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Your reference

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AUM/1217872844.7

30 July 2018

By Email : class-actions@alrc.gov.au

Dear Commission

AUSTRALIAN LAW REFORM COMMISSION'S INQUIRY INTO CLASS ACTION PROCEEDINGS AND THIRD-PARTY LITIGATION FUNDERS - DISCUSSION PAPER 85 ("DISCUSSION PAPER")

We would like to thank the Australian Law Reform Commission (**ALRC**) for the opportunity to comment on and provide this submission in relation to the Discussion Paper.

At the outset, we note our general agreement to the 16 Proposals that the ALRC has outlined in the Discussion Paper. In view of this, and because Australia's Federal Court class action regime has, since its inception, been the subject of much judicial consideration, public consultation and inquiry, this submission does not address every Proposal, nor does it respond to every Question raised in the Discussion Paper.

In this submission, we comment on those topics that are of particular relevance to our firm, which primarily participates in the Australian markets as the provider of commercial law services to both Australian and international clients in multiple jurisdictions around the world, some of which (notably the United States and Canada) have very mature class action and mass torts regimes.

For ease of reference, we adopt the heading and numbering sequence, used in the Discussion Paper.

1 INTRODUCTION TO THE INQUIRY

1.1 We agree with Proposal 1-1 that the Australian Government should commission a review of the legal and economic impact of the continuous disclosure obligations of entities listed on the Australian Stock Exchange and those relating to misleading and deceptive conduct contained in the *Corporations Act 2001 (Cth)* (**Corporations Act**) and the *Australian Securities and Investments Commission Act 2001* (**ASIC Act**) (Cth).

1.2 As noted in the Discussion Paper, "*the majority of funded class actions that were filed in the Federal Court in the last five years were claims by shareholders and investors*", which accounted for 76% of all funded class actions filed in the Federal Court.[1] Whilst we appreciate that class actions account for only a very small percentage of the proceedings filed in the Federal Court of Australia,[2] the large majority of these class actions are shareholder and investor class actions which leads us to the view that the proposed review of the relevant corporations laws is a welcome development.

1.3 We consider that the proposed review would be timely in the current environment where Australia's focus on its regulatory environment is ever increasing and the related obligations on directors and officers expanding.

1.4 We are also mindful of the international experience where we have seen sizeable securities actions run off the back of large regulatory investigations (including, by way of example, anti-corruption investigations). An example is shareholder class actions commenced to recover the loss in a company's share price which has resulted from the adverse publicity surrounding the regulatory investigations where the shareholders allege that the directors and officers of the company have failed in their duties to ensure the company was complying with its legal obligations.

1.5 Not only would the proposed review go a long way towards assisting corporate Australia to understand the exposure arising from a breach of the Corporations Act and ASIC Act, it may identify opportunities to ensure that the laws are streamlined and easily understood.

1.6 Any simplification of the laws and/or their application may also assist in taking away some of the current uncertainty that surrounds the litigation of such matters. For example, if parties are better informed and more certain about how far directors' and officers' obligations extend, the risk of speculative class action claims may be reduced.

3 REGULATING LITIGATION FUNDERS

3.1 Question 3-1 *What should be the minimum requirements for obtaining a litigation funding licence, in terms of character and qualifications of responsible officers?*

3.1.1 We agree with the ALRC's position that "*the skills and knowledge requirements of a litigation funding licensee would cover both the financial skills required to operate a funding business and the legal skills to understand civil litigation, including an understanding of court rules and processes*".[3] The following approach would set minimum requirements which would help ensure that only reputable and appropriately skilled organisations hold a litigation funding licence but at the same time would not be so onerous as to stifle competition by discouraging funders into the Australian market.

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[1] Australian Law Reform Commission, *Class Action Proceedings and Third-Party Litigation Funding*, Discussion Paper No 85 (2018), paragraph 2.12 and table 2.3.

[2] Australian Law Reform Commission, *Class Action Proceedings and Third-Party Litigation Funding*, Discussion Paper No 85 (2018), paragraph 2.5.

[3] Australian Law Reform Commission, *Class Action Proceedings and Third-Party Litigation Funding*, Discussion Paper No 85 (2018), paragraph 3.39

3.1.2 Adapt the Corporations Act character requirements for AFSL holders so that they apply to litigation funders. In particular, any litigation funder applicant must satisfy ASIC that they are of good fame or character (or that its responsible managers are of good fame or character) with ASIC having regard to those matters set out in section 913B of the Corporations Act.

3.1.3 Adapt the qualification requirements set out in Regulatory Guide 105 to confirm organisational competence (i.e. by reference to the knowledge and skills of the company's responsible managers). In particular, the requirements in Regulatory Guide 105 be adapted to ensure that the litigation funder comprises responsible managers who, collectively, have the knowledge and skills to cover both the:

3.1.3.1 financial skills required to operate a funding business; and

3.1.3.2 legal skills to understand civil litigation and the court's rules and procedures.

3.1.4 We agree with the ALRC's recognition that it remains the primary responsibility of the legal practitioner, rather than the litigation funder, to ensure that class action litigation is run competently. We do, however, see an advantage to having - as part of a litigation funder's competency requirement - that one of its responsible managers be legally qualified and maintain a valid Australian practising certificate. It is a reality that less "seasoned" mass torts litigators may need to rely on litigation funders to get a group proceeding off the ground, whilst large plaintiff law firms will seek to self-fund to maximise revenue returns, especially if the mooted introduction of contingency fees was to occur. It is imperative that there is some legal acumen at all levels to ensure that responsible litigation is generated by both lawyers and litigation funders. In addition to ensuring a comfortable level of competency, it would have the added advantage of assisting in the management of conflicts between a litigation funder and the group's solicitors as discussed at chapter 4 of the Discussion Paper. Any such reforms may see the avoidance of situations such as that which arose in *Melbourne City Investments Pty Ltd v Treasury Wine Estates Limited* [2016] FCA 787, which is also something to consider under Conflicts of Interest.

3.1.5 If the requirement to hold a current practising certificate is considered too onerous, another option would be to ensure that at least one responsible manager attends the accreditation course that the ALRC proposes all solicitors practising in class actions attend (see Proposal 4-3).

3.2 **Question 3-2** ***What ongoing financial standards should apply to third party litigation funders? For example, standards could be set in relation to capital adequacy and adequate buffers for cash flow.***

3.2.1 We support the need for greater regulation relating to the capital adequacy of litigation funders. This need will become increasingly important as the number of litigation funders in the Australian market grows.

3.2.2 Although outside the scope of the Discussion Paper, we note that litigation funding is becoming more prevalent in Australia for matters other than class actions (and insolvency). As the use of litigation funding becomes more common in mainstream litigation, the need for capital adequacy regulation will become even more important.

3.2.3 This recognition of the likely growth in litigation funding across all types of litigation leads us to the view that any capital adequacy regulation must be applied across all litigation funders in a fashion that is easily reviewed and monitored.

3.2.4 We consider that an effective approach would be to focus on minimum requirements for asset backing and cash flow. In this regard, we have reviewed the various different approaches outlined in the submission and believe that the following steps would go a long way towards providing an adequate (but not onerous) level of regulation.

3.2.5 We propose that on entry into the Australian market, and on an annual basis thereafter, a litigation funder must:

3.2.5.1 maintain liquid capital reserves equal to at least twice the amount of its total investment in litigation across its business (both in Australia and overseas);

3.2.5.2 satisfy ASIC that it has sufficient assets (or alternative insurance arrangements such as After The Event or adverse costs insurance) to cover the potential liabilities associated with its unsuccessful cases including both the cost of the plaintiff class and any adverse costs orders; and

3.2.5.3 in the interests of transparency to the market, disclose in its annual reports its total potential exposure to all litigation costs (including both the cost of the plaintiff class and any potential adverse costs orders) and the amount that it has made as a provision to cover its exposure to these costs.

3.2.6 The above steps should not detract from, or take the place of, the Court making orders for security for costs on a case by case basis. Security for costs orders provide an additional and, in our view, necessary level of regulation that ensures defendants will have adequate costs protection in the event that they are ultimately successful in their defence at trial.

3.2.7 The retention of the practice that has developed in the Australian Courts in relation to security for costs orders in class actions will be of particular importance if overseas litigation funders are exempt from applying for a litigation funding licence as discussed at paragraph 3.62 of the Discussion Paper.

3.2.8 Regardless of any licencing exemption that may apply to overseas litigation funders, in the interests of transparency to the Australian market, all litigation funders operating in Australia should be required to disclose in their annual reports their total potential exposure to all litigation costs globally and the amount that they have made as a provision to cover this exposure.

5 COMMISSION RATES AND LEGAL FEES

5.2 **Question 5-2** ***In addition to Proposals 5-1 and 5-2, should there be statutory limitations on contingency fee arrangements and commission rates?***

5.2.1 To ensure that the plaintiff class receives an adequate return from any successful litigation, statutory limitations should be applied on contingency fee arrangements and commission rates.

5.2.2 We do not consider that the limits should be set on a sliding scale so that the size of the settlement or judgment dictates the percentage costs recovery. Any model needs to take into account the complexity of the particular matter (which is not necessarily intrinsically linked to the dollar value of the litigation) and the individual aspects of each case. After all, a large but relatively uncomplicated quantum claim in which liability has been admitted should cost less to pursue than a lesser claim in which all issues are "alive". In saying that, the concerns raised by Justice J Forrest about the level of claimed costs in the Black Saturday bushfires class action have some resonance.

5.2.3 Instead, we consider that a statutory maximum portion of fees and commissions to be paid from any one settlement or judgment sum should be set. We do not express an opinion on whether this portion should be 49.9% or some other amount. The setting of a statutory maximum will give both potential class members and their solicitors a clear guideline of the value of the litigation to each of them. What should be sought is a balance between "reward for effort" (as opposed to risk) and maintaining the public's confidence that the legal profession is not "cashing in" on claims that are pursued as much for cost generation purposes as they are in the pursuit of justice. It would be disappointing to see some of the consumer class action activity in the US replicated here: group members in the millions all pursuing the $5 they spent on a beverage product that did not make them "feel healthier".

5.2.4 Within the statutory maximum, the Court should then be given a specific statutory power / discretion to determine and set commission rates and contingency fees on a case by case basis. There must be such a discretion so that there is not an assumed guaranteed costs return as that can give rise to conflicts of interest. The statutory maximum should be treated as a true maximum, to only be exceeded by the Court's order in exceptional cases and, in the usual course, for orders to be made by the Court at a level somewhat lower than the statutory maximum. This would further reduce the tension between the Court's broad power to vary commission rates and contingency fees and the preservation of contractual bargains entered into.

5.3 **Question 5-3** ***Should any statutory cap for third-party litigation funders be set at the same proportional rates as for solicitors operating on a contingency fee basis, or would parity affect the viability of the third-party litigation funding model?***

5.3.1 We are not in a position to express an opinion on whether parity would affect the viability of the third-party litigation funding model.

5.3.2 Leaving this issue aside, we consider that there are the same benefits to be gained from imposing statutory caps in relation to matters that are funded by litigation funders, as there are in the matters that are funded by solicitors operating on a contingency fee basis. In particular, it will help to ensure that the plaintiff class receives an adequate return from any successful litigation. The setting of a statutory maximum will also give the potential class members and their solicitors and funders a clear guideline of the value of the litigation to each of them. Of course, flexibility in terms of what percentage return a litigation funder seeks will help foster competition amongst litigation funders, which should also drive quality in terms of the cases that are ultimately pursued (a funder is unlikely to speculate on a risky case that has the prospect of only a modest return).

5.3.3 We consider that the setting of statutory maximums across all funding approaches is something that the class action regime in Australia should aspire to. This approach could also be applied to new funding models that come into the market.

6 COMPETING CLASS ACTIONS

6.1 **Question 6-1** ***Should Part 9.6A of the Corporations Act and s 12GJ of the ASIC Act be amended to confer exclusive jurisdiction on the Federal Court of Australia with respect to civil matters, commenced as representative proceedings, arising under this litigation?***

6.1.1 It is our view that access to justice issues require consideration before limiting the number of Courts equipped to hear such matters, however the benefits of there being a consistency of approach within one jurisdiction and the flow-on effects in terms of competing class actions makes a compelling argument. In any case, if there is to be a "one-stop" jurisdiction model, that Court's processes should also be reviewed to add greater ease to pursue US style Motions to argue class certification and to pursue Motions to Dismiss on the grounds that proceedings have little merit. Perhaps the ability to pursue such early Motions should be incorporated as a mandatory procedural step in any future standard draft litigation timetable.

6.1.2 The time may also have come to increase the number of group members required to institute a class action. Securities class actions can invariably capture large numbers of investors as group members, but the growing Australian population when combined with the growing appetite for representative proceedings invites the raising of the bar at several levels, including the minimum numerical threshold requirements to constitute a class.

7 SETTLEMENT APPROVAL AND DISTRIBUTION

7.2 **Question 7-2** ***In the interests of transparency and open justice, should the terms of the class action settlement be made public? If so, what, if any, limits on the disclosure should be permitted to protect the interests of the parties?***

7.2.1 In view of the nature of Australia's class action regime and, in particular, that it is premised on an 'opt out' approach, we believe that the terms of any class action settlement should be made public.

7.2.2 All personal details of class members and any individuals of the defendant(s), including for example, their names, addresses, telephone numbers, etc. should not be included in the disclosed settlement terms.

7.2.3 Appreciating that there may be individual circumstances which would benefit from the terms (or certain terms) of settlement remaining confidential, we consider that the plaintiff class and the defendant(s) may by agreement apply to the Court for orders that the terms (or certain terms) of the settlement remain confidential, which has of course happened.

We trust that the above is of assistance. We would be happy to answer any questions you may have.

Yours sincerely

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