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By email only (class-actions@alrc.gov.au)

29 July 2018

Dear Ms. McLean,

Submission to the Australian Law Reform Commission Discussion Paper 'Inquiry into Class Action Proceedings and Third Party Litigation Funders'

This submission is made by Therium Australia Limited pursuant to the invitation for responses extended by the Australian Law Reform Commission ('ALRC') with respect to its Discussion Paper – 'Inquiry into Class Action Proceedings and Third-Party Litigation Funders' (June 2018).

Therium Australia Limited is part of the Therium group of companies ('Therium'). Therium is one of the UK's leading funders of litigation and arbitration, active in England and Wales and internationally since 2009. Over that period, Therium has funded claims with a combined value comfortably in excess of GBP15bn. Many of those claims are group or multi-claimant 'class' claims. Therium is particularly active in the Australian class-action market, where Therium is funding four such claims, including the approved class in *GetSwift*.

Section 1- Introduction to the Inquiry

Proposal 1-1

The ALRC recommends that the Australian government commissions a review of the 'legal and economic impacts' of the continuous disclosure obligations of Australian listed entities.

As an active Third Party Funder ('TPF') in the Australian securities class action area[1], Therium would first note that such a review of Australia's continuous disclosure laws does not appear to have been raised or suggested in the Terms of Reference provided to the ALRC by former Attorney-General, The Honorable Mr. Brandis.

Be that as it may, a theoretical argument for a review of Australia's continuous disclosure regime in the context of the ALRC's review of class actions and litigation might be that unmeritorious securities class actions have proceeded (or are presently proceeding) under the current continuous disclosure laws and thus certain defendants have been, or are being, "greenmailed" into settling them. However, no such argument has been raised, or evidence cited, by the ALRC suggesting that this is the case.

Therium has first-hand knowledge of the time, effort and cost involved in both investigating and then funding a securities class action. It has only agreed to fund class action claims after undertaking very careful legal and economic analysis of the claims supported by professional and specialist advice.

Furthermore, Therium would point to the distinct and important difference between Australia's class action system and that pertaining in the United States. In Australia, the imposition of adverse costs orders against unmeritorious representative parties acts as a powerful disincentive to the commencement of spurious class action claims; there is no such 'costs shifting' regime in the U.S., something the U.S. Chamber Institute for Legal Reform consistently forgets.

Given the own costs and adverse costs involved in funding a securities class action, it seems counterintuitive to suggest that unmeritorious cases have been or are currently being pursued. Whether they fall upon a representative party or a litigation funder, the cost consequences of such an action failing is a powerful deterrent to the bringing of spurious claims. Moreover, since such actions are typically defended for D&O insurers, one might imagine that those defendants would comfortably be able to fight them to trial if they were unmeritorious. Yet, as the Discussion Paper notes, in the context of shareholder actions, no claims have resulted in concluding decisions of the Federal Court and 64% of all shareholder actions settle, and across class actions generally, 79% of such claims settle in Federal Court as against 43% of unfunded claims.

Data which would indicate that Australian corporations are facing more class action litigation has been used as the basis for the proposition that

[1] Therium is funding the shareholder class actions presently underway against Spotless Group Holdings Ltd, Commonwealth Bank of Australia Ltd, GetSwift Ltd and AMP Ltd.

Australian companies are too exposed to the threat of class actions, or that these cases are too easy to pursue. However, Therium's position is that a more respectable interpretation of this data is that increasingly Australian listed companies, for whatever reason, are breaching the relevant continuous disclosure laws; one only needs look to the conduct of the Royal Commission into Banking and Financial Services presently underway to find that instances of corporate misconduct abound.

Further, and contrary to hyperbolic speculation from some quarters, the prospects of an Australian listed entity facing such a claim are small. As at April 2018, there were around 2,400 listed companies in Australia[2]. Only a very small fraction of them, well less than 1%, have faced such claims. That is worth comparing with the U.K. where there have been very few instances of 'continuous disclosure' claims against listed entities brought by shareholder under section 90 of the Financial Services and Markets Act, with the only reported case progressing to a conclusion being an action against RBS which settled in circumstances where the defendant's costs exceeded GBP100m. In those circumstances, whilst the number of claims are small, it does seem that Australia strikes a more appropriate balance between the rights of shareholders and corporates than currently prevails in the U.K.

It goes without saying that financial market investors, as well as consumers, should be protected from law-breaking directors and that the market's integrity must be maintained. Measures taken in the United Kingdom and across Europe in recent years have been enacted to this end[3]. The private enforcement of the rights of consumers and shareholders including via class action litigation is a growing global trend. Indeed Therium is aware that Australia's own corporate regulator, the ASIC, has recently conceded as much, endorsing both class actions and the involvement of the litigation funding industry in them.

In summary, the contention that Australia's continuous disclosure laws should be reviewed – and potentially watered down due to the prevalence of class action litigation if that is the inferred solution – is, with the greatest respect, a flawed one. In an environment where Australian individuals collectively have a significant portion of their wealth invested in the equity markets through superannuation funds, such a dramatic move is surely ill-advised and may ultimately have unintended consequences.

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[2] Source: https://www.asxlistedcompanies.com/

[3] See for example the establishment of a class action regime introduced in the UK on 1 October 2015 by the Consumer Rights Act 2015 (the CRA), which facilitates collective proceedings in the Competition Appeal Tribunal (the CAT) for breaches of competition law.

Finally, the contention that companies are facing increases to their insurance premiums payable due to the prevalence of class action litigation seems contrived. It may be that such premiums have historically been under-priced by the insurance industry, or that in 'repricing' this product insurers are seeking to exploit or profit from current market conditions. On this point also, where a listed entity enjoys the privilege of access to the capital markets, surely it is incumbent upon it to either hold capital or pay for insurance coverage that is sufficient to provide redress when it has acted wrongly to the detriment of its stakeholders.

To take away the rights of shareholders and consumers to seek redress for wrongs perpetrated by big business would be in contrast and against the tide of worldwide efforts to enhance such rights and avenues of redress.

Section 3 – Regulating Litigation Funders

Proposal 3-1

This Proposal, provided under the heading 'Regulating Litigation Funders', states that the *Corporations Act 2001* (Cth) (Corporations Act) should be amended so as to require TPFs to both obtain and maintain a 'litigation funding license' to operate in Australia.

Therium notes the reference in the Discussion Paper to the Association of Litigation Funders of England & Wales ('ALF') of which Therium is a founder member and is represented on the Board. Although funder membership of ALF is voluntary, the self-regulation which it promotes by way of the Code of Conduct has been a success: the major funders in the UK (and internationally) are all members of ALF; the Ministry of Justice, whilst monitoring the development of ALF and the market, has seen no reason to consider the introduction of statutory regulation; and there have been no reported issues arising in the U.K market, whether from clients using funding, or lawyers, or the judiciary. Accordingly, whilst Therium steadfastly supports best practice in funding, it cautions against an over-zealous drive towards greater regulation where the grounds for doing so are theoretical and unsupported by empirical evidence.

However, should the Australian government consider regulation to be necessary in the Australian funding market, Therium urges that the following caveats be borne in mind:

Therium, funding in Australia from overseas, would not wish to be placed in a disadvantageous position relative to 'native' funders by the imposition of certain license conditions simply because of the location of their funding operations. Such a development threatens the competition that presently exists within the securities class action marketplace in Australia – as

reflected by decreasing funding commissions in recent cases which could only be viewed as advantageous to shareholder claimants.

Further, the imposition of any license such as an Australian Financial Services Licence ('AFSL') should not impose administrative processes which are overly burdensome and may increase indirectly funding costs.

In relation to the issue of prudential requirements, whilst Therium wholly supports the principle of capital adequacy, it is important that any proposal needs to acknowledge the varied business models run by TPFs, including different fund models. Investors in the larger funders, particularly those operating fund models, include large institutional investors (sovereign wealth funds, pension funds, university superannuation/endowment funds and insurance companies) who will prescribe the structures based on economic considerations, governance requirements, and also complicated multi-national tax considerations at an investor level. Any form of regulation should be structurally agnostic so as not to exclude either directly or indirectly funders with certain structures (particularly those operating internationally) from participating. As to capital adequacy rules, they should not implicitly require a) permanent capital in preference to access to funds for investments, and b) funds that have restrictions from being onshore to come onshore to satisfy these requirements. The ALF Code of Conduct is careful to encompass all funders within the U.K. funding stable, however they are structured, and the Code does not attempt to create a regime similar for instance to banking capital requirements. Litigation funding is about funding going forwards so any capital adequacy test should be at least in part forward looking.

Proposal 3-2

Therium supports all of the proposed license requirements described in this Proposal and makes the following points:

Therium presently has in place arrangements to manage conflicts of interest, adequate risk management systems and a dispute resolution system (LCIA arbitration), and is audited annually by major international accountancy firm.

With respect to the proposed condition of a licensee having 'sufficient resources (including financial, technological and human resources)', Therium agrees, albeit the former is an element of capital adequacy and the latter two resources are essential requirements of any successful funding business *per se* and not apt for regulation.

Section 4 – Conflicts of Interest

Proposal 4-1

If a licensing regime as suggested in Proposal 2-1 is not adopted, then the Proposal that TPFs remain subject to ASIC Regulatory Guide 248 is both uncontroversial and supported by Therium.

Proposal 4-2

If a licensing regime as suggested in Proposal 2-1 is not adopted, then the Proposal that the relevant definitions be included in the definition of a litigation scheme in the *Corporations Regulations* 2001 (Cth) is both uncontroversial and supported by Therium.

Proposal 4-3

Therium would support any specialist accreditation for class action solicitors. Such accreditation through professional development and the like would only enhance the advocacy and effectiveness of such solicitors, to the obvious benefit of both class members and funders involved in the cases.

Proposal 4-4

This proposal, which advocates a prohibition against any solicitors or law firm having a 'financial or other interest' in a TPF where that TPF is funding the same matter(s) in which that solicitor or law firm is acting, is *prima facie* sensible, but needs to be considered in light of the fact that the Discussion Paper advocates the introduction of contingency fees. The prohibition suggested would appear to make sense on the grounds that natural checks and balances in the market are lost where law firms operate their own funding entities; Therium is aware of firms 'double dipping' – accepting funding but then paying themselves to do work and charging to fund that (including a profit element).

Such separation and independence is vital as it enables important, expert oversight of the conduct of the solicitors and law firms on the record, including the costs incurred by way of professional fees plus disbursements. The introduction of contingency fees, it is noted, being the subject of Proposal 5-1 below, would see such important checks and balances potentially disappearing.

Proposal 4-5

Therium supports disclosure of the existence of third party funding in any class action proceedings and notes that such disclosure is in any event

presently required in the Federal Court of Australia via Practice Note GPN-CA. Thus this Proposal only reinforces the *status quo*.

Therium is however generally guarded against disclosure in the following respects:

- in terms of funding terms and commission rates, which it submits should remain confidential for strategic purposes, save where there is multiplicity of actions (on which see further below); and
- in 'any dispute resolution proceeding' including any arbitral proceeding.

With respect to arbitral proceedings, any proposal would appear to be beyond the scope of the present enquiry being undertaken by the ALRC. Therium simply notes for present purposes that it has been suggested, correctly in Therium's view, that the appropriate course of action with respect to disclosure generally is the confidential disclosure of funding terms (and where necessary the funding agreement) to the tribunal or court in 'camera'. This militates against the risk of satellite litigation over funding arrangements, and minimises the risk that the defendants utilise material in order to try and stifle claims – as appeared to be the case with adverse costs in the RBS group action in the High Court in London.

In the spirit of equality of arms, Therium would suggest disclosure in class actions ought to apply to the defendant in circumstances where the defendant is being funded in the proceedings, for instance by an insurer pursuant to any applicable insurance policy.

Proposal 4-6

This Proposal is both uncontroversial and supported by Therium.

Section 5 – Commission Rates and Legal Fees

Proposal 5-1

Therium does not support this Proposal, which would ultimately permit solicitors, confined to those acting for the representative plaintiff in class action proceedings, to enter into contingency fee arrangements.

Therium makes the following points:

Independence and oversight

As noted above, the involvement of a TPF in a funded class action provides important independent oversight of the conduct of, and costs incurred by,

the solicitors on the record. Funders also provide important strategic advice and support. The involvement of funders allows for expert third party management of solicitors' costs, which can be prohibitive in these types of cases, with legal budgets in the range of $5-10 million (and often higher) commonplace.

It would appear that contingency fees may be incompatible with lawyers' ultimate fiduciary duties - the position of the *status quo*, with a tripartite arrangement between client, lawyer and funder, and the lawyer acting as a protective buffer between client and funder, is a more sensible arrangement and serves the interests of the client better.

The UK experience

Secondly, as the ALRC will be aware, contingency fees were introduced into the UK legal services market in 2015. However, contingency fees, or 'Damages Based Agreements', are rarely used. Whilst formally citing the complexity and uncertainty of the regulations governing the regime, the practical realities militate against their use: most law firms are not set up economically for such funding arrangements and Therium's experience in the U.K. is that contingency fees are seen by lawyers as being a way of capturing more upside on top of their fees rather than a way of accepting risk. Therium would expect the introduction of contingency fees in Australia to lead to the development of structures where funding arrangements sit behind lawyers, but with additional layers of upside going to lawyers as well as the funder, which is unlikely to be more efficient. Since lawyers are gatekeepers to cases (particularly if there is accreditation) then it may be hard for shareholders or funders to drive this additional margin down.

The US experience

Experience in the U.S. – Therium has a New York office - shows that shareholder clients see funders as being a cheaper option to contingency fee law firms in securities class actions.

<u>Contingency fee limitations</u>

With respect to the potential limitations placed upon the use of contingency fee arrangements as described in the Proposal, Therium comments as follows:

- with respect to the contingency fee and funder prohibition, restrictions should prevent law firms charging fees <u>and</u> charging contingency fees, rather than there being parallel funding for disbursements and contingency fees for lawyers. The risk here is of lawyers 'double dipping' – winning in both scenarios – rather than risk sharing.

- Therium concurs with the contingency fee and time-cost fee prohibition.

- Therium concurs with the suggestion that solicitors must advance the cost of disbursements and indemnify the representative Party, subject to funding for such costs and indemnities being readily accessible to the relevant law firm through the third party funding and ATE insurance markets respectively.

Proposal 5-2

This Proposal is both uncontroversial and supported by Therium.

Proposal 5-3

This Proposal is that the Federal Court should be given an express power via Part IVA to reject, vary or set the commission rate in third party litigation funding agreements. Therium agrees that the court should be able to approve the commission, but that this should be done as early as possible (as part of multiplicity) to allow investors certainty over the economics of funding - otherwise funders will price for uncertainty. Therium does not consider that there should be any statutory restrictions on the amount or structure of fees or commission rates, since, in Therium's view, this would restrict pricing innovations. TPFs outside Australia often employ multiple underpins to their return which may well give risk to better pricing for shareholders - it allows TPF to manage the downside scenario and therefore soften the upside, leading to greater efficiency in pricing. The clear evidence is that the funding market innovates and is competitive in Australia so any regulation should encourage that organic growth without limitation.

Section 6 - Competing Class Actions

Proposal 6-1

This Proposal is very limiting in the sense that it does not allow for the bringing of 'closed' class actions. Some cases are best run on an open basis (where the economics mean multiple groups are inefficient) but requiring all to be 'open' creates a 'one-size-fits-all' approach which may not necessarily be the most efficient. The closed class should be permitted since it may provide price competition for those opting out of the open class which means that pricing responsibility does not fall solely on the court in multiplicity; for instance, if the price of the open class is too high then members may opt into the closed class which is cheaper.

Proposal 6-2

As Therium does not support all of Proposal 6-1, it would similarly not support this Proposal and the amendment of the Federal Court's Class Action Practice Note.

Section 7 – Settlement Approval and Distribution

Proposal 7-1

Therium broadly supports the proposal that a referee be appointed to assess the reasonableness of costs charged in a class action prior to settlement approval. This was Therium's innovation in some of its Australian class book, for example *Spotless* and *GetSwift* where, based on experiences in the U.K., Therium wanted external checks and balances on costs. Therium considers that this ought to apply even when there are contingency fees, since this reduces the risk of law firms running up costs which the TPF has to fund against a diminishing contingency fee pot.

Whilst such a measure would provide assurance to class members and the funder alike (if applicable), it is difficult to provide a blanket endorsement of such a proposal without further information available as to the extent of the work the costs assessor would undertake, what she would charge for her work, what her work product would be, and who would bear the cost.

Consistent with the above, Therium strongly believes that costs management rigour ought to apply to the defendant too to prevent the adverse costs risk escalating excessively to the tactical advantage of the defendant and the dis-advantage of the claimant class.

Section 8 – Regulatory redress

Proposal 8-1

Therium considers that the mischief behind this proposal might be better met via the private sector or lawyers acting *pro bono*. For instance, at Therium we are rolling out 'Therium Access', supporting access to justice as part of a CSR initiative. It is difficult to legislate across all the funders in an area such as this – fund managers may not have an investor mandate allowing funds to be utilised for this purpose – so we consider universal prescription almost impossible here.

We hope this submission is helpful. Please do not hesitate to contact us should you require any further information or assistance.

Yours sincerely,

[redacted]

Neil Purslow

Director

Therium Australia Limited