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AUSTRALIAN LAW REFORM COMMISSION

**INQUIRY INTO CLASS ACTION PROCEEDINGS
AND THIRD-PARTY LITIGATION FUNDERS**

**SUBMISSION BY LITIGATION CAPITAL MANAGEMENT LIMITED
JULY 2018**

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Litigation Capital Management Limited

1. Litigation Capital Management Limited (and its subsidiaries) (“LCM”) is a provider of litigation funding services and, from that perspective, makes the below submission in response to proposals and questions raised in the Australian Law Reform Commission (“ALRC”) Discussion Paper “Inquiry into Class Action Proceedings and Third-Party Litigation Funders” (June 2018) (“Discussion Paper”).
2. Founded in 1998, LCM was one of the first professional litigation funders in Australia, and it is one of the oldest litigation funders globally. LCM is publicly listed and further information about LCM can be found on www.lcmfinance.com.
3. Since its inception, LCM has continued to assist claimants to pursue meritorious claims and recover funds from the legal avenues and actions available to them.
4. LCM funds commercial, insolvency and arbitral proceedings, as well as representative actions.

Part 1: Introduction to the Inquiry

Proposal 1-1: The Australian Government should commission a review of the legal and economic impact of the continuous disclosure obligations of entities listed on public stock exchanges and those relating to misleading and deceptive conduct contained in the Corporations Act 2001 (Cth) and the Australian Securities and Investments Commission Act 2001 (Cth) with regards to:

- ***the propensity for corporate entities to be the target of funded shareholder class actions in Australia;***
 - ***the value of the investments of shareholders of the corporate entity at the time when that entity is the target of the class action; and***
 - ***the availability and cost of directors and officers liability cover within the Australian market.***
5. By way of preliminary comment, LCM notes that it does not take the Discussion Paper to be pre-empting or advocating that any review that may be conducted under Proposal 1-1 ought to necessarily lead to a particular change in the subject legislation, or to any such change. For example, LCM does not understand the Discussion Paper to be suggesting that the proposed review should necessarily lead to a relaxing of listed entities’ continuous disclosure obligations in order to ameliorate the propensity for corporate entities to be the target of funded shareholder actions.
 6. The Discussion Paper notes that there is said to be “...growing evidence of unintended adverse consequences caused by the existing framework of the Australian class action regime, coupled with the peculiar characteristics of the Australian statutory provisions concerning continuous disclosure obligations...and those relating to misleading and deceptive conduct”¹. LCM understands that the review suggested in Proposal 1-1 arises from the Inquiry’s acknowledgement that these asserted “unintended adverse consequences” are mostly outside the terms of reference for the present Inquiry and are not matters that are able to be resolved by the Inquiry’s mandated consideration of the “two overarching issues of the class action regime: the integrity of third-party funded class actions, and the efficacy of the class action system”². The Discussion Paper confirms that the ALRC agrees that

¹ Discussion Paper at [1.73]

² Ibid at [1.21]

public debate about the underlying law was more appropriate than changing the mechanism by which class actions were prosecuted³.

7. On the above basis, LCM does not oppose a proposal that the Australian Government conduct a further review of the issues outlined in Proposal 1-1 if it elects to do so.
8. However, LCM respectfully submits that if a review were to be conducted into these issues, any such review ought not be conducted on terms of reference that apply a magnifying glass to a hand-picked list of narrow questions without consideration of the wide-reaching effects of the subject legislation. By way of example, LCM suggests that any review of the described questions ought to also include consideration of at least the following related matters:
 - 8.1. Broadly, the favourable legal and economic impact of the legislation, including its importance in reducing information asymmetry between companies and investors, maintaining confidence of market participants and, critically, encouraging greater investment into the very corporate entities that are listed on the stock exchange.
 - 8.2. The contribution made to a transparent and fully functioning market by the deterrent effects of securities class actions, taking into account the fact that regulatory action cannot address every contravention.
 - 8.3. Avenues to minimise the adverse effect of a securities class action on the defendant company's market value at the time that it is the target of an action. This may include an introduction of threshold insurance requirements in order to mitigate direct risk to a defendant company's assets if it is targeted, thereby diminishing cause for alarm in the market and retaining value for existing shareholders.
 - 8.4. Consideration of compulsory insurance requirements for listed entities as a means of increasing the premium pool of directors and officers insurance (noting the Discussion Paper's comments (at 1.74) that the current pool is said to be inadequate to meet the current and projected levels of insured securities class action losses).
 - 8.5. Avenues to decrease the cost and delay faced by shareholders mounting securities actions, including legislative change aimed at simplifying loss assessment and procedural change aimed at effecting earlier resolution of securities claims.
9. For completeness, although LCM does not understand the Discussion Paper to be suggesting it, LCM expressly rejects any proposition that the prevalence of shareholder class actions ought to be curtailed, particularly by way of any change in the enforceability of the underlying obligations presently owed by listed entities. LCM submits that there is limited evidence of any "unintended adverse consequences" that might warrant such action and that such a change, if effected, would almost certainly create far-reaching and drastic consequences contrary to shareholder interests and, ultimately, contrary to the ongoing viability of securities markets and the availability of capital.

³ Discussion Paper at [1.82]

Part 3: Regulating Litigation Funders

Proposal 3–1: The Corporations Act (2001) (Cth) should be amended to require third-party litigation funders to obtain and maintain a ‘litigation funding licence’ to operate in Australia.

10. Subject to its responses to Proposal 3-2 and Question 3-1 below, LCM supports the introduction of a licence for litigation funders operating in Australia.
11. However, LCM notes the Discussion Paper’s limitation that:

“For the purposes of this Inquiry, a litigation funder does not include an insurer funding the litigation costs under a pre-existing policy, or a solicitor acting on a ‘no win, no fee’ basis (or under a contingency fee agreement, in jurisdictions where this is permitted)”⁴
12. LCM submits that it is artificial to draw this distinction in certain circumstances and addresses the need for a broader application of licencing requirements in the relevant sections below.
13. LCM also notes that the proposed licence will be “to operate in Australia” but that:

“There would be no need for foreign litigation funders to meet the specific Australian requirements provided they meet comparable requirements in their home jurisdiction”⁵
14. LCM submits that the exemption to be provided needs to take care not to give foreign entities a market advantage over Australian litigation funders and that it is critical to carefully review each Australian requirement when considering whether and how the foreign entity is said to be meeting “comparable requirements in their home jurisdiction”.

Proposal 3–2: A litigation funding licence should require third-party litigation funders to:

- ***do all things necessary to ensure that their services are provided efficiently, honestly and fairly;***
 - ***ensure all communications with class members and potential class members are clear, honest and accurate;***
 - ***have adequate arrangements for managing conflicts of interest;***
 - ***have sufficient resources (including financial, technological and human resources);***
 - ***have adequate risk management systems;***
 - ***have a compliant dispute resolution system; and***
 - ***be audited annually.***
15. The Discussion Paper suggests that a litigation funders’ licence could impose “comparable obligations” to an AFSL⁶, could require funders to comply with the “same general obligations as those set out in Chapter 7 of the Corporations Act”⁷ and could entail a “bespoke regulatory regime”⁸.

⁴ Discussion Paper at [1.7]

⁵ Ibid at [3.62]

⁶ Ibid at [3.4]

⁷ Ibid at [3.5]

⁸ Ibid at [3.4]

16. LCM understands that the Discussion Paper does not make a final proposal for litigation funder licensing, and LCM suggests that careful consideration and further consultation would be required in order to ensure that the licensing regime ultimately proposed meets its objectives and does not impose measures that are counter-productive to the efficient and fair provision of funding services.
17. It is presently difficult to comment on proposals around “sufficient” technological and human resources, “adequate” risk management systems or “compliant” dispute resolution systems without considerable further detail of what this may entail. The scope of the proposed audit requirement is also presently unclear.
18. However, LCM supports the move for licensing as an added means of ensuring continued integrity within the litigation funding industry and LCM would be pleased to actively participate in further consultation with respect to licensing requirements if offered an opportunity to do so.

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

19. LCM respectfully agrees with the ALRC’s suggestion 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”⁹. LCM further submits that it is important for a litigation funding licensee to demonstrate attributes required to recognise and manage potential conflicts of interest, so as to ensure compliance with the requirements of *Corporations Amendment Regulation 2012* (No. 6) (Cth).
20. LCM submits that:
 - 20.1. In order for a litigation funding entity to be licensed, its responsible managers (persons that have direct responsibility for significant day-to-day decisions about funded claims) ought to be of good fame and character, and have skills and knowledge that demonstrate competence to effectively provide litigation funding services.
 - 20.2. In assessing whether a person is of good fame and character, the licensing body shall consider the person’s:
 - 20.2.1. Criminal convictions or judicial findings of dishonesty, fraud or breaches of obligations relating to conflicts of interest;
 - 20.2.2. Any suspension or disqualification of the person’s AFLS, Practising Certificate, registration as a liquidator or right to serve as a Director;
 - 20.2.3. Bankruptcy status;
 - 20.2.4. Status as an officer of any company that has been wound up in insolvency or placed in external administration.
 - 20.3. In assessing whether a person has appropriate skills and knowledge, the licensing body shall consider the person’s demonstrated:
 - 20.3.1. Legal education, qualifications and experience;

⁹ Ibid at [3.39]

- 20.3.2. Understanding of Australian Court rules and processes;
 - 20.3.3. Understanding of solicitors' obligations as officers of the Court;
 - 20.3.4. Understanding of solicitors' obligations to their clients (as distinct from any obligations to funders).
- 20.4. Persons holding a current solicitor's Practising Certificate in Australia should be deemed to satisfy the requirements for a litigation funding license.

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

- 21. It is, of course, critical that third-party litigation funders have sufficient resources in order to conduct their business.
- 22. Although LCM notes that security for costs does presently provide some protection to both defendants and, indirectly, to plaintiffs, LCM respectfully agrees with the ALRC's view that "the mechanism for providing security for costs, while important, does not negate the need for a capital adequacy requirement as part of the licensing regime"¹⁰. However, LCM also agrees with ALRC's comments that "the appropriate capital adequacy standard for litigation funders needs careful consideration to ensure that it is sufficient but not so burdensome that it undermines access to justice"¹¹.
- 23. LCM submits that the appropriate balance in capital adequacy requirements would be struck by requiring funders to:
 - 23.1. Meet solvency requirements;
 - 23.2. Manage future solvency requirements by having access to sufficient capital within Australia to meet forecasted funding obligations in this jurisdiction;
 - 23.3. Manage the risk of contingent liabilities for adverse costs by having access to capital representing a percentage of the entity's uninsured exposure, capped at a set amount. LCM submits that in order to recognise the natural spread of risk across diverse claims, the extent of the requirement ought to be inversely proportionate to the number of claims being funded. For example, the scale could range from 5% of uninsured risk capped at \$1million, and require higher percentages and caps for entities funding fewer claims;
 - 23.4. Obtain independent audits of their financial reports and of their compliance with capital adequacy licensing requirements;
 - 23.5. Have ongoing disclosure obligations in respect of the capital adequacy requirements, including an obligation to promptly report to the licensing body if the funder becomes aware that it is in breach of any of those requirements.
- 24. LCM further submits that listed entities with market capitalisation of over \$20million should be deemed to satisfy the requirements for a litigation funding license.

¹⁰ Discussion Paper at [3.49]

¹¹ Ibid

Question 3–3: Should third-party litigation funders be required to join the Australian Financial Complaints Authority scheme?

25. LCM submits that there is presently insufficient evidence to support an argument in favour of compulsory Australian Financial Complaints Authority (“AFCA”) membership for litigation funders. In the absence of such further evidence, LCM suggests that AFCA may not be the best forum for resolution of the disputes and complaints that may commonly arise between funders and funding product “consumers”.
26. It should be noted that litigation funding contracts are diverse and bespoke products, most often entered into by a funder with sophisticated commercial parties.
27. AFCA’s rules and terms of reference are not yet clear, and by reference to the rules of the Superannuation Complaints, Financial Ombudsman and Credit Investments services that AFCA will replace, it is difficult to identify the types of common litigation funding service disputes or complaints that would fall within AFCA’s jurisdiction. LCM notes the ALRC’s comment that “if access to AFCA was granted to consumers of litigation funding services, it would be necessary to determine in what circumstances access to AFCA would be appropriate”¹². LCM agrees and respectfully submits that in the absence of a clear understanding of these circumstances and AFCA’s suitability to address them, any decision on compulsory membership would be premature.
28. Anecdotally, LCM’s standard dispute resolution mechanisms set out a process through which the parties are directed to a prompt conciliation meeting which, if unsuccessful, is followed by a prompt and binding arbitration before a legally qualified arbitrator agreed by the parties or, in the absence of agreement, by a person selected by the President of the Law Society in the relevant State. The costs of the arbitration are then borne as the arbitrator decides. In LCM’s experience, this process allows for prompt, efficient and fair resolution of disputes and complaints in the unlikely case that one arises.
29. By way of more general comment on complaints resolution, LCM stresses the paramount importance of confidentiality and efficiency of any compulsory process that may be introduced. Litigation funding services naturally operate in parallel to an adversarial legal proceeding, which must at all times be progressed in an efficient and timely way. It is of critical importance that any complaint-handling procedure offers a fast and confidential method of dispute resolution and adjudication. The process ought not be capable of delaying or adversely impacting the underlying legal proceedings, or otherwise providing the defendant with information or other tactical advantage. LCM suggests that the satisfaction of these important requirements may require a bespoke regime or process.

¹² Discussion Paper at [3.68]

Part 4: Conflicts of Interest

Proposal 4–1: If the licensing regime proposed by Proposal 3–1 is not adopted, third-party litigation funders operating in Australia should remain subject to the requirements of Australian Securities Investments Commission Regulatory Guide 248 and should be required to report annually to the regulator on their compliance with the requirement to implement adequate practices and procedures to manage conflicts of interest.

30. LCM supports Proposal 4-1, save that LCM stresses the importance of maintaining confidentiality of individual litigation funding arrangements in certain claims (particularly commercial matters). LCM submits that any reporting obligation ought not require reporting on individual cases unless such reporting is anonymised and confidential.

Proposal 4–2: If the licensing regime proposed by Proposal 3–1 is not adopted, ‘law firm financing’ and ‘portfolio funding’ should be included in the definition of a ‘litigation scheme’ in the Corporations Regulations 2001 (Cth).

31. LCM supports Proposal 4-2.

Proposal 4–3: The Law Council of Australia should oversee the development of specialist accreditation for solicitors in class action law and practice. Accreditation should require ongoing education in relation to identifying and managing actual or perceived conflicts of interests and duties in class action proceedings.

32. LCM supports Proposal 4-3, save as to note that in LCM's experience skilled class action lawyers are mindful of their duties in class action proceedings and are careful and considered in managing those duties as well as any actual or perceived conflicts of interest that may arise.

Proposal 4–4: The Australian Solicitors’ Conduct Rules should be amended to prohibit solicitors and law firms from having financial and other interests in a third party litigation funder that is funding the same matters in which the solicitor or law firm is acting.

33. LCM supports Proposal 4-4, subject to LCM's submission on in response to Proposal 5-1.

Proposal 4–5: The Australian Solicitors’ Conduct Rules should be amended to require disclosure of third-party funding in any dispute resolution proceedings, including arbitral proceedings.

34. The Discussion Paper states that “The Federal Court of Australia’s Practice Note [GPN-CA] requires disclosure of litigation funding agreements to the Court and other parties. There is no comparable obligation for solicitors to disclose the existence of litigation funding agreements in any other forms of dispute resolution proceedings that do not have court supervision”¹³. LCM respectfully highlights that the subject Practice Note sets out arrangements for the management of class actions matters within the National Court Framework and only applies to actions commenced under Part IVA of the *Federal Court of Australia Act 1976 (Cth)*. Therefore, the Practice Note does not require disclosure of litigation funding agreements in any claims other than class actions.

¹³ Discussion Paper at [4.66] and footnote 81

35. LCM further submits that the benefits or reasons for the proposed unprecedented disclosure of litigation funding agreements to the Court and/or to other parties in proceedings other than class actions are not entirely clear.
36. In support of such disclosure, the Discussion Paper states that “clear rules relating to disclosure of litigation funding in all forms of dispute resolution will provide greater transparency around funding arrangements and, in turn, enhance confidence in the legal profession and the civil justice system”.¹⁴
37. LCM respectfully submits that in actions other than class actions, it is difficult to advocate for “greater transparency” around funding arrangements and difficult to see how such transparency would enhance confidence in the legal profession or the civil justice system.
38. Litigation funding arrangements are private commercial contracts between a litigant and a funder. Those arrangements are not the subject of the dispute before the Court or any request for judicial advice. They are separate arrangements negotiated by a litigant as a means of leveraging against the asset of the litigation in order to obtain a financial product. The litigants enter into these arrangements with a view to effectively presenting their claims before the Courts. How the use of such products can be said to erode confidence in the legal profession or the civil justice system is unclear and, in LCM’s submission, lacks evidentiary basis.
39. LCM also submits that it is inappropriate to require a party using litigation funding services to disclose the source of its resources when an opponent using any other financial product (including speculative fee arrangements with solicitors, loans from financial institutions or insurance) has no obligation to do so. The purpose of this narrow spotlight on funding disclosure is not apparent and its effect is not fair. If disclosure is required (which LCM does not support), LCM submits that it ought to apply equally to all means of costs funding (including insurance policies relied on by defendants). LCM notes that the *ICCA Queen Mary Task Force Report on Third-Party Funding in International Arbitration* recommended the disclosure of litigation funding agreements in arbitral proceedings on the basis that contracts of insurance which had the effect of funding the respondent to an arbitration, should also be disclosed.
40. Further, LCM submits that the compulsory disclosure of litigation funding agreements may have broader detrimental consequences. By way of example:
 - 40.1. LCM highlights that mandatory disclosure of the existence of litigation funding arrangements will have the consequence of bringing to light both those who do, and also those who do not, have funding in place. If disclosure is mandatory for all matters, the absence of a disclosure will by inference signal the absence of litigation funding which fact alone could, in some cases, confer a tactical advantage on a defendant. Not only would it send a message about the resources allocated to the plaintiff’s case, but it could also be an indicator that the plaintiff was unable to obtain funding (perhaps because a litigation funder has assessed the merits of the case and has declined to invest in it).
 - 40.2. There are also commercial reasons why certain parties may not wish to have their funding arrangements made public. Parties should be entitled to discretion in regard to their choice of financial products and if this is not available, some parties may be forced to refuse litigation funding which would

¹⁴ Ibid at [4.67]

otherwise allow them to pursue their meritorious claims in the most effective way.

41. Finally, LCM notes that Federal Court of Australia Class Actions Practice Note GPN-CA does not allow for blanket disclosure of third-party funding, but includes restrictions such as a permission to redact the funding agreement in order to conceal any information which might reasonably be expected to confer a tactical advantage on another party to the proceeding. LCM submits that if Proposal 4-5 is to be accepted (which LCM does not support), any such disclosure ought not be unfettered, but rather should allow redactions in order to, at least, conceal information which might be expected to confer a tactical advantage.

Proposal 4–6: The Federal Court of Australia’s Class Action Practice Note (GPN-CA) should be amended so that the first notices provided to potential class members by legal representatives are required to clearly describe the obligation of legal representatives and litigation funders to avoid and manage conflicts of interest, and to outline the details of any conflicts in that particular case.

42. LCM supports Proposal 4-6.

5. Commission Rates and Legal Fees

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.***

43. By way of general observation, in its role as a litigation funder LCM does not take a view on whether solicitors ought to be permitted to enter into contingency fee agreements. Although LCM acknowledges that the introduction of contingency fee arrangements has the prospect of increasing competition in litigation funding products, LCM also sees this as an opportunity.
44. LCM does, however, wish to offer its comments on certain aspects of the Discussion Paper and Proposal 5-1. LCM’s comments are broadly focussed on cost, conflict, “hybrid” funding models and risk.

Cost

45. With respect to the cost of funding products, the Discussion Paper notes that the “expansion of the funding market would promote competition and eventually lower commission rates set by litigation funders, creating a more level playing field”¹⁵.
46. Although LCM acknowledges the economics of increased competition, LCM respectfully submits that the Discussion Paper does not give sufficient weight to the

¹⁵ Discussion Paper at [5.11]

commercial risks, pressures and imperatives that inform a funder's commission. Experienced funders do not simply set funding terms at an arbitrary rate. The rates are arrived at by a careful analysis of the claim at hand as well as a disciplined consideration of broader factors that make a litigation funding business viable in the long term.

47. LCM makes further submissions on the cost of funding products in response to Proposal 5-3 and Question 5-2 below. However, for the purposes of Proposal 5-1 LCM merely submits that if lawyers effectively assume the same risks and costs as those faced by funders (including the very real risk that some matters will not succeed and will result in considerable losses), it is rather optimistic to expect that lawyers' financial modelling would not ultimately drive their contingency fee rates into a similar range to the rates developed over the life of the litigation funding industry.

Conflict

48. The Discussion Paper sets out various alternative views on the question of conflicts in contingency fee arrangements and LCM otherwise acknowledges that a great deal of consideration and careful attention has already been given to the issue.
49. LCM generally agrees with advocates for the retention of the ban on contingency fees.
50. LCM submits that it is almost impossible to see how the conflict issues that may arise in a tripartite funding arrangement could be said to be mitigated by merging the interests of two out of the three parties. LCM submits that the issues will only be exacerbated. By way of illustration, if the lawyers accept the role of a funder in addition to their role of representative and advisor, they will face a daily tension between their ethical and professional duties to the Court and to the litigant, as against their own interests and their objectives to:
 - 50.1. minimise professional fee earners' time on a matter;
 - 50.2. minimise disbursement outlay;
 - 50.3. minimise adverse costs risk;
 - 50.4. maximise return; and
 - 50.5. manipulate the timing of a resolution, depending on the lawyers' own cash flow and other commercial pressures.
51. LCM submits that in practice the separation between the funder and the lawyers, the funder's limited ability to take steps without the lawyers' involvement and the litigant's approval, and the lawyers' overriding duty to act in the interest of the litigant, all serve as effective safeguards for that litigant's interests.
52. Presently, the lawyers can advise a litigant to take a course that may be contrary to the interests of the funder. However, if the lawyers are the funder, they will be constantly faced with decisions on how and when to disclose specific conflicts to clients, and how and when to advise clients against the lawyers' own interests. The resulting minefield is unlikely to be entirely transparent and cannot be said to mitigate any issue said to be presented by the practice of litigation funding.
53. Finally, the Discussion Paper confirms that the ALRC considers that Australian Solicitors' Conduct Rules "should expressly prohibit solicitors from being invested in the outcome of a funded matter in which they are acting through having an interest in

that litigation funder”¹⁶. The rationale for introducing such prohibitions on the one hand, while recommending that solicitors should be permitted to charge contingency fees on the other, is unclear and the result is somewhat contradictory.

Hybrid model of funding

54. Firstly, LCM notes that Proposal 5-1 restricts a funder ability to “directly” fund a claim “on a contingency basis” if that claim is also funded by lawyers charging on a contingency basis. For the sake of clarity, LCM submits that there ought not be any prohibition on a funder directly funding a claim on a contingency basis, as long as that funder’s relationship is only with the solicitor and the funder’s interest (which is to be negotiated by the funder and the solicitor) cannot rise any higher than the commission to be received by the lawyers from their contingency fee arrangement. If this were the case, LCM submits that:
- 54.1. The interests of class members are protected by the certainty of a single commission rate;
 - 54.2. If the class members’ interests are protected as above, there is no apparent need for any further restriction on the relationship between the solicitors and funders that may “sit behind them, as opposed to alongside them”; and
 - 54.3. In order for there to be greater access and utility in the proposed contingency fee methods, there ought to be much greater flexibility in the way that solicitors elect to manage their exposure.
55. Secondly, the Discussion Paper confirms that the Proposals “aim to protect class members from the possibility of paying out a percentage of settlement to both solicitors and funders. It does not prohibit moneys being returned to litigation funders from solicitors when funding is on a **portfolio basis**—that is where the funding sits behind the solicitor, as opposed to alongside the solicitor”¹⁷ (emphasis added).
56. Portfolio funding is a term that is ordinarily used to refer to the funding of multiple cases and LCM submits that contrary to the above comments in the Discussion Paper, there is no basis to restrict a funders’ involvement to “portfolio funding” only and thereby exclude single-case funding arrangements.

Risk

57. LCM submits that lawyers availing themselves of the opportunity to charge on a contingency basis should be subject to the same licensing regulations that may apply to litigation funders, unless they satisfy the Court that their financial outlay and adverse costs risks are underwritten by a “hybrid” arrangement with a litigation funder (as described in the Discussions Paper at 5.37, subject to the above comments).

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.

58. LCM does not comment on Proposal 5-2.

¹⁶ Discussion Paper at [4.64] and Proposal 4-4

¹⁷ Discussion Paper at [5.37]

Question 5–1: Should the prohibition on contingency fees remain with respect to some types of class actions, such as personal injury matters where damages and fees for legal services are regulated?

59. LCM does not comment on Question 5-1.

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.

60. LCM notes that Proposal 5-3 is limited to class action proceedings. However, the Proposal is not limited to applications for settlement approval under section 33V of the Federal Court of Australia Act. Nor is it limited to common fund order applications. What appears to be proposed is that the Court's existing supervisory role in approving settlements or discontinuances within its class action lists is to be extended into an unfettered and express power to "reject, vary or set" key terms in funding contracts.
61. LCM respectfully submits that this Proposal is unworkable.
62. Firstly, the proposed power has no restrictions as to timing, purpose, benefit, consideration or procedure. It is simply a broad power to intervene in financial agreements between funders and class members. The scope for interlocutory chaos is vast.
63. Secondly, a statutory power to "reject, vary or set" commission rates is counterproductive to the objective of offering greater certainty to class members. It only offers greater unpredictability.
64. Thirdly, if the Proposal were accepted, a funder would be expected to invest very significant costs and face very considerable adverse costs risk in the hope that the Court will "set" an acceptable commission at some point in the action and, if the Court does so, that it will not thereafter "vary" or "reject" it. The prospect of investing in class actions that are regulated in this way is not a commercially sound proposition. It will not appear attractive to experienced funders, nor will it appear that way to any party that invests capital in the litigation funding industry.
65. As was noted in *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq) (No 3)* [2017] FCA 330 at [160], "if any exercise of power under Part IVA is to be in the best interests of group members, it is not conducive to that objective to take a step that would unnecessarily chill a mechanism that group members may need to access the regime under Part IVA in the first place". LCM respectfully submits that as it is presently drafted, Proposal 5-3 would go a long way towards chilling funder investment and would ultimately have a considerable adverse effect on potential class members' access to justice.

Question 5–2: In addition to Proposals 5–1 and 5–2, should there be statutory limitations on contingency fee arrangements and commission rates, for example:

- **Should contingency fee arrangements and commission rates also be subject to statutory caps that limit the proportion of income derived from settlement or judgment sums on a sliding scale, so that the larger the settlement or judgment sum the lower the fee or rate? or**
- **Should there be a statutory provision that provides, unless the Court otherwise orders, that the maximum proportion of fees and commissions paid from any one settlement or judgment sum is 49.9%?**

66. LCM answers Question 5-2 in the negative.

67. Firstly, by way of preliminary comment, LCM notes that Question 5-2 is posed “in addition” to Proposals 5-1 and 5-2, which Proposals are directed exclusively at class actions. Question 5-2 also refers to contingency fees, which are only proposed for class claims. However, the terms of Question 5-2 itself do not appear to be restricted to class action proceedings.

68. If Question 5-2 is intended to cover single-claim funding, LCM expressly rejects the proposition of any legislative change that would restrict freedom of contract by imposing arbitrary restrictions on commercial terms available to the parties. There is no evidence of a need or a call for legislature (or the judiciary) to do so, and LCM submits that it is an unnecessarily interventionist step that would only serve to decrease flexibility in funding products, render some meritorious claims un-fundable and, ultimately, have a direct adverse effect on willing contracting parties’ access to justice and an indirect adverse effect on availability of funding generally.

69. Secondly, LCM submits that despite continued attention to the issue of costs and commissions, there remains no adequate pretext for Question 5-2. Although the Discussion Paper refers to two matters in which group members received less than 50% of the recovery, it also acknowledges that in each of those cases the Court conducted a detailed review of all the circumstances and concluded that a) the resolution amount was reasonable; b) the costs were reasonable and c) the funding commission was reasonable. In short, the class incurred reasonable costs in progressing a litigation, but achieved an outcome in the litigation that was less than what it hoped for. LCM submits that this result, while never strived for, is nevertheless an age-old risk for any claimant embarking on a piece of litigation.

70. Litigation is unpredictable and risky, and the cost of advancing a claim, particularly against an adversarial defendant, can have a very significant impact on the action’s ultimate proceeds. This is true of both funded and unfunded proceedings, both commercial claims and class actions. However, the services of a litigation funder allow the rights of a litigant to be enforced with that litigant facing no risk or cost, while retaining an interest in any net upside. And it is merely a commercial reality that those services have a cost, just like the services of a solicitor. It is trite to say that in the absence of funding and legal assistance (the costs of which were confirmed by the Court to be reasonable) the class members would have recovered nothing.

71. Thirdly, LCM notes the Discussion Paper’s comment (at 5.71) that:

“...the maximum cap would likely become the default amount awarded to solicitors or funders. This has been the experience with uplift fees for solicitors. However, it is not envisaged by the ALRC that any imposition of statutory caps in Australia would decrease the need for court oversight—considered critical to ensure that each commission/contingency fee is set appropriately, and not just at the top of the cap.”

72. LCM agrees with the default-rate risk identified by the ALRC. Aside from this, however, LCM submits that the above comment highlights the inherent paradox in the rationale for capping proposals. It is acknowledged that judicial oversight will remain critical in the review of funding commissions. The Discussion Paper otherwise refers to “a policy imperative to give the Court more tools to ensure that the proportion of settlements returned to the class is reasonable and appropriate”¹⁸. However, what is then proposed in Question 5-2 are provisions that would fetter judicial power by imposing predetermined outcomes. LCM opposes such an approach and advocates for continued recognition of the nuanced and multifaceted nature of settlement approval and common fund order applications, and the need for flexibility in judicial consideration of funding costs on a case-by-case basis.
73. Fourthly, as to the specific mechanisms raised in Question 5-2, LCM submits that:
- 73.1. At present, funding terms are usually communicated, negotiated and agreed at the commencement of the funding relationship and are not re-negotiated as the action progresses.
- 73.2. However, legal costs do increase throughout the life of the proceedings, at times beyond the levels that were anticipated at the commencement of the action. Claim quantum and settlement expectations have also been known to scale downwards as a case evolves.
- 73.3. In testing the proposition that it might be desirable to set caps on funding commissions and fees, the Discussion Paper refers to two recent settlement approvals, namely *Clarke v Sandhurst Trustees Limited (No 2)* [2018] FCA 511 and *Caason Investments Pty Limited v Cao (No 2)* [2018] FCA 527. In these actions the solicitors received 31% and 43% of the recovery respectively. The funder received 30% in both.
- 73.4. It must be highlighted that the legal costs that are approved in a class action are borne by the funder over the course of the matter. It is the funder that outlays those costs and carries the risk that they will not be reimbursed (and, worse, that adverse costs will also need to be met).
- 73.5. The use of predetermined caps or scales for funding commissions based only on the quantum of recovery fail to properly recognise the ongoing costs and risks faced by a funder, which costs and risks the funder has limited power to control.
- 73.6. The only way that statutory caps could achieve an appropriate outcome would be if they were somehow aligned with a cap on the total legal costs that can be charged in respect of the action by both a plaintiff and a defendant. LCM does not advocate this approach, but does note that despite referring to the extent of solicitors’ fees in certain claims, the Discussion Paper Proposals only offer that the aggregate of solicitors’ fees and funder’s commissions ought to be capped (leaving open the question of how solicitors’ fees and funder’s commissions are to be apportioned within that cap), and otherwise focuses on the capping or varying/setting/rejecting of funders’ commissions.

¹⁸ Discussion Paper at [5.64]

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

74. Subject to LCM's submissions on statutory caps and contingency fee arrangements, LCM agrees that any statutory caps for third-party litigation funders should be set at the same proportional rate as for solicitors operating on a contingency fee basis.

Question 5–4: What other funding options are there for meritorious claims that are unable to attract third-party litigation funding? For example, would a 'class action reinvestment fund' be a viable option?

75. LCM does not comment on Question 5-4.

6. Competing Class Actions

Proposal 6–1: Part IVA of the Federal Court of Australia Act 1976 (Cth) should be amended so that:

- **all class actions are initiated as open class actions;**
- **where there are two or more competing class actions, the Court must determine which one of those proceedings will progress and must stay the competing proceeding(s), unless the Court is satisfied that it would be inefficient or otherwise antithetical to the interest of justice to do so;**
- **litigation funding agreements with respect to a class action are enforceable only with the approval of the Court; and**
- **any approval of a litigation funding agreement and solicitors' costs agreement for a class action is granted on the basis of a common fund order.**

76. LCM notes that, although much of the discussion around competing class actions has been focussed on securities claims, Proposal 6-1 is not restricted to proceedings of that nature. The Discussion Paper refers to *Perera v GetSwift Limited* [2018] FCA 732 and the Honourable Justice Lee's comments that the decision focussed on "how the Court deals with competing commercial enterprises which seek to use the processes of the Court to make money". LCM respectfully suggests that this focus cannot apply to all class actions that are commenced in the Federal Court, and submits that the full range of affected representative proceedings needs to be carefully considered before any prohibitions of the type proposed are introduced.

77. LCM further submits that policy considerations ought to prevent the introduction of Court Rules that stand in the way of a party's right to choose their legal representation. In this regard:

77.1. The Discussion Paper states its intention that the Proposal is "largely consistent with the most recent decision of the Federal Court in *GetSwift*"¹⁹.

77.2. LCM does note that in *GetSwift* at [241] the Honourable Justice Lee commented that "at least insofar as the funder is concerned, I think that this notion of 'choice' may be somewhat exaggerated". However, His Honour then went on to find that "the choice of solicitors may be in a slightly different category, given the nature of the relationship between a solicitor and client, but in the event that a particular group member has sufficient desire to retain a particular solicitor, this can be accommodated by that group member opting out".

¹⁹ Discussion Paper at [6.28]

- 77.3. The Discussion Paper does acknowledge that individuals would have the opportunity to opt out of a proceeding. However, it goes on to add that “any individual actions (will be) stayed until the class action is resolved”²⁰.
- 77.4. LCM respectfully submits that this suggestion of a stay of individual claims is close to a complete barrier to a party’s right to choose its representation.
78. Additionally, LCM submits that the combined effect of the Proposals would naturally encourage a race to commence, followed by a flurry of “bids” from alternative funders and lawyers.
79. Although LCM notes the intention to allow no “first mover advantage”, it submits that the filing of any significant claim would almost certainly invite the filing party’s peers to file competing claims in the hope that their offering will be selected. With bookbuild and clients being offered no place in this Proposal, there would be little preventing firms and funders from treating the process as a sort of public auction. Importantly, the expectation that only one firm and funder would be “chosen” in any event would create a hesitation amongst firms to invest significant resources in working a claim up before filing. The “bids” could often be hastily prepared, without sufficient consideration of case theory, pleadings or assessment of likely loss and damage. LCM submits that this combination of factors would only serve to undermine public perception of the civil justice system.
80. LCM further notes that Proposal 6-1 does not address the factors that the Court should have regard to in determining “which one of those proceedings will progress”. In addition to its comments on Proposal 6-1 generally, LCM respectfully submits that the question of competing actions ought not be the subject of a rigid “one size fits all” solution.
81. LCM again advocates for continued recognition of the nuanced and multifaceted nature of class action claims, and the need for flexibility in judicial consideration of these issues on a case-by-case basis. LCM submits that the fast-developing jurisprudence on these issues is best placed to provide clarity and fairness in this rapidly developing area in the long term.
82. In response to the proposals for Court approval of litigation funding agreements and compulsory common fund orders specifically, LCM:
- 82.1. Refers to the thrust of its submissions in response to Part 5;
- 82.2. Notes that in advocating for this approach, the Discussion Paper states (at 6.35) that “Resolving the funding rate at the beginning of litigation gives both funders and class members certainty as to the costs they will have to pay in the event litigation is successful. A similar approach is proposed with respect to lawyers’ fees”. LCM queries how this approach interacts with the powers proposed in Part 5 of the Discussion Paper. Nevertheless, LCM supports the proposal that any applications for common fund orders ought to be decided at the beginning of a class action, with that commission being fixed for the life of the claim.
83. Finally, LCM respectfully submits that the Proposals advanced in relation to competing class actions have the (presumably unintended) combined effect of disenfranchising class members from the process of enforcing their legal rights. The Proposals render funding contracts with class members meaningless, allow class

²⁰ Ibid at [6.46]

members no choice of representation and stay the claims of any individuals that choose to opt out. When one considers that this Proposal applies equally to securities class actions and also to claims relating to property destruction, product liability and environmental damage, LCM submits that such Proposal are particularly detrimental and counter-productive. This is particularly so in circumstances where the current system is, in LCM's view, achieving excellent outcomes for class members.

Proposal 6–2: In order to implement Proposal 6-1, the Federal Court of Australia's Class Action Practice Note (GPN-CA) should be amended to provide a further case management procedure for competing class actions.

84. LCM refers to its responses to Proposal 6-1. However, if Proposal 6-1 is accepted (which LCM does not support), LCM supports Proposal 6-2.

Question 6–1: Should Part 9.6A of the Corporations Act 2001 (Cth) and s 12GJ of the Australian Securities and Investments Commission Act 2001 (Cth) be amended to confer exclusive jurisdiction on the Federal Court of Australia with respect to civil matters, commenced as representative proceedings, arising under this legislation?

85. LCM answers this question in the negative. LCM submits that there is insufficient evidence to support a constriction of the jurisdiction of State Courts and the rights of parties to progress their claims within those forums.

7. Settlement Approval and Distribution

Proposal 7–1: Part 15 of the Federal Court of Australia's Class Action Practice Note (GPN-CA) should include a clause that the Court may appoint a referee to assess the reasonableness of costs charged in a class action prior to settlement approval and that the referee is to explicitly examine whether the work completed was done in the most efficient manner.

86. LCM supports Proposal 7-1, save for commenting that the appointment of such a referee ought not be compulsory but merely another tool available to the Court in its consideration of class action settlements.

Question 7–1: Should settlement administration be the subject of a tender process? If so:

- ***How would a tender process be implemented?***
- ***Who would decide the outcome of the tender process?***

87. LCM does not comment on Question 7-1.

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

88. Although funders are ordinarily not party to class action settlement agreements, LCM responds to Question 7-2 in the negative.

89. LCM notes the motivation set out in the Discussion Paper, namely that “class action settlements are different from other settlements principally because the law requires the Court to approve any settlement” and that “a reasoned judgment can only be delivered if the terms of the settlement are entirely, or at least in large part, public”²¹.

²¹ Discussion Paper at [7.35]

90. LCM submits that the fact that the Court approves settlement agreements and publishes its judgments does not mean that, by extension, the subject matter of those judgments ought to also be publicly disclosed. LCM notes, with respect, that Courts are skilled at navigating confidentiality issues in arguments and in published reasons.
91. LCM submits that the disclosure of settlement terms would have a natural and direct effect on the defendants' propensity to agree to settlements, as well as the quantum of those settlements. As is acknowledged in the Discussion Paper²², the confidentiality of an agreement assists to protect a defendant's reputation. It also protects the defendant from the tactical disadvantage of third parties being aware of precisely the terms that a defendant will agree in relation to a particular case. If the defendant has to disclose these matters as part of a settlement, this would create a significant barrier to negotiated resolution.

8. Regulatory redress

Proposal 8–1: The Australian Government should consider establishing a federal collective redress scheme that would enable corporations to provide appropriate redress to those who may be entitled to a remedy, whether under the general law or pursuant to statute, by reason of the conduct of the corporation. Such a scheme should permit an individual person or business to remain outside the scheme and to litigate the claim should they so choose.

92. LCM does not comment on Proposal 8-1.

Question 8–1: What principle should guide the design of a federal collective redress scheme?

93. LCM does not comment on Question 8-1.

²² Ibid at [7.34]