Australian Law Reform Commission, *Class Action Proceedings and Third-Party Litigation Funding,* Discussion Paper No 85 (2018)

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Submissions of Johnson Winter & Slattery in respect of contingency fees

1 Introduction

These are submissions and comments on the Discussion Paper made on behalf of Johnson Winter & Slattery (**JWS**)[1] in respect of **Section 5 Commission Rates and Legal Fees[2].** The views are those of JWS in its own right and should not be attributed to the firm's clients (past or present) or any third-party litigation funder.

2 Executive summary

2.1 While JWS agrees that solicitors should be permitted to enter into contingency fee agreements in class action proceedings, JWS does not support the adoption of the contingency fee model as outlined in Proposals 5-1, 5-2 and 5-3 ("Model").

2.2 JWS respectfully submits that the Model will not permit most Australian law firms to finance long and hard-fought class proceedings on a contingency fee basis. The proposed statutory interventions, if implemented, are likely to be a barrier to entry for most law firms acting for plaintiff representatives on a contingency fee basis other than a few established larger plaintiff firms.

(a) A statutory requirement for solicitors to indemnify a representative plaintiff against adverse costs is likely to be prohibitive for most law firms if this requirement requires law firms to hold cash or set aside capital as security for adverse costs, or if there is further statutory intervention in the form of capital adequacy requirements for law firms wishing to enter into contingency fee arrangements.

(b) An express statutory power to reject, vary or set contingency fees at any stage of the class action proceedings creates financial uncertainty for law firms. The deferral of the final determination of contingency fees arrangements to the settlement approval stage or after judgment is likely to be a significant commercial risk for law

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[1] **Attachment 1** briefly list JWS's experience in the both plaintiff and defence work in class actions.

[2] **Proposal 5–1** Confined to solicitors acting for the representative plaintiff in class action proceedings, statutes regulating the legal profession should permit solicitors to enter into contingency fee agreements.
This would allow class action solicitors to receive a proportion of the sum recovered at settlement or after trial to cover fees and disbursements, and to reward risk. The following limitations should apply:
- an action that is funded through a contingency fee agreement cannot also be directly funded by a litigation funder or another funding entity which is also charging on a contingent basis;
- a contingency fee cannot be recovered in addition to professional fees for legal services charged on a time-cost basis; and
- under a contingency fee agreement, solicitors must advance the cost of disbursements and indemnify the representative class member against an adverse costs order.

Proposal 5–2 Part IVA of the *Federal Court of Australia Act 1976* (Cth) should be amended to provide that contingency fee agreements in class action proceedings are permitted only with leave of the Court.
Proposal 5–3 The Federal Court should be given an express statutory power in Part IVA of the *Federal Court of Australia Act 1976* (Cth) to reject, vary or set the commission rate in third-party litigation funding agreements.
If Proposal 5–2 is adopted, this power should also apply to contingency fee agreements.

firms and deter most law firms from taking on the very cases the introduction of contingency fees are thought to promote namely, smaller matters with higher risk.

(c) *Interventions in the form of statutory caps or statutory maximums for the proportion of contingency fees from any one settlement or judgment fundamentally fails to recognise the much broader factors in play in the funding of a class action on a contingency fee basis than just the "risk/work" of an individual case. A law firm may require a higher return in some cases, even if that case is low risk or less difficult, to allow them to continue to be commercially viable and/or to have sufficient cashflow to fund other cases of a more speculative nature.*

2.3 *The Model is therefore unlikely to "level the playing field" and generate the intended competition in the funding of class actions that could lead to any demonstrable improvement in access to justice. The implementation of the Model will result in Australia's class action regime continuing to be dominated by a few large plaintiff law firms.*

2.4 *JWS submits that flexibility as to the structure of the funding by law firms of individual cases and certainty as to the contingency fee arrangements are critical to the implementation of a successful contingency fee model.*

2.5 *Class actions are closely scrutinised and controlled under existing statutory powers in Part IVA of the Federal Court of Australia Act 1976 (Cth). The Court would continue to exert strict supervisory control through an approval process at the beginning of the class action proceedings (for the grant of leave to permit the contingency fee agreement in the proceedings). JWS submits that it is at this point that the law firm should be required to justify the proposed contingency fee arrangements and that once approved, other than upon an application by the law firm to vary those arrangements in limited circumstances, the Court should not have the power to vary the contingency fee arrangements. The proportionality of the fees as against the return to the class members from a settlement should not be a factor that is taken into account on a settlement approval application when those fees have been earlier approved by the Court and the case has been funded and conducted on that basis.*

3 Submissions

3.1 Goal to increase access to justice

The principal argument for the introduction of contingency fee arrangements is the desirability of redressing a key limitation of the current class action system, or gap in funding services, in respect of medium-sized actions (where the return to the class is between $30 million and $60 million), and to expand the funding market to promote competition and eventually lower commission rates set by litigation funders, creating a more level playing field. The ultimate goal is to increase access to justice including for prospective class members in more risky and difficult cases.

3.2 Creating a level playing field

To create a more level playing field (including as between the law firms), to avoid unfair barriers to entry in the funding market, and to increase access to justice, law firms must be permitted to structure funding arrangements on a case by case basis.

The enormity of the risks involved in funding on a contingency fee basis is widely acknowledged. Leading academics in class actions, Professors Vince Morabito and Vicki Waye have stated that "…*there would be few Australian law firms that would be in a position to not only finance long and*

hard-fought class proceedings on a contingency basis but also to bear the potential risk of adverse costs"[3].

Ben Slade from Maurice Blackburn, regarded as Australia's most successful plaintiff law firm, has stated that there are now fewer plaintiff firms to take on big cases since major competitor Slater & Gordon had suffered financial blows. "*All the other firms are very small and haven't got the resources you need to take on big cases. There are more corporate wrongdoings happening than Maurice Blackburn can address*", he said[4]. Mr Slade also stated that Maurice Blackburn had become much more sophisticated in the way it ran class action cases. "*It took us about 10 years to accept that we had to meet the defendant's resources if we were going to succeed. Litigation funding has helped enormously because taking on the cashflow impact of a litigation is frightening*," he said[5].

Unlike third party litigation funders, the core business of Australian law firms is the provision of legal services, not litigation funding. Most law firms would simply not be in a financial position to fund long and hard-fought class actions and assume the risk of adverse costs. The cashflow impact and potential risks of not recovering a substantial portion of their professional fees at settlement or from a judgment may be prohibitive for most law firms. Law firms operating as partnership may need to use profits to build up the necessary capital to fund class actions on a contingency fee basis. This may expose the partnership to further risk if they are required to pay (high personal) tax on the profits before achieving any return on the investment in the class action.

However, law firms could be in a position to take on cases on a contingency fee basis if they could structure funding on a case by case basis (unfettered by statutory caps or maximums) and had certainty as to the fundamental financial basis upon which they funded and conducted the case from the outset.

Each class action is different. It will have its own particular risks and issues. However, medium-sized class actions can generate the same or similar levels of legal costs and disbursements as the larger class actions especially where the litigation is highly complex and involves multiple respondents or for a variety of other reasons (e.g. the vigorous defence of the proceedings by deep pocketed respondents). In some cases where the proportion returned to class members is less than 50%, the settlement may still be fair and reasonable and in the best interests of class members. The examples discussed at [5.56] to [5.62] of the Discussion Paper clearly demonstrate this[6].

As noted by the Productivity Commission, "*law firms will have a combination of income sources, encompassing both normal or damages-based billing, across a range of matters including complex litigation and simple transactions*". In order to determine whether it can take on a class action on a contingency fee basis, and if so, how to structure the funding of the case, the law firm will be required not only to assess the 'case specific risks' including the difficulty of the matter, likelihood of success and the costs of bringing the action, but also the 'firm specific risks' such as the firm's current income sources and cashflow, capital resources, availability of third party litigation funding and its exposure in other class actions (or other engagements). A law firm will need to balance all of these factors, and in some

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[3] *Seeing Past the US Bogey—Lessons from Australia on the Funding of Class* Actions, Vince Morabito and Vicki Waye (2017) 36 C.J.Q., Issue 2 at page 226

[4] AFR article *Best Lawyers: defendant lawyers dominate class action list* by Misa Han Apr 7 2017 quoting Ben Slade.

[5] See AFR article *Best Lawyers: defendant lawyers dominate class action list* by Misa Han Apr 7 2017

[6] In *Clarke v Sandhurst Trustees Limited (No 2) [2018]* FCA 511, Lee J approved settlement of an investor claim for the sum of $16.85 million, of which the funder received 30% and solicitors received 31%, leaving group members with only 39% of the final settlement sum. In *Caason Investments Pty Limited v Cao (No 2)* [2018] FCA 527, Murphy J approved a settlement where the solicitors received 43% of the $19.25 million total (inclusive of costs) and the funder received 30% via a common fund—leaving group members with 27% of the final settlement sum.

cases may require a higher return, even if that case is low risk or less difficult, to continue to be commercially viable and/ or to fund other cases of a more speculative nature.

While JWS agrees with the ALRC that the administration of justice would benefit from certainty regarding the scope of the Court's power to reject, vary or reset contingency fees,[7] JWS submits that the reasonableness or otherwise of the proposed contingency fees should be considered by the Court on the application for leave at the outset because this is the basis upon which the case is proposed to be funded and conducted. JWS submits that other than upon an application by the law firm in limited circumstances (e.g. a material change in circumstances such as the introduction of a new cause of action likely to increase the level of difficulty of the case and significantly prolong the litigation), the Court should not have the power to vary the previously approved contingency fee arrangements. The proportionality of the fees as against the return to the class members from a settlement should not be a factor that is taken into account on a settlement approval application when those fees have been previously approved by the Court and have formed the basis upon which the class action has been funded and conducted by the law firm.

The Model appears to contemplate "*After the Event"* insurance (as a means of meeting liability for adverse costs) and does not prohibit moneys being returned to litigation funders from solicitors where the funding (which may include an indemnity for adverse costs) sits behind the solicitor, as opposed to alongside the solicitor.[8] However, JWS submits that solicitors should not be required by statute to indemnify a representative plaintiff against adverse costs if this requirement requires law firms to hold cash or set aside capital as security for adverse costs, or if there is further statutory intervention in the form of capital adequacy requirements for law firms wishing to enter into contingency fee arrangements. Most law firms would simply not be able to meet those requirements (in addition to the other cashflow impacts of funding the conduct of the case). Significant cash or capital may be required to be set aside by law firms for long periods to cover adverse cost exposure for each case[9].

4 Concluding remarks

JWS favours the lifting of the ban on contingency fees for law firms acting for plaintiff representatives in class action proceedings but submits that allowing law firms flexibility in how they structure the funding of individual cases and certainty as to the contingency fee arrangements are key to the implementation of a successful contingency fee model and achieving the desired result of increasing access to justice.

Dated 27 July 2018

[redacted]

[7] [5.52]
[8] [5.37]
[9] Adverse costs exposure even in medium-sized class actions could be in the order of $2-5 million.