities. This includes transparency vis-à-vis courts or administrative authorities, defendants and claimants, and therefore obligations should apply to disclose third party funding agreements in full to courts or administrative authorities and defendants, subject to appropriate limitations to protect any necessary confidentiality.
- (23) In proceedings to which a third-party funding agreement applies, the relevant court or administrative authority should assess upon request by a party to the proceedings whether that agreement complies with this Directive and whether claimants and those they represent, including consumers, are protected.
- (24) Litigation funders should establish internal processes to avoid conflicts of interests between the litigation funder and claimants. Compliance with transparency

requirements should ensure that claimants are fully aware of any relationship a litigation funder may have with defendants, lawyers, other litigation funders, or any other third party, which may create an actual or perceived conflict.

- (25) Litigation funders that have a direct interest in the financial outcome of proceedings may be incentivised to claim unfair, disproportionate or unreasonable rewards at the expense of claimants. Courts or administrative authorities should be empowered to assess the context of third-party funding agreements relevant to the case before them, including the legal position and the knowledge of the claimants, in order to determine effectively whether in all the circumstances the third-party funding agreement is fair and complies with the laws of the Member State concerned.
- (26) Where third-party funding agreements permit litigation funders to receive a share of any reward or certain fees in priority to any awards allocated to claimants, the available award could be so reduced as to leave little or nothing for claimants. Litigation funders should not be permitted to require the prioritisation of their own reward.
- (27) As the share of any reward received by litigation funders reduces any relief obtained by claimants, courts or administrative authorities should exercise oversight over the value and proportion of this share to prevent any disproportionate allocation of monetary awards to litigation funders. Save in exceptional circumstances, when a share of any reward claimed by a litigation funder would dilute the share of any total award (including all damages amounts, costs, fees and other expenses) available to claimants and intended beneficiaries to 60% or below, it should be presumed unfair and invalid.
- (28) Additional conditions should be put in place to ensure that litigation funders do not influence the decisions of claimants in the course of proceedings in a manner that would benefit the litigation funder itself. In particular, litigation funders should not direct or influence decisions on how cases are pursued, which interests are prioritised, or whether or not claimants should accept any particular outcome, award or settlement.
- (29) Litigation funders should not be allowed to withdraw the funding they have agreed to provide, except in limited circumstances as set out in this Directive, so that funding is not withdrawn to the disadvantage of claimants or intended beneficiaries in mid-case due to the litigation funder's business interests or incentives changing.
- (30) Where litigation funders have instigated, supported or funded proceedings which are not successful, they should be jointly liable with claimants for any adverse costs they caused defendants to incur and that may be awarded by courts or administrative authorities. Courts or administrative authorities should be granted adequate powers to ensure the effectiveness of such an obligation, and third party funding agreements should not exclude responsibility for such adverse costs.
- (31) Member State courts or administrative authorities should be entitled to determine any adverse costs awards in accordance with national law, including by reliance on any scientific, statistical or technical evidence as may be relevant, or through reliance on any experts, assessors or tax accountants, as may be suitable in the circumstances of the proceedings.
- (32) This Directive respects fundamental rights and observes principles recognised in particular by the Charter of Fundamental Rights of the European Union. Accordingly,

this Directive should be interpreted and applied in accordance with those rights and principles, including those related to the right to an effective remedy and to a fair trial, as well as the right of defence.

- (33) The objectives of this Directive, namely to ensure the harmonisation of Member States' rules applicable to litigation funders and their activities, and thus to ensure that common minimum standards for the protection of the rights of funded claimants and intended beneficiaries in proceedings financed wholly or in part by third-party funding agreements apply in all Member States, cannot be sufficiently achieved by the Member States as litigation funders operate in multiple Member States and are subject to different national rules and practices, but can rather, by reason of the scale of the emerging market of third-party litigation funding, the need to avoid diverging rules and practices that are likely to constitute an obstacle to the proper functioning of the internal market and the need to avoid 'forum shopping' by litigation funders seeking to optimise national rules, be better achieved at Union level. The Union may thus adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality, as set out in that Article, this Directive does not go beyond what is necessary in order to achieve those objectives.
- (34) In accordance with the Joint Political Declaration of 28 September 2011 of Member States and the Commission on explanatory documents, Member States have undertaken to accompany, in justified cases, the notification of their transposition measures with one or more documents explaining the relationship between the components of a directive and the corresponding parts of national transposition instruments. With regard to this Directive, the legislator considers the transmission of such documents to be justified.

HAVE ADOPTED THIS DIRECTIVE:

## *Chapter I*

### *General Provisions*

#### *Article 1*

##### *Subject Matter and purpose*

This Directive is aimed at harmonising the rules of Member States applicable to third-party litigation funders ('litigation funders') and their authorised activities, and also at protecting funded claimants and intended beneficiaries, including where relevant those whose interests are represented by qualified entities, in proceedings financed wholly or in part by third-party litigation funding. It lays down safeguards to prevent conflicts of interest, abusive litigation as well as the disproportionate allocation of monetary awards to litigation funders.

#### *Article 2*

##### *Scope*

This Directive applies to third party litigation funders and to the third-party funding agreements that they are entitled to offer to claimants in the Union.

#### *Article 3*

##### *Definitions*

For the purposes of this Directive, the following definitions apply:

- (a) 'litigation funder' means any undertaking that enters into a third-party funding agreement in relation to proceedings, even though it is neither a party to those proceedings, a lawyer representing a party to such proceedings, or a provider of regulated insurance services to a party in such proceedings;
- (b) 'claimant' means any natural or legal person who brings or intends to bring proceedings against another party before a court or administrative authority;
- (c) 'court or administrative authority' means a competent court, administrative authority, arbitral body or other body tasked with adjudicating on proceedings;
- (d) 'intended beneficiary' means a person who is entitled to share directly in the distribution of an award in proceedings and whose interests in the proceedings are represented by the funded claimant or a qualified entity bringing the action;
- (e) 'proceedings' means any domestic or cross border civil or commercial litigation, or any voluntary arbitration procedure or alternative dispute resolution mechanism, through which redress before a court or administrative authority in the Union is sought concerning a dispute;

- (f) ‘qualified entity’ means an organisation representing consumers’ interests and designated as qualified under Directive (EU) 2020/1828;
- (g) ‘supervisory authority’ means a public authority designated by a Member State to be responsible for granting or withdrawing the authorisation for litigation funders, and for supervising the activities of litigation funders;
- (h) ‘third-party funding agreement’ means an agreement in which a litigation funder agrees to fund all or part of the costs of proceedings in exchange for receiving a share of the monetary amount awarded to the claimant or a success fee, so as to cover the reimbursement of its funding and, where applicable, remuneration for the service provided, based wholly or partially on the outcome of proceedings. This definition includes all agreements in which such a reward is agreed, whether offered as an ‘arm’s length’ service, or achieved through a purchase or assignment of the claim.

## *Chapter II*

### *Approval of litigation funders’ activities within the Union*

#### *Article 4*

##### *Authorisation system*

1. Member States may determine in accordance with national law whether third party funding agreements can be offered in relation to proceedings within their Member State, or for the benefit of claimants or intended beneficiaries resident within their Member State.
2. Where such activities are permitted, Member States shall create a system for the authorisation of the activities of litigation funders within their Member State. That system shall include designating an independent supervisory authority tasked with granting or withdrawing authorisations for litigation funders and supervising the activities of litigation funders.
3. The system of authorisation provided for by this Directive shall apply only to the activities connected to the offering of third-party funding agreements by litigation funders. Where litigation funders are also providers of other legal, financial or claims management services supervised by another authority within the Union, this Directive shall be without prejudice to any system of supervision and authorisation that exists in relation to those other services.

#### *Article 5*

##### *Conditions for authorisation*

1. Member States shall ensure that supervisory authorities only grant or maintain authorisations, whether for domestic or cross-border litigation or other proceedings, to litigation funders who comply with the provisions of this Directive, and who meet, in addition to any suitability or other criteria as may be set out in national law, at least the following criteria:

- (a) they conduct their business through a registered office in a Member State, and apply for and maintain an authorisation in that same Member State;
  - (b) they commit to concluding third-party funding agreements subject to the laws of the Member State of any intended proceedings, or, if different, of the Member State of the claimant or intended beneficiaries;
  - (c) they demonstrate to the satisfaction of the supervisory authority that they have procedures and governance structures in place to ensure their ongoing compliance with this Directive, with the transparency requirements and fiduciary relationships this Directive provides for, and with any additional national requirements relating to the conclusion of third-party funding agreements;
  - (d) they meet the capital adequacy requirements set out in Article 6; and
  - (e) they satisfy the supervisory authority that they have the governance and procedures in place to ensure that the fiduciary duty provided for in Article 7 is discharged and respected.
2. The system of authorisation established by this Directive shall be without prejudice to the application of Union law governing the provision of financial services, investment activity, or consumer protection as may apply to litigation funders.

#### *Article 6*

##### *Capital adequacy*

1. Member States shall ensure that supervisory authorities are empowered to verify whether litigation funders would be able to have at their disposal at all times adequate financial resources to fulfil their liabilities under their third-party funding agreements. In particular, supervisory authorities shall ensure that litigation funders have the capacity to:
- (a) pay all debts arising from their third-party funding agreements when they become due and payable;
  - (b) fund all stages of any proceedings they have committed to, including to trial and any subsequent appeal, and
  - (c) cover aggregate funding liabilities under all of the third-party funding agreements they have entered into, for a period of 24 months.
2. Member States shall ensure that supervisory authorities are empowered to verify whether litigation funders would be able to maintain access at all times to the minimum liquidity required to pay in full all foreseeable adverse costs in all proceedings they have funded. Member States shall ensure that their courts or administrative authorities can request litigation funders to provide security for costs in the forms admitted by national law, should a defendant so request based on reasoned specific concerns.

#### *Article 7*

##### *Fiduciary duty*

1. Member States shall ensure that supervisory authorities are empowered to verify that litigation funders have the governance and internal procedures in place to ensure that the third-party funding agreements they enter into are based on a fiduciary relationship and that they commit under those agreements to acting fairly, transparently and in the best interests of a claimant.
2. Where a claimant intends to take a claim on behalf of others in proceedings, such as where the claimant is a qualified entity representing consumers, the litigation funder shall also be required to owe a fiduciary duty to such intended beneficiaries. Litigation funders shall be obliged to acting in a manner that is consistent with their fiduciary duty throughout the course of proceedings. In the event of a conflict between the interests of the litigation funder and those of claimants or intended beneficiaries, the litigation funder shall commit to placing the interests of the claimants or intended beneficiaries above its own interests.

### *Chapter III*

#### *Powers of supervisory authorities and coordination between them*

#### *Article 8*

##### *Powers of supervisory authorities*

1. In the Member States where third party funding agreements are permitted in accordance with Article 4, Member States shall provide that an independent public supervisory authority is responsible for overseeing the authorisation of litigation funders established within its jurisdiction, offering third party funding agreements to claimants and intended beneficiaries within its jurisdiction, or in relation to proceedings within its jurisdiction.
2. Member States shall ensure that a complaints procedure before supervisory authorities is available for any natural or legal person who wishes to raise concerns regarding the compliance of a litigation funder with its obligations under this Directive and the applicable national law.
3. Each supervisory authority shall in particular be empowered and required to:
  - (a) receive from litigation funders applications for authorisation and any information that is necessary for the purposes of considering those applications, and decide upon any such applications in a timely fashion;
  - (b) take any decisions necessary to grant or deny authorisation to any applicant litigation funder, to withdraw any authorisation, or to impose any condition, restriction or penalty upon any authorised litigation funder;
  - (c) decide on the suitability and fitness of a litigation funder including by reference to their experience, reputation, any conflicts of interest or knowledge;
  - (d) publish on its website any decision taken pursuant to point (b), having due regard

to commercial confidentiality;

- (e) assess at least every year whether an authorised litigation funder continues to comply with the criteria for authorisation referred to in Article 5(1) and ensure that such authorisation is withdrawn if it no longer complies with one or more of those criteria.
  - (f) under the system referred to in Article 9, receive and investigate complaints in relation to the conduct of a litigation funder and the compliance of such litigation funder with the provisions laid down in Chapter IV of this Directive and any other applicable requirements under national law.
4. Member States shall ensure that litigation funders are required to notify a supervisory authority without delay of any changes affecting compliance by a litigation funder with the capital adequacy requirements laid down in Article 6 paragraphs 1 and 2. In addition, Member States shall ensure that litigation funders certify, at regular intervals and at least once annually, that they remain in compliance with those paragraphs. Such a certification shall contain the opinion of a recognised national or international audit firm that the litigation funder is in compliance.
5. Member States shall ensure that supervisory authorities oversee fiduciary relationships between litigation funders and claimants and intended beneficiaries in general, and are able to make directions and orders to ensure that claimants' interests and those of intended beneficiaries are protected.

### ***Article 9***

#### ***Investigations and complaints***

1. Member States shall ensure that a complaints system is in place that allows for the reception and investigation of complaints as referred to in Article 8, paragraph 2.
2. Under the complaints system referred to in paragraph 1, Member States shall ensure that supervisory authorities are empowered to assess whether a litigation funder is in compliance with any obligations or conditions associated with its authorisation, with the provisions of this Directive and with any other applicable requirements under national law.
3. Member States shall ensure that, in exercising their oversight with litigation funders' compliance with such obligations, supervisory authorities are empowered to:
- (i) investigate complaints received from any natural or legal person;
  - (ii) investigate complaints from any other supervisory authority or the Commission;
  - (iii) initiate investigations on an ex officio basis,
  - (iv) initiate investigations following a recommendation from a court or administrative authority that has concerns regarding a litigation funder's compliance with such obligations arising from any proceedings before such a court or administrative

authority.

### ***Article 10***

#### ***Coordination between supervisory authorities***

1. Member States shall ensure that their supervisory authorities apply this Directive in close cooperation with the supervisory authorities of other Member States.
2. The Commission shall oversee and coordinate the activities of the supervisory authorities in performing the functions set out in this Directive, and shall convene and chair a network of supervisory authorities. The modalities for cooperation within the network shall be laid down and revised by the Commission by means of delegated acts, in close cooperation with the supervisory authorities.
3. The supervisory authorities may consult the Commission on any matter involving the implementation of this Directive. The Commission may issue guidelines, recommendations, best practice notices and advisory opinions to supervisory authorities on the implementation of this Directive, and in relation to any apparent inconsistency in this regard, or in relation to the supervision of any litigation funders. The Commission may also set up a centre of competence to provide qualified expertise to court or administrative authorities seeking advice on how to assess litigation funders' activities within the Union.
4. Each supervisory authority shall communicate every quarter to the Commission a list of the litigation funders it has authorised and make that list publicly available. Supervisory authorities shall inform the Commission each and every time there is a change to that list.
5. Each supervisory authority shall communicate every quarter to the Commission and other supervisory authorities details of all decisions taken with regard to the supervision of litigation funders, including details of all decisions taken pursuant to Article 8(2)(b).
6. Where a litigation funder has sought authorisation from a supervisory authority, and subsequently seeks authorisation from another, such supervisory authorities shall coordinate and share information to the extent appropriate, with a view to taking consistent decisions.
7. Where a litigation funder is authorised by a supervisory authority in a Member State, but wishes to offer a third party funding agreement for the benefit of a claimant or other intended beneficiary in another Member State, or for proceedings in another Member State it shall notify the supervisory authority of the host Member State, and present proof of authorisation from its home Member State supervisory authority.

### ***Chapter IV***

#### ***Third party funding agreements and activities of litigation funders***

### ***Article 11***

#### ***Content of third party funding agreements***

Member States shall ensure that third party funding agreements are required to be written in one or more of the official languages of the Member State in which the claimant(s) and intended beneficiaries are resident, and presented in clear and easily understood terms, in particular with regard to the following elements:

- a. the share of any award or fees that will be paid to the litigation funder or any other third party, or any other financial costs borne by the claimants and /or intended beneficiaries directly or indirectly both in absolute terms, and also modelled on a range of realistic outcomes given the facts then known about the claim;
- b. the risks that the claimants and/or intended beneficiaries are assuming, including:
  - i. any restrictions on the claimants' autonomy in issuing instructions to the claimant law firm or otherwise controlling the conduct of the litigation;
  - ii. the scope for escalating costs in the litigation, and how that impacts the financial interests of the claimants and/or beneficiaries;
  - iii. the circumstances in which the third party funding agreement can be terminated and the risks to claimants and/or beneficiaries in that scenario, and
  - iv. any potential risk of having to pay adverse costs, including circumstances in which adverse costs insurance or indemnities may not cover such exposure.

### ***Article 12***

#### *Transparency requirements and avoidance of conflicts of interest*

1. Member States shall require litigation funders to establish a policy and to implement internal processes for the avoidance and resolution of conflicts of interest. That policy and those internal processes shall be appropriate to the nature, scale and complexity of the litigation funder's business, and shall be set out in writing and made publicly available on the litigation funder's website. They shall also be clearly stated in an annex to any third-party funding agreement.
2. Member States shall require litigation funders to disclose to a claimant and intended beneficiaries in the third-party funding agreement all information that may reasonably be perceived as having the potential to give rise to a conflict of interest. Required disclosures shall include at least the following:
  - (a) details of any arrangements that exist, financial or otherwise, between the litigation funder and any other undertaking that relates to the proceedings, including any arrangements with any relevant qualified entity, claims aggregator, lawyers, or other interested party;
  - (b) details of any other third-party funding agreements that the litigation funder has entered into which are related, relevant or similar to the claimant's case, and
  - (c) details of any relevant connection between the litigation funder and a defendant in the proceedings.

### ***Article 13***

### *Invalid agreements and clauses*

1. Member States shall ensure that third-party funding agreements concluded with persons who are not authorised to act as a litigation funder have no legal effect.
2. Member States shall ensure that third-party funders are not permitted to influence the decisions of a claimant in the course of proceedings. To this end, any clause in third-party funding agreements granting a litigation funder the power to take or influence decisions in relation to proceedings shall have no legal effect. Any such clause or arrangement consisting of, inter alia, the following shall have no legal effect:
  - (a) the grant of an explicit power to a litigation funder to take or influence decisions in the course of proceedings, such as with respect to specific claims pursued, settlement of the case, or management of expenses associated with the proceedings;
  - (b) the provision of capital, or any other resource with a monetary value, for the purposes of proceedings contingent on the approval by third-party funders of its specific use.
3. Member States shall provide that agreements in which a litigation funder is guaranteed to receive a minimum return on its investment before a claimant or intended beneficiary can receive their share, have no legal effect.
4. Absent exceptional circumstances, where a litigation funding agreement would entitle a litigation funder to a share of any award that would dilute the share available to the claimant and the intended beneficiaries to 60% or below of the total award (including all damages amounts, costs, fees and others expenses), such an agreement shall have no legal effect.
5. Member States shall ensure that third-party funding agreements do not contain provisions that limit the liability of a litigation funder in the event of an order for adverse costs following unsuccessful proceedings. Provisions that purport to limit a litigation funder's liability for costs shall have no legal effect.
6. Claimants and intended beneficiaries shall be indemnified in respect of any losses caused by a litigation funder that entered into a third-party funding agreement which is found to be invalid.

### *Article 14*

#### *Termination of third-party funding agreements*

1. Member States shall prohibit the termination of a third-party funding agreement by a litigation funder without the claimant's informed consent, except where a court or administrative authority has granted the litigation funder permission to terminate the agreement, having considered whether the interests of the claimant and intended beneficiaries would be adequately protected despite the termination.
2. Sufficient notice as provided for in national law shall be required to be given in order to terminate the third-party funding agreement.

## *Chapter V*

### *Review by courts or administrative authorities*

#### *Article 15*

##### *Disclosure of the third-party funding agreement*

1. Member States shall ensure that claimants or their representatives are required to provide a complete and unredacted copy of any third-party funding agreements relating to the proceedings concerned to the relevant court or administrative authority at the earliest stage of those proceedings.
2. Member States shall ensure that courts or administrative authorities are empowered, upon request by a party to the proceedings, where that party has justified doubts in respect of the compliance of such third party funding agreement with this Directive and any other applicable national law in accordance with Article 16.
3. Where paragraph 2 applies, in accordance with national procedural law, subject to the applicable Union and national rules on confidentiality, Member States shall ensure, if requested by the defendant, that the court or administrative authority is able to require the claimants or their representatives to provide the defendant with a copy of any third-party funding agreement used to support the proceedings. The court or administrative authority may permit certain information, which could confer a tactical advantage to a defendant to be redacted from the third-party funding agreement prior to disclosure to the defendant.

#### *Article 16*

##### *Review of third-party funding agreements by courts or administrative authorities*

Member States shall designate the competent court or administrative authority to perform the different judicial and administrative tasks under this Directive. Such designation shall in particular specify which court or administrative authority is to conduct controls on the impact of funding agreements on the cases before them, by exercising powers:

- (a) to make orders or give directions that are binding on a litigation funder, such as requiring the litigation funder to provide the funding as agreed in the relevant third-party funding agreement or requiring the litigation funder to make changes in respect of the relevant funding and, if necessary, rejecting the legal standing of the funded claimant, in particular, when the action is brought by a qualified entity, in accordance with Article 10, paragraph 4, of Directive (EU) 2020/1828 of the European Parliament and of the Council;
- (b) to assess the compliance of each third-party funding agreement with the provisions laid down in this Directive, particularly with the fiduciary duty owed to claimants and intended beneficiaries under Article 7, and, where that agreement is found not to be compliant, order the litigation funder to make the necessary changes, or declare the clause to be null and void in accordance with Article 13;

- (c) to evaluate the suitability of each third-party funding agreement with respect to the transparency requirements under Article 12, taking in particular into account the level of clarity and transparency of the third-party funding agreement, and the degree to which any risks and benefits were presented to and knowingly undertaken by claimants or those intended beneficiaries represented by claimants;
- (d) to assess whether a third-party funding agreement entitles a litigation funder to an unfair, disproportionate or unreasonable share of any award, and to annul or adjust such agreements accordingly. Member States shall specify that in making such an assessment, competent courts or administrative authorities may take into consideration the characteristics and circumstances of the intended or ongoing proceedings including, as appropriate:
  - (i) the parties that are involved in the case, as well as the intended beneficiaries of the proceedings, and what they understood to be agreed as regards the amount the litigation funder would receive under the funding agreement, upon a successful outcome;
  - (ii) the likely value of any award;
  - (iii) the value of a litigation funder's financial contribution and the proportion funded by the litigation funder of the claimant's overall costs, and
  - (iv) the proportion of any award that the claimant and intended beneficiaries stand to receive;
- (e) to impose any penalty the court or administrative authority deems appropriate to ensure compliance with this Directive;
- (f) to consult or seek expertise from persons with appropriate knowledge to assist in the performance of the court's or administrative authority's assessment powers, including from any suitably qualified expert or from supervisory authorities.

### *Article 17*

#### *Responsibility for adverse costs*

1. Where the claimant party has insufficient resources to meet adverse costs, Member States shall ensure that courts or administrative authorities are empowered to make cost orders against litigation funders, whether jointly or severally with claimants, following an unsuccessful outcome in proceedings. In such a case, courts or administrative authorities may require litigation funders to pay any appropriate adverse costs, having regard to:
  - (a) the value and proportion of any award that the litigation funder would have received had the claim been successful;
  - (b) the extent to which any costs that are not paid by a litigation funder would instead fall on a defendant, the claimant, or any other intended beneficiaries.
  - (c) the conduct of the litigation funder throughout the proceedings and, in particular, its compliance with this Directive and whether its conduct has contributed to the

- overall cost of the proceedings; and
- (d) the value of the litigation funder's initial investment.

## ***Chapter VI***

### ***Final provisions***

#### ***Article 18***

##### ***Sanctions***

1. Member States shall lay down the rules on sanctions applicable to infringements of national provisions adopted pursuant to this Directive and shall take all measures necessary to ensure that they are implemented. The sanctions provided for shall be effective, proportionate and dissuasive. Member States shall, [by .../without delay], notify the Commission of those rules and of those measures and shall notify it [, without delay,] of any subsequent amendment affecting them.
2. Supervisory authorities may in particular impose proportionate fines calculated on the basis of an undertaking's turnover, temporarily or indefinitely withdraw the authorisation to operate, and other appropriate administrative sanctions.

#### ***Article 19***

##### ***Review***

1. No later than [...] years after the date of application of this Directive], the Commission shall carry out an evaluation of this Directive and present a report on the main findings to the European Parliament, the Council and the European Economic and Social Committee. The evaluation shall be conducted in accordance with the Commission's better regulation guidelines. In the report, the Commission shall in particular assess the effectiveness of the Directive, with particular regard to the level of fees or interests diverted from claimants' awards (including to intended beneficiaries) to litigation funders and the impact litigation funders have on the level of dispute resolution activity.
2. Member States shall provide the Commission, for the first time by [ ] years after the date of application of this Directive and annually thereafter, with the following information necessary for the preparation of the report referred to in paragraph 1:
  - (a) the identity, number and type of entities that are recognised as authorised litigation funders;
  - (b) any changes to that list and the reasons therefor;
  - (c) the number and type of proceedings that are funded in whole or in part by a litigation funder;
  - (d) the outcomes of those proceedings in terms of the amounts earned by litigation funders in comparison to the awards delivered to claimants and intended beneficiaries.

#### ***Article 20***

##### ***Transposition***

1. Member States shall adopt and publish, by XXXX, the laws, regulations and administrative provisions necessary to comply with this Directive. They shall immediately inform the Commission thereof.

They shall apply those measures from XXXX.

When Member States adopt those measures, they shall contain a reference to this Directive or shall be accompanied by such a reference on the occasion of their official publication. The methods of making such a reference shall be laid down by Member States.

2. Member States shall communicate to the Commission the text of the measures of national law which they adopt in the field covered by this Directive.

#### **Article 21**

##### *Entry into force*

This Directive shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

#### **Article 22**

##### *Addressees*

This Directive is addressed to the Member States.

## EXPLANATORY STATEMENT

*“It is incredibly frustrating when a person wins a case, only to walk away almost empty-handed because the money has been soaked up by unfair legal fees. [...] The days of some litigation funders charging such excessive fees need to come to an end.”* Attorney-General Martin Pakula from the Australian Labour Party in 2017 when he announced the review of the existing legal framework that covers the activities of litigation funders in legal proceedings.

To spare European citizens from the unjust legal outcomes that thousands of Australians – and others around the world – have had to face in recent years, this legislative own-initiative report aims to regulate third party litigation funding (TPLF) before it gains traction in all of our Member States. This particular type of commercial practice can be best understood as a business model whereby an investor pays for the litigation costs on behalf of a claimant or a representative of a group of claimants, in exchange for an agreed fee in the event that the legal proceeding is successful. The fee is usually a percentage of the award made or the settlement secured in favour of the funded claimant party.<sup>1</sup> Litigation funders themselves are not a party to the legal proceeding and have only an economic interest, not a legal interest in it.

TPLF originated in Australia but has since expanded into a global industry worth billions of Euros, which is today present in many jurisdictions including the USA, Canada, the United Kingdom and more recently, the EU. As confirmed by the European Parliamentary Research Service, TPLF in the EU is in a state of rapid growth.<sup>2</sup> Litigation funders are mainly interested in high value cases but do also invest in arbitration and insolvency cases. Investments in single cases are the norm although the so-called 'portfolio-funding' is becoming increasingly widespread over the last years.<sup>3</sup> This model means that the litigation funder finances a bundle of claims under the same funding agreement in order to spread the investment risk. Together with the growing number of litigation funders in general and portfolio-funding investments in particular, one can also observe an increased cooperation of litigation funders with qualified entities, law firms as well as aggregators such as claims-collection or award-distribution-platforms combined with aggressive advertising.

Proponents of TPLF often argue that it improves access to justice and that it discourages wrongdoings. According to them, justice becomes more affordable to everyone by litigation funders bearing the risks and costs. TPLF would also help to close the gap in financial resources by weakening the defendant's ability to defeat the case through superior economic power. Eventually, proponents argue that it serves as a vehicle for the pursuit of low value claims, which would otherwise not be pursued.

However, the main argument for TPLF, the improvement of 'access to justice', is not borne out by experience. Instead, TPLF is a profit-making enterprise, in which justice for the claimant may or may not be a by-product. In its report, the Australian Parliament observed that litigation funders mainly invest in class action lawsuits on behalf of investors and

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<sup>1</sup> See for instance Bentham Europe Limited (14 October 2014), Submission to the Ministry of Security and Justice, Dutch Draft Bill on Redress of Mass Damages in a Collective Action, par. 2.10 on page 4 (<https://www.internetconsultatie.nl/motiedijksma/reactie/7bf391e6-0b57-44c3-a650-b9797efb4c29>).

<sup>2</sup> See chapter 2.1 of the European added value assessment (p. 3-10) as well as chapter 2.1 / 2.2 of the annexed study p.49-54.

<sup>3</sup> EPRS Study (2021): Responsible litigation funding. State of play on the EU private litigation funding landscape and on the current EU rules applicable to private litigation funding, p. 28 -29.

shareholders.<sup>4</sup> Claims from employees or product liability claims from consumers are, on the other hand, regularly assessed as too risky, impossible to settle fast or not profitable enough. If litigation funders do invest in such cases of ordinary citizens, they are regularly demanding excessive returns. In Europe, rates of returns for litigation funders may be up to 300% or even 3.000%<sup>5</sup>. There are also various examples of litigation funders assuming effective control of litigation to further maximise their returns or to push for a settlement, without regard to the fairness of the financial outcome for the funded claimant party. In such cases, a losing defendant effectively transfers wealth to an unharmed investor, while claimants who have suffered a harm risk receiving little or no redress.

This report seeks to address these problems by proposing a new regulatory framework. Its provisions shall safeguard the integrity of our justice system by effectively protecting European citizens from financial exploitation by litigation funders. Ensuring that victims that suffer harm receive adequate compensation is key for the Rapporteur. With this report, he wants to create a rulebook for a proactive regulation of TPLF, which will help to avoid the problems faced in third countries and which are now starting to occur also in the EU. The Rapporteur regards the following points as necessities for the upcoming legislation towards litigation litigation funders:

- An authorization system managed by national supervisory authorities
- Capital adequacy requirements as well as an obligation to pay adverse costs
- Fiduciary relationship towards claimants
- Disclosure of TPLF agreement towards the court, the claimants and the defendant
- Strong safeguards against conflicts of interest
- A cap for fees to guarantee fair and proportionate returns for claimants
- Prohibition to take control over the proceedings or withdraw without clear justification

Some efforts have already been made to regulate TPLF. Recognizing the problems that stem from TPLF, Australia has recently introduced a requirement for litigation funders to hold an Australian financial services license. It has also completed a parliamentary inquiry into the regulation of TPLF in collective redress proceedings, in which some litigation funders have indicated that they would support further regulation in order to improve transparency and confidence in the system.<sup>6</sup> Pending legislation also exists in Canada, in the province of Ontario, where a bill reforming the collective redress regime contains provisions on TPLF.

The Commission suggested in its 2013 Collective Redress Recommendations several provisions to underscore the need to regulate TPLF, for instance (a) the prohibition on litigation funders from charging excessive interest on the funds provided to fund the claim (Rec 16(c)) and (b) the prohibition on litigation funders from basing their remuneration or interest on the

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<sup>4</sup> See Australian Law Reform Commission (2019): An Inquiry into Class Action Proceedings and Third-Party Litigation Litigation funders, p 34.

<sup>5</sup> See Bentham(2014): Submission to the Ministry of Security and Justice. Dutch Draft Bill on Redress of Mass Damages in a Collective Action, par. 2.15 on page 5 as well as 1266/7/7/16 Walter Hugh Merricks CBE v MasterCard Incorporated and Others – Judgment (CPO Application) [2017] CAT 16 | 21 Jul 2017 in section 99 and 100 on page 37 and 38. The funding agreement for the case Walter Hugh Merricks CBE versus Mastercard foresees as a total investment return “the greater of (i) £135,000,000; or (ii) 30% of the Undistributed Proceeds up to £1 billion, plus 20% of the Undistributed Proceeds in excess of £1 billion.

<sup>6</sup> Australian Parliamentary Joint Committee on Corporations and Financial Services, Litigation funding and the regulation of the class action industry, 22 December 2020, par. 16.18 on p 293.

settlement amount awarded except where the funding agreement is regulated by a public authority (Rec 32).

This Recommendation only addressed TPLF safeguards for collective cases (and not the general regulation of TPLF, as it is required). Nevertheless, it is noteworthy that when the Commission reviewed Member State compliance with the Recommendation in 2018<sup>7</sup> ('Commission 2018 Report'), it noted:

- “On this point [adoption of TPLF safeguards], the Recommendation has not been implemented in any of the Member States. None of them have regulated third party financing, let alone in accordance with the Recommendation.” (page 9)
- Only Slovenia “is the exception to this general situation, as (...) private third party funding is regulated in accordance with the principles set out in the Recommendation.” The report goes on to state that: “This general lack of the implementation means that unregulated and uncontrolled third party financing can proliferate without legal constraints, creating potential incentives for litigation in certain Member States.”

The EU’s 2018 Directive on representative actions for consumers also contains some provisions on TPLF in the context of collective action litigation that seek to address transparency as to sources of funds and conflicts of interest like Recital 52 and Art 10 (2a) (“unduly influence(d)”, “does not divert”) and Art 4 (1e) (“prevent influence”).

This report however argues - based on the arguments outlined above - that those provisions are not sufficient, and in any case only apply to a certain sub-set of disputes.

Soft law approaches have also proved not to be effective<sup>8</sup>. The only self-regulatory code (i.e. soft law) in Europe is the Association of Litigation Funders (ALF) in the UK. However, only 12 of the 80 or more litigation funders operating in Europe are a member. Moreover, the sanctions in the code are not effective. When the code is for example violated the funder may face a fine of up to GBP 500 (the equivalent of approximately EUR 570) or the exclusion from the organisation. After exclusion, it can continue any actions it pleases.

Furthermore, allowing Member States to regulate separate without coordination from the EU will lead to the proliferation of divergent outcomes, which will create inconsistent safeguards for the EU citizens across the internal market. As the Commission 2018 Report notes (on page 10): “(...) there will always be a possibility for fund providers based in one Member State to avoid stringent national rules by seeking to fund collective actions in another EU Member State, where collective redress mechanisms are available and private third party funding remains unregulated.”

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<sup>7</sup> Report from the Commission to the European Parliament, the Council and the European Economic and Social Committee on the implementation of the Commission Recommendation of 11 June 2013 on common principles for injunctive and compensatory collective redress mechanisms in the Member States concerning violation of rights granted under Union Law (2013/396/EU). Brussels, 25 01 2018, COM(2018) 40 final.

<sup>8</sup> See chapter XX of the annexed study - UK example (describe):  
[https://www.europarl.europa.eu/RegData/etudes/STUD/2021/662612/EPRS\\_STU\(2021\)662612\\_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/STUD/2021/662612/EPRS_STU(2021)662612_EN.pdf)

As such, this report argues for the expansion of the existing regulatory framework by a new Directive, establishing minimum safeguards across the EU, while respecting Member States' wishes not to permit TPLF at all if it is incompatible with their domestic systems.

The Rapporteur rejects the view of some policy makers that the EU is immune to TPLF-related problems. The main ingredient for the discussed problems is the same as in Australia, Canada, the USA or Europe: actors seeking for profit maximization at the expense of claimants. Only strong legal safeguards combined with sound knowledge of the use of TPLF will prevent us from scenarios that occurred in other parts of the world. The European Union should use this matter to demonstrate to its citizens that the European Institutions are not only able to find solutions after a crisis has done already severe damage but that they can also act pre-emptively, at an early stage to stop the further erosion of our justice system and to guarantee adequate compensation and protection for our citizens.