AustralianSuper | An Industry SuperFund

30/07/2018

Australian Law Reform Commission
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Dear Sir/Madam

RE: AUSTRALIANSUPER SUBMISSION TO THE INQUIRY INTO CLASS ACTION PROCEEDINGS AND THIRD-PARTY LITIGATION FUNDERS

AustralianSuper welcomes the opportunity to make a submission to the above Inquiry.

About AustralianSuper

AustralianSuper is Australia's largest single superannuation fund and is run only to benefit members. We don't pay commissions to anyone to recommend us, nor do we pay dividends to shareholders. The fund has over 2.2 million members and manages over $130 billion of members' assets. Our sole focus is to provide the best possible retirement outcomes for members.

Key Points

This submission highlights the following risks and emerging issues for institutional investors participating in class actions which we have identified via AustralianSuper's potential participation in shareholder class actions over a number of years:

- i) Spurious actions including the attendant risk that these may cause overly risk averse governance standards in companies over time and the cost for institutions to assess such claims.
- ii) High costs to participate and the lack of alternative participation options.
- iii) Insufficient information available to assess the action at sign-up date.
- iv) Entrance of new third-party litigation funders into the Australian market and the difficulty of undertaking sufficient due diligence of these funders.
- v) Proliferation of multiple, near-identical competing actions.

As a result, we express support for Proposal 3-1, Proposal 5-3, Proposal 6-1 and Proposal 7-1 which we believe will go some way to addressing the issues outlined above.

We express our disagreement, however, with Proposal 1-1 to review Australia's continuous disclosure obligations and misleading and deceptive conduct laws as a response to issues which we believed have primarily emerged as a result of the evolution of Australia's shareholder class action system itself, rather than the continuous disclosure regime.

This information is of a general nature and does not take into account your personal objectives, situation or needs. Before making a decision about AustralianSuper, consider your financial requirements and refer to the Product Disclosure Statement (PDS). AustralianSuper Pty Ltd ABN 94 006 457 987 AFSL 233788, Trustee of AustralianSuper ABN 65 714 394 898. Industry SuperFund logo used with permission of Industry Fund Services (IFS). This consent had not been withdrawn at the date of publication.

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Note that the views expressed in this submission will be further supported by our planned consultation with the Australian Law Reform Commission regarding this Inquiry in August.

AustralianSuper's Approach to Participation in Class Actions

AustralianSuper occasionally participates in shareholder class actions and we consider class actions as a cost-effective way to recover member losses in cases of genuine unlawful conduct. In assessing our participation however, we carefully consider the merits of each claim and seek to participate in actions only as a governance mechanism of last resort. We believe that in a system in which class actions are launched only in instances of genuine unlawful conduct, that they can act as a mechanism to improve general governance standards over the long term.

However the way the class action system in Australia has evolved has created a number of issues for institutional investors, such as AustralianSuper, who are seeking to only participate in cost-effective meritorious claims. In the following sections we address these issues and our support for the proposals introduced in the discussion paper which we believe will go some way to addressing them.

Spurious Actions

Spurious actions are those in which the allegations made against a company are in the best cases very weak and in the worst cases, false. The traditional closed nature of shareholder class actions in Australia creates a risk that spurious actions can incorrectly appear to have significant institutional investor support. Institutional investors are approached by a law firm or a third-party litigation funder to sign up for an action. Often, investors lack the resources or there is insufficient information to be able to carefully consider the claim and therefore they may sign up on the basis that there is nothing to lose. This can create the illusion that a significant proportion of the shareholder register believes there is merit to the allegation. Company boards in this position face a decision to spend potentially significant board and company resources to contest the claim or to settle the claim quickly, and at a lower cost, despite its potentially spurious nature.

To remove the risk that shareholders signing on to a class action – as required in a closed action – is incorrectly interpreted as endorsing the merits of a claim, we support Proposal 6-1 that Part IVA of the *Federal Court of Australia Act 1976* (Cth) should be amended so that all class actions are initiated on an open class basis.

High Cost to Participate

As highlighted in the discussion paper, shareholder class actions can often be expensive. Litigation funding fees in general appear too high but shareholders have little leverage to negotiate substantially lower fees as only a single participant in the market. We note that when there is competition for an action, often litigation funding fees – which are typically set at 28 - 40% – can often come down to 19 – 24%. This is taken by us as evidence that litigation funding fees can be lower but the structure of the market makes it difficult for participants to negotiate lower fees.

As a participant seeking to participate in genuine actions in order to recuperate losses borne by our members, we support proposals which can lower costs. Therefore we support:

i) Proposal 5-3, that the Federal Court be given express statutory power to reject, vary or set the commission rate in third-party litigation funding agreements and;
ii) Proposal 7-1, that the Federal Court of Australia's Class Action Practice Note 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.

We believe that these two proposals have the capacity to substantially decrease costs for participants. In the event that Proposal 5-3 is accepted, given that shareholders typically lack leverage to negotiate improved fee structures, we do not believe that institutional shareholder support for a litigation funding agreement should be used as a basis itself to determine appropriate fees. From our experience, signing a litigation funding agreement is typically a reflection of our belief in the merits of the claim and our lack of alternative options to pursue the claim rather than an endorsement of the agreement's fee structure.

Insufficient Information at Sign-up Date

The traditional closed nature of shareholder class actions in Australia means that shareholders are required to sign-up by a specific deadline. At this point investors often have insufficient information regarding the merits of the claim or further information is can be revealed after the deadline. In order to remedy this issue, we support Proposal 6-1 that all class actions are initiated as open class actions. This will ensure that participants are not required to make a decision whether to participate and therefore implicitly endorse an action based on insufficient information.

Entrance of New Third-party Litigation Funders into the Australian Market

We have noticed a significant number of new third-party litigation funders approaching AustralianSuper to participate in class actions. As potential participants in funded actions, we welcome a competitive litigation funding market and recognise that:

i) Third-party litigation funders play a valid role in Australia's class action system and;
ii) The introduction of new third-party litigation funders will naturally lead to more competitive pricing.

However, we also note that it is often difficult and onerous for investors to undertake adequate due diligence on these new third-party entrants regards to their resourcing, risk management systems, capital adequacy and the accuracy of their communications. We therefore support the concept of Proposal 3-1 that third-party litigation funders should obtain and maintain a litigation finding license to operate in Australia.

Notwithstanding, we encourage this reform to be negotiated in collaboration with litigation funders to ensure that licensing requirements are not so onerous as to discourage competition in the litigation-funding landscape.

Proliferation of Multiple Competing Actions

In recent years we have observed a proliferation in the number of competing actions. Comparing competing actions is often complex and time-consuming for potential participants. Further, the existence of competing actions per se does not appear to be accompanied with significant benefits for participants.

Therefore we are supportive Proposal 6-1 and Proposal 6-2 which seek to provide greater clarity on the case management procedure for competing class actions. We also note that Proposal 6-1, which proposes that all class actions are initiated on an open basis, may discourage competing class actions.

Proposal to Review Continuous Disclosure Obligations and Misleading and Deceptive Conduct Laws

Australia's continuous disclosure obligations regime and misleading and deceptive conduct laws are a foundation of free and open markets. Indeed, we believe the current regime typically functions well and contributes to market efficiency.

As we have outlined above, we acknowledge that there are issues currently causing the suboptimal operation of Australia's shareholder class action system. However, we believe that these issues are a result of the structure of the class action system itself rather than as a result of the continuous disclosure regime. Further, we believe that through the Proposals advanced by the Inquiry regarding the requirement to run all actions on an open basis, the regulation of litigation funders, conflicts of interest, commission rates, claims consolidation and settlement approval, many of the distortions in the class action system can be addressed.

Therefore we disagree with Proposal 1-1 that the Australian Government should commission a review of continuous disclosure obligations and laws relating to misleading and deceptive conduct as a response to the Inquiry into class action proceedings and third-party litigation funders.

If you have any questions of us or would like further information please do not hesitate to [redacted] in the first instance.

Yours sincerely

Andrew Gray
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