25/7/2018

Australian Law Reform Commission
GPO Box 3708
**Sydney NSW 2001**

By email: class-actions@alrc.com.au

Dear Sir/Madam,

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

As an academic at the University of Sydney that has empirically studied aspects of the Australian class actions regime and as someone who has also participated in shareholder class actions (SCAs) as a lead applicant, I am grateful for the opportunity to make a submission to the ALRC's Inquiry into Class Action Proceedings and Third Party Litigation Funders.

My experience and research has demonstrated to me there are some core fundamentals at work in the Australian class actions regime, the purpose of which is to provide checks and balances against misconduct by large organisations, ensuring that breaches of continuous disclosure do not go unpunished simply due to the distributed nature of the harm and the significant cost burden of litigation. Any proposed reform should do everything possible to preserve and enhance the fairness and efficiency of the market, namely:

(a) improving access to justice;
(b) driving down the costs of litigation and increasing returns to group members; and
(c) ensuring courts retain adequate powers to manage issues surrounding class actions so as to preserve confidence in the regime.

The Discussion Paper covers a variety of issues that are worth better understanding. On the whole, my research suggests that Australian class actions have been effective in providing an efficient mechanism to challenge misconduct, exact appropriate redress and enforce a better level of compliance and accountability for large organisations. This is in stark contrast to jurisdictions such as the US, where far more numerous, smaller SCA's are undertaken. Therefore, while it is prudent to look for improvements all the time, such a quest does not necessarily require overhaul.

In my brief submission below, I will highlight a few particular topics covered in the Discussion Paper to support that view and, in turn, reinforce the importance of the key areas I have touched on above.

I hope the Commission considers my insights of some utility as it goes about this work.

## SUBMISSION

A reasonable depth of literature now exists on the class actions regime in Australia and the effectiveness of its operation in achieving the goals of increasing access to justice and improving corporate conduct and accountability.

The 2014 Productivity Commission's Access to Justice Arrangements Report has provided extensive insight into many of the important issues canvassed in the ALRC's current work. The Law Institute of Victoria has also contributed to the body of understanding around contentious issues such as allowing contingency fees, as has the recent Victorian Law Reform Commission inquiry, and there is academic literature from Australia and across the globe that now includes substantial empirical data on the impact the introduction of an effective class actions regime has had here in addressing issues of improving access to justice and improving accountability for corporate misconduct.

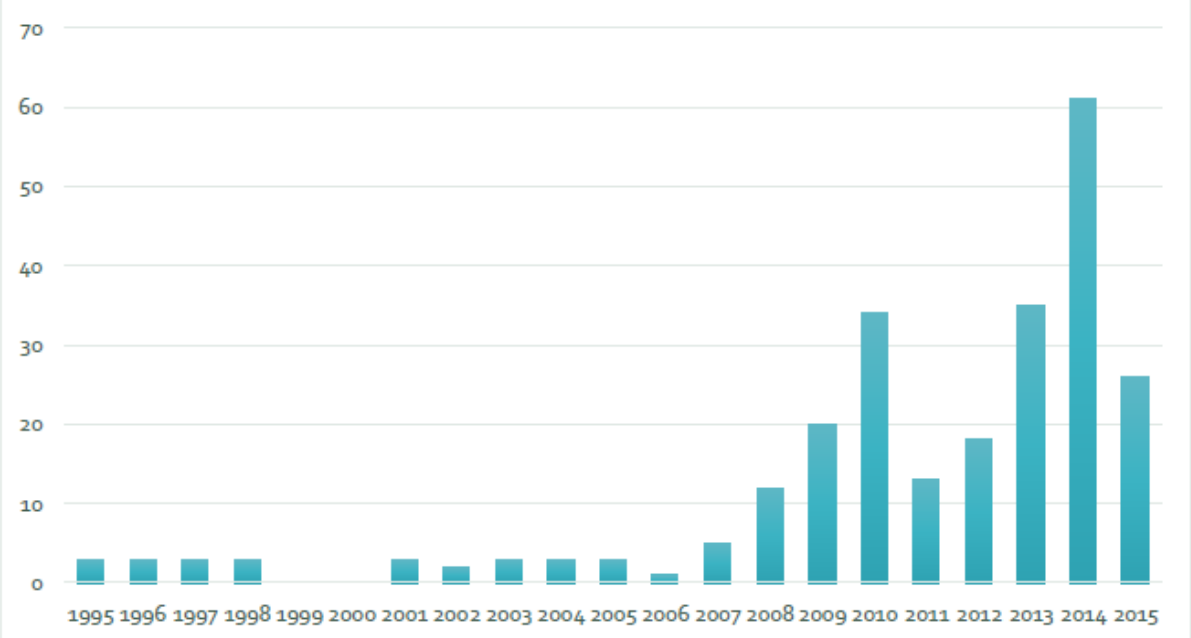
To that extent, it is fortunate that there is already some excellent material in existence that has examined this area of interest, and it is from much of that literature, in addition to my own research, that I make the below comments.

### Continuous Disclosure Obligations

It is a testament to our existing class actions regime that it has always been flexible and adaptable, however there is an urgent need to ensure that we continue to use opportunities for law reform to increase access to justice, not restrict it.

Ensuring the provision of access to justice is at the core of the Australian regime, however the proposal to decrease continuous disclosure obligations for ASX-listed companies would in fact threaten the integrity of the market and counteract the significant progress the regime has made over the course of the past 26 years. It is essential to protect and maintain the laws currently in place surrounding proper disclosures from large companies in order to continue to effectively deal with corporate misconduct in Australia, minimise the potential for insiders to profit and hold wrongdoers to account. If anything, the recent findings of the Banking and Financial Services Royal Commission have demonstrated that shareholders around the country would be better protected if transparency obligations were increased. Indeed, the number of ASX Aware letters (aka speeding tickets) has grown in recent years, as shown in Figure 1 below.

**Figure 1: ASX Aware Letters by Year (to June 2015)**



This stands in stark contrast to the relatively stable level of SCAs shown in Figure 2. This can be attributed to the cost recovery regime employed in Australia. Further, the returns observed around these two events presented in Figure 3 reinforces the role of the two disciplinary measures, with SCA's recording reductions of around 40% prior to announcement, whilst Aware letters are typically preceded by 40% increases in share price.

**Figure 2: Shareholder Class Actions (to December 2014)**

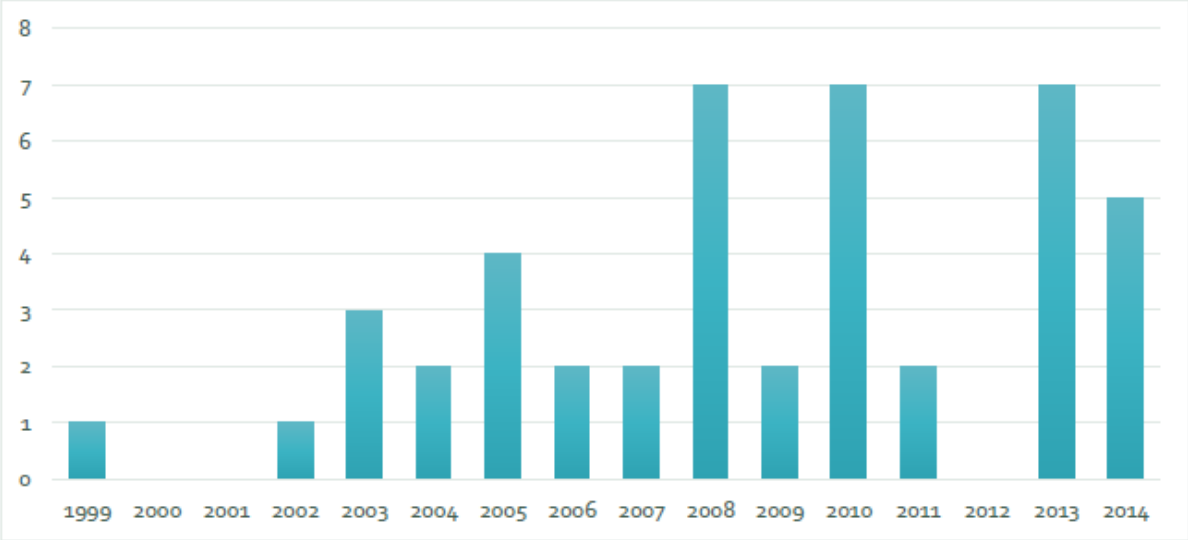
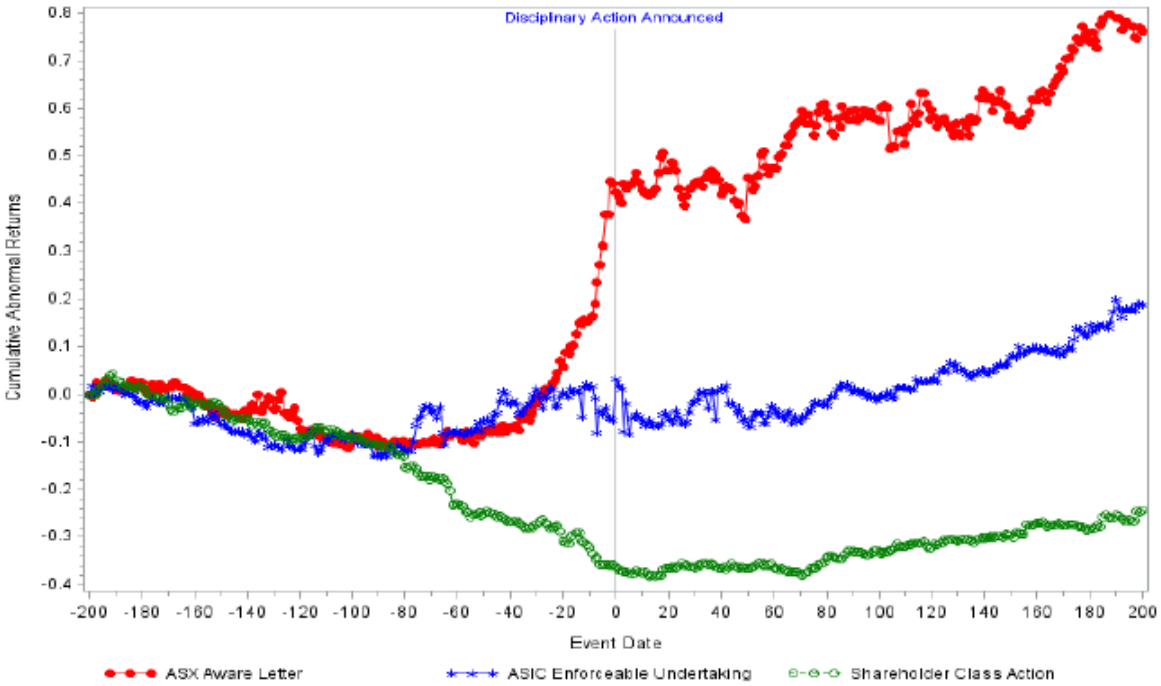



**Figure 3: Returns Around Disciplinary Actions**




Shareholder class actions also result in quantifiable changes at the firm level, with Table 1 documenting marked increases in spending on audit fees after SCAs, as well as a move towards using reputable "Big 4" accounting firms, increasing from 79% of firms to 92%. SCA firms also see improvements in audit opinion, indicating firms are more frequently issued an unqualified report.

**Table 1: Accounting Metrics Surrounding Shareholder Class Actions**

| | Event Period | Audit Fees | Other Services Fees | Taxation Service | Big 4 Firm | Audit Opinion |
|---|---|---|---|---|---|---|
| Aware | -2 | $878,186 | $362,182 | $78,762 | 0.57 | 1.08 |
| | -1 | $993,530 | $361,965 | $134,890 | 0.57 | 1.11 |
| | 0 | $1,106,521 | $224,322 | $173,338 | 0.57 | 1.22 |
| | 1 | $1,131,581 | $151,600 | $159,510 | 0.64 | 1.15 |
| SCA | -2 | $3,097,028 | $1,481,524 | $138,700 | 0.79 | 1.05 |
| | -1 | $2,858,935 | $1,467,755 | $242,033 | 0.79 | 1.16 |
| | 0 | $3,690,149 | $690,536 | $414,752 | 0.86 | 1.10 |
| | 1 | $3,187,130 | $737,471 | $495,219 | 0.92 | 1.21 |

## Contingency Fees

As the Commission progresses its inquiry into SCAs, some have expressed concerns that allowing contingency fees could flood our system with unmeritorious and frivolous litigation; that lawyers might not fully and appropriately consider the merits of a case and, instead, prioritise the financial incentives of proceeding with speculative claims.

I believe that lifting the ban on contingency fees would have the opposite effect; in fact, promoting access to justice by increasing the number of smaller worthy claims that may be heard which lawyers would otherwise be prevented from pursuing should the estimated return fail to equate to sufficiently more than the projected costs and make the case financially viable. Without such remedy, we exist in a system where only large claims can be made, providing profits to large, listed litigation funders and potentially stifling competition in this area.

The existing requirements of our regime mean that regardless of whether billing is implemented under a conditional or contingent arrangement, lawyers operating on a ‘no win no fee’ basis already have sufficient incentive to proceed only with cases of reasonable merit as they are at risk of not recovering their fees if they are unsuccessful. Additional disincentive to litigate claims without reasonable prospects of success comes from our effective laws regarding adverse costs. Both claimants and lawyers are dissuaded from pursuing frivolous litigation at the risk of being ordered to pay the other side’s legal fees and bearing the entire cost of the proceedings. Such laws have been demonstrated to sufficiently deter the commencement of high-risk speculative claims, particularly in Canada and the United Kingdom. For this reason, evidence against allowing contingency fees based on cases in the United States, where they do not enforce adverse costs, is misguided.

Where concerns have been voiced that the availability of contingency fees could encourage lawyers to prioritise their own financial gain, the Law Institute of Victoria identifies that this model is readily available to litigation funders who have no obligation to meet the same ethical and professional requirements as Australian legal practitioners.

Not only would contingency fees allow claimants to benefit from higher returns, but there would also be increased certainty at the outset of a matter surrounding the potential total cost of litigating the claim. Lawyers could assure their clients that their fees would be proportional to the final recovery and do not run the risk of recovering insufficient funds to pay legal bills charged at an hourly rate.

Ultimately, confidence in the class action regime depends on the integrity of the mechanisms utilised to implement it. The notion that the interests and incentives of lawyers would conflict with their clients exclusively under a contingency fee regime seems inherently inaccurate.

In my view, the availability of contingency fees would see lawyers and clients share the common incentive to resolve the dispute in the shortest possible time and achieve the highest possible recovery.

Please do not hesitate to contact me if I can further assist with the Commission's important work.

Sincerely,

Dr Sean Foley
Senior Lecturer,
Finance Discipline, University of Sydney