SUBMISSION TO AUSTRALIAN LAW REFORM COMMISSION (ALRC) INQUIRY INTO CLASS ACTION PROCEEDINGS AND THIRD-PARTY LITIGATION FUNDERS

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In response to the proposals and questions raised by the ALRC in its Discussion Paper dated June 2018 the following submissions are made:

General

Balancing competing legitimate objectives

The merits of, on the one hand, increasing access to the civil justice system and enforcement of laws that in some cases have a public purpose and on the other, not unduly increasing civil disputation in society, are both legitimate considerations of public policy that need to be balanced in a fair manner (see further discussion below).

Implications of a legislative 'go ahead' to third party litigation funding

The licensing of litigation funders will clearly amount to a recognition by the legislature of litigation funding as a mainstream business activity. In giving the 'go ahead' to litigation funding, the legislature needs to be mindful that it has addressed the mischiefs that were the genesis of the original (and admittedly somewhat ancient) prohibition of litigation funding and the reasons for the long standing rule against maintenance and champerty.

Mischiefs to be addressed

The original concerns that led to third party litigation funding (as maintenance and champerty) being banned for over a millennia appear to have been essentially (1) a possible increase in the amount of civil litigation such as was said to be against the public interest;[2] (2) the need to protect vulnerable litigants from unconscionable funding agreements and from the

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[2] See e.g. *Alabaster v Harness* [1895] 1 QB (Per Lord Escher at 342).

(costs) consequences of a failed suit and;[3] (3) early concerns as to corruption of the civil judicial process.[4]

These all therefore need to be dealt with and I shall consider each in turn.

(i) An increase in the amount of civil litigation such as is said to be against the public interest

The ban on third party litigation funding arose partly out of concerns that removing it would see the amount of litigation increased in a way that may be considered to be against the public interest. In *Alabaster v Harness*,[5] Lord Escher MR in the Court of Appeal spoke of considerations of public policy, in that maintenance and champerty may increase the amount of litigation 'in a way that would be mischievous to the public interest'.[6] This reflects the public policy maxim that *interest rei publicae ut sit finis litium*. This has been variously translated as 'it concerns the state that lawsuits be not protracted' [7] 'it is in the interests of the state that there be an end to litigation'[8] and 'it is advantageous to the public that there be an end to lawsuits'.[9] The maxim is certainly not an historical curiosity as it is underlies much of the modern push to mediation and alternative dispute resolution which are clearly designed to end controversies and avoid the expensive and time consuming process of parties having 'their day in court'.[10] There is perhaps a question whether the maxim sees mischief in the *number* of cases or the *length* of those cases[11] as on its face it may appear to focus on the latter.[12]

Certainly, today, legitimate public interest in generally minimising civil disputation[13] is also balanced against legitimate public interest and social justice arguments in allowing plaintiffs to pursue meritorious claims and sometimes to break new ground in using the law to increase accountability.[14] This appears to have gone some way to increasing access to civil justice[15] in increasing the number of claims brought by citizens who would otherwise be unable to access the legal system.[16] This would appear to have brought greater balance between the rights

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[3] Ibid.
[4] See Percy H Winfield, 'History of Maintenance and Champerty (1919) 35 *Law Quarterly Review* 50
[5] [1895] 1 QB.
[6] [1895] 1 QB, 342.
[7] John Burke, *Osborne's Concise Law Dictionary* (Sweet and Maxwell 1976).
[8] Peter Nygh and Peter Butt (eds), *Butterworths Concise Australian Legal Dictionary* (Second Edition 1998).
[9] Oxford Reference http://www.oxfordreference.com/view/10.1093/acref/9780195369380.001.0001/acref-9780195369380-e-742 .
[10] See generally Tania Sourdin, *'Alternative Dispute Resolution,* Lawbook Co 2012.
[11] M Duffy, "Two's Company, Three's a Crowd? Regulating Third-Party Litigation Funding, Claimant Protection in the Tripartite Contract, and the Lens of Theory" (2016) 39(1) *University of New South Wales Law Journal* 165, 172 (footnote 37).
[12] Though see Hon Justice Keane, PA, "Access to Justice and Other Shibboleths", paper delivered to the Judicial Conference of Australia, October 2009. See also the minority judgment of Callinan and Heydon JJ in *Campbells Cash and Carry Pty Ltd v Fostif Pty Limited ("Fostif* in the High Court*")* (2006) 229 CLR 386.
[13] Justice P A Keane, *Access to justice and other shibboleths*, Paper presented at the JCA Colloquium Melbourne 10 October 2009.
[14] Using the courts to increasing the accountability to citizens of mechanised online corporate businesses or service providers is likely to be an increasingly desirable area for growth.
[15] Justice B Murphy and Camille Cameron, 'Access to Justice and the Evolution of Class Action Litigation in Australia' (2006) 30(2) *Melbourne University Law Review* 399.
[16] Hon Justice Murphy and Vince Morabito, 'The first 25 years: Has the class action regime hit the mark on access to justice?' Ch 3 in Damian Grave and Helen Mould (eds) *25 Years of Class Actions in Australia* (Ross Parsons Centre 2017).

and interests of ordinary citizens of modest means and those with comparatively large resources (including both corporations and government).[17] In some cases this has also seen better enforcement of laws which may sometimes have a public regulatory purpose.[18] It is suggested that these developments should not be generally discouraged by regulation that might make such access uneconomic.[19]

Further, a reasonable level of access to the courts and to representation can be argued to be an antecedent or necessary assumption of the concept the rule of law. Access to justice has been described as 'fundamental human right which ought to be readily available to all.'[20]

(ii) Need for protection of litigants

Another basis for the ban on third party litigation funding was a bid to protect litigants from unfair or unconscionable funding agreements, as well as the consequences of a failed suit (such as being ordered to pay the defendant's costs).[21]

Theoretical research in agency theory, game theory and transaction cost economics[22] suggests that the first is a legitimate concern and may benefit from laws for simplified and better disclosure, which appear to be contemplated in ALRC Proposal 3-2 below suggesting a requirement of 'clear, honest and accurate disclosure'.

The second is partly being remedied by market forces in terms of funders agreeing to provide indemnities, though there is currently no legal requirement on funders to do this and the ALRC recommendations do not appear to require this (though somewhat inconsistently, they do suggest such a legal requirement for lawyers to provide an indemnity if acting on a contingent fee basis - see ALRC Proposal 5–1 below).

Though ALRC Proposal 3-2 below suggests that funders must have sufficient resources including financial, technological and human resources, (see below), in its current form it does not require them to provide indemnities.

(iii) Possible corrupting effects on the civil judicial system?

Lastly but importantly, historical legal research[23] shows that the oldest reason for the ban on 'maintenance and champerty' going back to the thirteenth century was to remedy problems with corruption of public officials including judges, sheriffs and clerks of the king,[24] lords of court[25] and the 'Chancellor, Treasurer or Justices'[26] (i.e. public officials of both the executive and judicial branches – given a lack of clear separation of the two at this early time). It focused on receipt of property by such persons while a thing was 'in plea' before the king's

[17] V Morabito and J Eckstein, 'Class Actions Filed for the Benefit of Vulnerable Persons – An Australian Study' (2016) 35 *Civil Justice Quarterly* 61.
[18] See e.g. M. Duffy, 'Australian Private Securities Class Actions and Public Interest: Assessing the 'Private Attorney-General' by Reference to the Rationales of Public Enforcement' (2017) 32(2) *Australian Journal of Corporate Law* 162.
[19] Information from funders themselves will be important in relation to assessing what is economic or otherwise.
[20] Per Lord Millett in *Thai Trading Co v Taylor* [1998] QB 781, 786.
[21] *Alabaster v Harness* [1895] 1 QB.
[22] Duffy above n 11.
[23] Percy H Winfield, 'History of Maintenance and Champerty (1919) 35 *Law Quarterly Review* 50.
[24] Ibid 59, 65
[25] Ibid 60.
[26] Ibid 61.

court (curia regis).[27] In modern terms this could be seen as bribery to influence the outcome of civil litigation.

Bribery or conflicted incentives

Today, there are substantial layers of law and regulation designed to more directly avoid corruption of the legal process, by punishing false testimony,[28] banning bribery of witnesses[29] or Commonwealth public officials[30] (including judicial officers[31]) or otherwise perverting the course of justice or conspiring to defeat justice.[32] There is obviously also substantial statutory regulation of lawyers[33] in addition to civil liability for breaches of fiduciary duty. These laws operate in various forms to the present day and generally work well, though regulatory vigilance will always be required to avoid conflicts of interest. Some of the proposals of the ALRC (4-1 through 4-6) undoubtedly recognise the problems of conflicts of interest and perverse incentives in the legal profession and the submitter has made further suggestions in 4 and 5 to deal with these.

Bias, conflict and recusal of judges regarding funders or insurers

Further, civil courts are in the particularly privileged position of being empowered by the state to order large redistributions of private and public property (according to law) and this is a privilege which has traditionally been used by Australian courts with the utmost propriety.

Nevertheless, there remains the question of bias, conflicts and recusal which may take on new importance as large litigation funders backed by equity markets become increasingly involved in civil litigation[34] backing plaintiffs seeking large sums from defendants who may be backed by large insurance companies.

Quite apart from the obvious issue of the interests of judicial officers and others in litigants themselves, the question arises whether a judicial officer with a large or material direct financial interest in either a litigation funder or an insurer which is backing one of the parties, has a direct financial interest in the case before her/him. There is little authority on this but the courts have certainly looked at an ownership interest in a *party* at least. This may give some guidance.

In *Ebner v. Official Trustee in Bankruptcy; Clenae Pty Ltd v. Australia; New Zealand Banking Group Ltd* [35] a majority in the High Court (Gleeson CJ, McHugh, Gummow and Hayne JJ) indicated that the mere fact of ownership of shares in a listed public company which is a litigant did not mean that a judge had a direct pecuniary interest in the outcome of

[27] Ibid 60.
[28] *Crimes Act 1914* (Cth) s35.
[29] Ibid s37.
[30] *Criminal Code Act 1995* (Cth) s142.
[31] Ibid [490.7].
[32] *Crimes Act 1914* (Cth) s41-s45.
[33] See e.g. *The Legal Profession Uniform Law Application Act 2014* of each Australian state containing at schedule 1 the *Legal Profession Uniform Law.*
[34] According to one respected litigation funder there is currently a 'literal wall of money' looking to be invested, a percentage of which is looking at investment in funded litigation claims: Remarks by Hugh McLernon of Bentham IMF at Monash Business School-Federal Court Seminar 'Increased regulation of litigation funding - a timely crackdown or a regulatory 'solution' in search of a problem? Federal Court Melbourne 9 April 2018. http://www.fedcourt.gov.au/digital-law-library/seminars
[35] (2000) 205 CLR 337.

the litigation. Stating that there was a difference between having an interest in the outcome of a case, and having an interest in a party to the case, they stated that the question was whether the judge had a financial interest in the outcome of the litigation. If so, the application of the apprehension of bias principle would lead to the judge being disqualified. In contrast, where the outcome of a case would have no bearing upon the value of the shares held by the judge in the listed public company then the judge did not have a direct pecuniary interest in the outcome of the litigation.[36] Interestingly, Kirby J and Gaudron J took a stricter view with the former holding that a judge would be automatically disqualified from hearing a matter if he or she had a direct pecuniary interest either in 'the subject matter of, or in a party to, litigation'.[37]

Australian law in this area is mainly case law[38] though there is some statutory regulation in s 34(4) of the *Crimes Act 1914* (Cth) which provides for an offence for a federal judge or magistrate who 'has a personal interest' in a matter and then 'perversely exercises jurisdiction' in the matter.

This may be an area for further review and consideration.

Specific proposals

In response to the specific proposals and questions raised by the ALRC in its Discussion Paper dated June 2018 the following submissions are made:

1. Introductory proposal

ALRC 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.*

Submission

[36] Ibid 337-338.
[37] Ibid 394.
[38] In contrast to the United States where there is statutory regulation and where Title 28 of the United States Code (USC) deals with judicial disqualification in the federal judicial system. The test is whether impartiality might reasonably be questioned (s455).

Both liability caps[39] and/or proportionate liability[40] to moderate the impact of such claims on corporations and their shareholders (and insurers) have been advocated in the literature.

On the other hand it is submitted that a balanced review should also consider and assess the public interest value of shareholder class actions in achieving inter alia, compensation, a fairer and more efficient securities market, deterrence of misleading conduct and non-disclosure in securities markets and other law enforcement objectives that may lead to these outcomes.[41] This might also include an evaluation which is comparative with the outcomes of ASIC enforcement in these areas.[42]

3. Regulating Litigation Funders

ALRC 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.

Submission

The submitter generally supports a form of licensing as a general principle subject to the general issue of the effects of giving a 'go ahead' to litigation funding as discussed above and also to the following considerations.

Technical drafting issues

The interaction of this proposal with the somewhat complicated 'financial product' and 'financial service' provisions under the *Corporations Act 2001* (Cth) ('the Corporations Act') is not entirely clear as it is normally the provision of actual financial products or financial services that leads to the requirement of a licence. This was the approach of the New South Wales Court of Appeal in *International Litigation Partners Pte Ltd v Chameleon Mining NL*,[43] where Giles, Young and Hodgson JJA found that a litigation funding agreement was a 'financial product' as it was a facility through which the litigant managed financial risk.[44]

On appeal to the High Court[45] however, the main focus was on the question of whether the third party litigation funding agreement was in fact a 'credit facility' under the Corporations Act and therefore excluded from the definition of financial product by section 765A(1)(h)(i) of the Act.[46] Applying the definition of 'credit' in regulation 7.1.06(3)(a) of the *Corporations Regulations 2001* (Cth), the Court found that a contract, arrangement or understanding that is any form of financial accommodation is 'credit', and its provision 'for any period' would be a 'credit facility'.[47] The majority (French CJ, Gummow, Crennan and Bell JJ) noted the

[39] M. Duffy, 'Investor loss from securities nondisclosure: A statutory presumption of causation on the Canadian Model? (2009) 32(3) *University of New South Wales Law Journal* 965, 982.
[40] Justice Jonathan Beach, 'Some current issues in securities class actions' (2017) 36 *Civil Justice Quarterly* 146, 151.
[41] There is such an analysis in Duffy above n 18.
[42] Ibid.
[43] *International Litigation Partners Pte Ltd v Chameleon Mining NL* (2011) 276 ALR 138.
[44] Under s 763A (1) of the Act, a 'financial product' includes a facility which, or through the acquisition of which, a person manages financial risk. Section 763C provides that a person manages financial risk if they manage the financial consequences to them of particular circumstances happening.
[45] *Chameleon Mining* (2012) 246 CLR 455.
[46] This set out specific things that were not financial products.
[47] Ibid 463–4 [26] (French CJ, Gummow, Crennan and Bell JJ).

obligation undertaken by the funder in the funding deed to pay the litigant's legal costs[48] and concluded that the funding deed was a 'credit facility'[49] and therefore did not need an Australian Financial services Licence (AFSL).

Whilst the submitter agrees with ALRC that some of the detail of ASIC's regulatory guidance in relation to AFSL's may not be all fit for purpose for litigation funding, this might suggest that separate ASIC guidance is necessary but not that existing legislative regime is necessarily inapt. In that regard it is noted that ALRC states that most of the obligations under s912A are appropriate. It may be of course that the prolix Financial Services provisions of Chapter 7 (s760-s 1101J) of the Corporations Act are somewhat problematic (which, at nearly 400 pages, are in the submitter's view, prolix and potentially problematic generally!). Nevertheless, as a matter of drafting and legislative power (including constitutional power), it is not completely clear whether or not a litigation funding agreement would need to specifically be included as a 'financial product' in s764A of the Corporations Act for the licencing requirement or power to arise.

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.*

Submission

The submitter generally supports these proposals subject to the following.

Prudential regulation

There is obviously a question as to how far the requirement to have sufficient resources including financial, technological and human resources [50] amounts to a form of *de facto* prudential regulation. The answer is somewhat unclear and there appears to be some variation based upon the attitude of ASIC to the financial services or products being offered and its (soft law) regulatory guides.[51] This obviously falls short of full prudential regulation through APRA.

Conflicts of interest

In relation to conflicts of interest, it is submitted that the conflict between a litigant's interest and a funder's interest in a proceeding could be harmonised somewhat by the introduction of a statutory duty of utmost good faith of a funder to a litigant.[52]

[48] Ibid 464 [29].
[49] Ibid 465 [33].
[50] As appears in *Corporations Act 2001* (Cth) s 912A (d).
[51] Robert Baxt, Ashley Black and Pamela Hanrahan, *Securities and Financial Services Law* (Lexisnexis Butterworths 2008) [14.26].
[52] This would also incidentally tend to reduce conflict between a lawyer's fiduciary duty to the litigant and the lawyer's obligations, duties or allegiances to a funder.

To that end the submitter proposes the introduction of a provision for a statutory obligation of good faith to be implied into litigation funding contracts. The obligation would be mutual – both funder and litigator to owe the duty to each other.[53]

Duty of good faith – rationale

Funders are not lawyers so that a fiduciary duty to the litigant is not appropriate. Funders are probably more analogous to insurers.[54] They (a) are third parties who fund a litigant in an action; (b) through their contractual arrangements with the litigant exercise some control over the litigant and the proceedings; (c) may provide an indemnity for adverse costs and (d) have a financial interest in the outcome of proceedings. This 'insurance analogy' has some judicial support[55] though it is not universally accepted.[56]

Some arrangements between lawyer and funder state that in a situation of conflict the litigant's instructions to the lawyer override the funder's instructions to the lawyer.[57] This however may be subject to the litigant's obligation to act consistently with his/her agreement with the funder which includes the obligation to follow all reasonable legal advice and fully co-operate with the funder and lawyer.[58] There may also be agreement between the lawyer and funder that the lawyer-funder agreement overrides any lawyer-litigant agreement which may cause uncertainty.[59] A lawyer may have incentives or interests in pleasing the funder as the latter may be a source of work.[60] Thus the lawyer may be tempted to act in the funder's interests which though often coincident with the litigant's interest, may occasionally diverge from or conflict with the litigant's interests.

These issues could be partly resolved, and conflicts somewhat harmonised by making funders subject to a statutory duty of good faith in the same manner as insurers are under *Insurance Contracts Act 1984* (Cth) ss 13–14. A statutory duty could not be contracted out of. Such a duty would fall short of a fiduciary duty in that it would not require the funder to prefer the

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[53] In relation to good faith duties Professor Waye has stated: 'The characterization of the relationship between funder and claimholder as non-fiduciary does not exclude the imposition of an implied duty of good faith in respect of the exercise of the funder's powers under the funding agreement either. Although a funder may not be expected to sacrifice its own interests in favour of a claimholder as a fiduciary, because of the high degree of reliance reposed in the funder, it will be appropriate to impose a duty upon the funder to regard the interests of the claimholder as well as its own and to require the funder to act accordingly when exercising particular powers, for example, the power to negotiate settlement.' See Vicki Waye 'Conflicts of Interest Between Claimholders, Lawyers and Litigation Entrepreneurs' (2007) 19(1) *Bond Law Review* 225, 256-257

[54] John Walker, 'Policy and Regulatory Issues in Litigation Funding Revisited' (2014) 55 *Canadian Business Law Journal* 85, 86. See Duffy above n 11, footnote 189.

[55] Waye notes President Mason's citing of the insurance analogy in *Campbell's Cash and Carry v Fostif NSWCA* (2005) 63 NSWLR 203, 225 [82] and Justice Ipp's approach in *Project 28 Pty Ltd v Barr* [2005] NSWCA 240, [70]–[72]: 'Conflicts of Interests', above n 53, 242. In the latter case, his Honour noted that the law had already countenanced insurers' absolute control over proceedings on the ground that that control was tempered by a duty on the part of the solicitors and the insurers to conduct the proceedings with due regard to the nominal claim holder's interests.

[56] Grave, Adams and Betts point to differences arguing that (a) insurers are usually totally indemnifying or seeking to recover an indemnified loss through subrogation rights so that in general their financial interest in the litigation is greater than a funder; (b) funders typically exercise greater control of litigation than insurers; and (c) funders usually have rights to terminate the agreement at will whereas insurers usually do not: see Damian Grave, Ken Adams and Jason Betts, *Class Actions in Australia* (Thomson Reuters, 2nd ed, 2012) 860–1.

[57] Duffy above n 11, footnote n 156.

[58] Ibid.

[59] Ibid.

[60] Of course a desire to get repeat work is not to be criticised in itself. It may require an informed consent however.

litigant's interests over its own interests, requiring rather, regard to the interests of both parties.[61] In the insurance context this duty has been developed somewhat in Australia to include having regard to the legitimate interests of the litigant (as well as to the insurer's own interests), fairness, decency and honesty and full and frank disclosure.[62] Finkelstein J has noted that the obligation may be incapable of precise definition but that good faith may connote an absence of bad faith.[63]

Such a duty,[64] like the insurance duty, should be mutual so that it would also require the litigant to fully disclose the relevant facts of the dispute, including any weaknesses in the case, to the Funder who in turn has overarching obligations to the court (to further the administration of justice, act honestly and not make frivolous claims lacking a proper basis[65]) so that it will be less likely that flawed claims will be brought before the courts – which could otherwise waste the court's time and resources.

Appropriate provisions may be:

> **The duty of the utmost good faith** [based partly upon *Insurance Contracts Act 1984* (Cth) s13]
>
> A litigation funding contract is a contract based on the utmost good faith and there is implied in such a contract a provision requiring each party to it to act towards the other party, in respect of any matter arising under or in relation to it, with the utmost good faith.
>
> Parties not to rely on provisions except in the utmost good faith [based partly upon *Insurance Contracts Act 1984* (Cth) - sect 14]
>
> If reliance by a party to a third party litigation funding contract would be to fail to act with the utmost good faith, the party may not rely on the provision.
>
> In deciding whether reliance by a litigation funder on a provision of the third party litigation funding contract would be to fail to act with the utmost good faith, the court shall have regard to any notification of the provision that was given to the litigant.

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[61] *Overlook v Foxtel* (2002) Aust Contract Reports 90-143, 91,970.

[62] See *CGU Insurance Ltd v AMP Financial Planning Pty Ltd* (2007) 235 CLR 1. For other relevant case law and commentary see Geoffrey R Masel, *Australian Insurance Law* (annotated loose-leaf), 2005-present, LexisNexis Butterworths, [10,305.10]-[1305.20].

[63] See *Pacific Brands Sport & Leisure v Underworks Pty Ltd* (2005) 12 Aust Contract Reports 90-213, para 65. Per Finkelstein J:

> *I appreciate that the standard of conduct imposed by a covenant of good faith is incapable of precise definition. That does not produce an unworkable obligation. There are many instances to be found in the law of contract and elsewhere of obligations that are incapable of clear definition. Reference need only be made to the obligation of reasonableness that pervades so much of our law. Be that as it may, a good starting point in any particular enquiry is to see whether the impugned conduct (in this case a termination) was motivated by bad faith, or was for an ulterior motive or, if it be any different, whether the defendant acted arbitrarily or capriciously. It may also be proper to investigate whether the impugned act was oppressive or unfair in its result. If any of these things can be established then, in all probability, the obligation will be breached and the resultant act (or omission) of no effect.*

[64] See also generally, Geoffrey Kuehne 'Implied Obligations of Good Faith and Reasonableness in the Performance of Contracts: Old Wine in New Bottles?" (2006) 33(1) *University of Western Australia Law Review* 63.

[65] *Civil Procedure Act 2010* (Vic) ss 10, 16-18.

Excesses – rationale

Another method of reducing conflicts of interest by better aligning the interests of funders and litigants is to permit litigation funders to allow a small reasonable nominal 'excess' on their indemnity for adverse costs. Insurers generally do this on most forms of indemnity. The latter will have the effect of better aligning funders' and litigants' interests, particularly in relation to settlement discussions.[66] In settlement discussions a representative party and group members may be more likely to want to 'bat on' in court where they have no downside costs risk because they are fully indemnified and the funder carries all risk. Some limited liability of the litigant due to an excess would give the litigant 'skin in the game' in taking the risk of going to trial and thus better align their interests with the funder.

A permitted excess on the adverse costs indemnity would also have the effect of discouraging parties from bringing unmeritorious or frivolous claims.[67] Though the spectre of liability for adverse costs orders as a useful disincentive for frivolous or vexatious claims or defences is sometimes disputed,[68] the writer's experience is that the spectre is a disincentive to client litigants going to court with unmeritorious claims (indeed this fear is presumably the genesis of the market for indemnities from funders). In this manner, an excess may bring back some of the traditional effects of the traditional *English rule*[69] on cost shifting in discouraging claimant litigants bringing claims with a low probability of success.[70] It may also slightly reduce funding costs.

The permitted excess should be reasonable and subject to court approval to avoid abuses.

A possible provision in relation to this might be:

> **Excesses**
>
> A third party litigation funding agreement may provide for an excess on indemnity for adverse costs provided that:
>
> (a) the excess is reasonable in all the circumstances;
>
> (b) the excess does not substantially reduce the litigant's access to justice;
>
> (c) the excess has been clearly disclosed to the litigant before entering any agreement with the funder;
>
> (d) the excess is approved by the Court.

ALRC Question 3–1

[66] See generally Duffy above n 11, 189, 200, and 204.
[67] As to costs orders being a disincentive against pursuing frivolous claims see Victorian Law Reform Commission, *Civil Justice Review Report*, [2008] VLRC 645.
[68] Australian Government Productivity Commission, Access to Justice Arrangements, 2014 (quoting ALRC Costs Shifting - Who Pays for Litigation (ALRC Report 75) 1995) 443.
[69] I.e. that the loser pays the winner's costs.
[70] Charlotte Wrendenburg 'Legal costs awards and access to justice' Ch 5 in Willem van Boom (ed) *Litigation, Costs, Funding and Behaviour* (Routledge 2017) 87.

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

Submission

Qualifications requirements are set out in s912A of the *Corporations Act 2001* (Cth) ('the Corporations Act). Good fame and character requirements are set out in s913B. These would presumably apply were funders to be required to have Australian Financial Services Licences (AFSL). It is not entirely clearly, nor has it been demonstrated, that there should be special good fame and character requirements above and beyond what is required for an AFSL under s912A and s913B of the Corporations Act. If standards in this regard are to be heightened because litigation funding 'is involved in the justice system, which is a public good'[71] then it would appear to logically follow that these would also need to be imposed on insurers who are similarly involved in the justice system.

ALRC 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.

Submission

This is discussed in response to No submission other than to observe that expert corporate financial evidence may be required to determine this.

ALRC Question 3–3

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

Submission.

There would not seem to be a compelling reason for exemption. The AFCA might however require a specialist division to deal with the unique and specialist nature of complaints in this area. The option of litigants to seek redress through the courts should also be preserved and there might need to be allowance for application to transfer AFCA complaints into courts dealing with the subject funded litigation.

4. Conflicts of Interest

ALRC 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

[71] ALRC, *Inquiry into Class Action Proceedings and Third Party Litigation Funders*, June 2018, 3.27.

annually to the regulator on their compliance with the requirement to implement adequate practices and procedures to manage conflicts of interest.

Submission

A statutory duty of good faith as discussed above would go some way to *harmonising* and partly eliminating conflicts of interest whereas RG 248 is mainly about *managing* such conflicts.

Further, RG 248 is very much in the nature of non-binding 'soft law'. RG 248 addresses conflicts by requiring them to be disclosed and for written procedures to be established to deal with them. Despite its length, RG 248 does not say much about what those procedures might be other than certain suggestions as to what the lawyer and/or funder should 'consider including' in agreements[72] and certain matters that ASIC 'expects' in regard to their relations (including procedures for settling differences on settlement offers).

In relation to the latter RG 248.88 states that

> We expect that if your litigation scheme settles without a proceeding being issued, the terms of any settlement agreement should also be approved by counsel (or senior counsel if involved).

The provision does not specify who instructs counsel or who counsel owes duties to in this process so this process is somewhat ambiguous.[73] For instance, if counsel's instructing solicitor and the funder both want to settle but the litigant (who is counsel's client[74]) does not want to settle, is counsel placed in a dilemma by being instructed to provide binding advice to the litigant on whether to settle? The problems of this type of heavy reliance of Australian courts upon the opinions of Senior Counsel in determining whether such a settlement is fair and reasonable has been noted.[75] A greater use of contradictors in the settlement phase has been advocated as one solution.[76]

Save for these matters, which might suggest a review and/or some tinkering with RG 248 the submitter generally supports this proposal.

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[72] These include a cooling-off period which provides an opportunity for members to seek legal advice; an obligation for the lawyer to give priority to the instructions given by the member over those given by the funder; the procedure that will be applied in reviewing and deciding whether to accept any settlement offer, including the factors that will and will not be taken into account in deciding to settle; an obligation to provide clear and full disclosure of any terms of settlement to all members and to the court (where applicable); how disputes in relation to the scheme will be resolved; and an obligation to provide clear and full disclosure to members of the terms of the agreement between the funder and the lawyers. See ASIC Regulatory Guide 248 [RG 248.71]

[73] Duffy above n 11, 165, 195-196, 200

[74] See, e.g. *Legal Profession Uniform Conduct (Barristers) Rules 2015* (NSW) r 120; Róisín Annesley, *Good Conduct Guide: Professional Standards for Victorian Barristers*, (Victorian Bar, 2006) 77-9 [5.23]–, [5.24]. If there is a conflict between the litigant's interests and the instructing lawyer's interests, the barrister must advise the client of this in writing: The Victorian Bar Incorporated, *Practice Rules: Rules of Conduct and Compulsory Continuing Professional Development Rules* (at 22 September 2009) Rule 73. An alternate view might be a 'stakeholder' approach where in some cases the barrister acts for the solicitor but the client is a 'stakeholder'.

[75] Ibid. See also Vicki Waye, (2018) "The initiation and operations phase of the litigation funder – class action law firm relationship: An Australian perspective" (2018) 60 (2) *International Journal of Law and Management* 595.

[76] Ibid 616.

ALRC 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).

Submission

This proposal seems sensible though may require further information about and consideration of the detail and variety of actual and potential funding mechanisms.

ALRC 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.

Submission

There are quite a number of issues for lawyers in this area (see Annexure One) so that accreditation is desirable as is some clarification, guidance or suggested policy from national and state law societies on those issues.

ALRC 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.

Submission

Such interests, if material, could incentivise the lawyer to act in the funder's interests rather than the litigant's interests. This could be adverse to the litigant's interests unless it can be shown that the litigant's and funder's interests are completely harmonised (which they will not always be[77]). Otherwise the lawyer has an obligation as a fiduciary to avoid conflicts with the litigant's interests.[78] It probably follows therefore that lawyers and funders owning substantial or material interests in each other by way of equity or otherwise may not generally be in the litigant's interest. If it did occur it would require in all cases, full disclosure to the litigant (Proposal 4–6 may go some way toward such disclosure) followed by the litigant's informed consent, including possible independent legal advice on the issue.[79] If the latter

[77] Though they may be more harmonised if both have similar duties to the litigant. A statutory duty of good faith of funder to litigant would obviously assist here in matching somewhat the lawyer's fiduciary duties to the litigant.

[78] Law Council of Australia, *Model Rules of Professional Conduct and Practice* (at March 2002) r 8.2.

[79] In RG 248 ASIC suggests that disclosure may solve this dilemma but does not go so far as to require a fully informed consent and/or independent legal advice. ASIC expects that there will be either: (a) independence between the funder, lawyers and members; or (b) if there is no such independence, the relationship will be disclosed to members: *RG 248*, above n 72, 23 [248.81] (interestingly the same analysis could be made about relations between lawyers and insurers but there does not appear to be similar regulation of this relationship). It

occurs it would satisfy the requirements of the law of equity (though economic agency dilemmas may remain[80]).

The issue is whether this existing fiduciary law is adequate or not.[81]

ALRC 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.

Submission

Once again parity between the position of insurers and litigation funders is an issue here as there is a question as to why plaintiff funding agreements should be disclosed if defendant (insurance) funding agreements are not. Subject to this observation it is submitted that a power of a court to order disclosure of a funding agreement or a relevant insurance policy should be considered which would be a power of a court to order, of its own motion or on application by a party, disclosure to the court or to any party, on any terms the court deems fit.

Special circumstances may or may not exist in relation to the situation of arbitrations and no submission is made on that point.

ALRC 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.

Submission

The submitter generally supports this proposal though finding a formula for a short and simple explanation of such matters that does not confuse the potential litigant may not be a simple matter.[82]

5. Commission Rates and Legal Fees

ALRC Proposal 5–1

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is likely that equity would require more than disclosure by the lawyer and that fully informed consent of the litigant would be needed to avoid the lawyer breaching his or her fiduciary duties.

[80] In agency terms it does not eliminate the problem but merely makes it known and consented to. See Duffy above n 11, 191-193.

[81] Again, cross ownership between insurance companies and law firms would probably raise similar issues.

[82] It might be observed that, in theory, an insured should receive a similar notice from its lawyers given similar potential for conflict of interest. On the other hand such 'consumer protection' measures may be less relevant in that sort of context given that insured's may be repeat players in litigation.

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.*

Submission

This submission will canvass the issue of contingency fees generally as well as responding to specific suggestions.

The argument against contingency fees – conflict of interest

The prohibition on contingency fees seems to be based on the notion that percentage contingency fees may create a conflict between the duty to the court and the duty to the client by which there is a temptation to prefer the obligation to the client over the obligation to the court because of the lawyer's personal interest in the outcome. The danger is said to be that ethical standards in a case may be 'undermined with a view to achieving a favourable outcome.'[83] It can be noted however that this 'outcome incentive' argument logically applies not just to percentage contingency fees but to any contingency fee including (a) a speculative 'no win no pay' fee (involving the payment of normal fee in the event of success and no fee in the event of loss) and (b) an uplift fee (involving the payment of a greater fee on success than on loss). The conflict may of course be less in these cases as the fee is usually less than a percentage contingency fee however the principle remains the same.[84] It is noted that no win no pay fees and uplift fees are legal in Victoria.

Some of the arguments about conflict in third party litigation funding may also apply to contingency fees. The potential conflict between a litigant who wants to go to trial and a lawyer who wants to settle is one (though it could be argued that 'time charging' may sometimes induce the inverse potential conflict with the lawyer wanting to go to trial and the litigant wanting to settle – see below). This conflict might also be addressed by permitting a reasonable excess on the adverse costs indemnity as discussed above.

The potential conflict of lawyers' duties to a funder conflicting with lawyer's duty to the litigant – itself arising from the fact that the lawyer has a fiduciary duty to the litigant but the funder does not – will not arise here in the exactly same manner as there is no non-fiduciary relationship of a funder involved. That is, the funder (the lawyer) in this case will have a fiduciary relationship to the litigant. This is not to discount the potential conflict between the

[83] VLRC above n 67, 685.
[84] Australian Government Productivity Commission *Access to Justice Arrangements* Inquiry Report Volume 2 No. 72, 5 September 2014, 614.

lawyer's duty to the client and the lawyer's personal financial interest, however this is a perennial dilemma which cannot be completely eliminated and will rely on lawyers' professionalism,[85] honesty, ethics, reputation and overriding duties[86] to the court.[87]

The arguments for contingency fees - increased competition and reduced duplication of expense

Lifting the ban on contingency fees in this area may bring more competitive pressure on lawyers and litigation funders leading to greater efficiencies and lower costs. Given some possible duplication in functions between the lawyer and the funder (e.g. reviewing evidence and assessing the merits), it may also reduce overall costs.

Better competition is subject to the proviso that asymmetric information (i.e. unduly complicated charging agreements which legal consumers do not understand) does not make it difficult to compare costs. Asymmetric information might be remedied somewhat by Proposal 3–2 under which a litigation funding licence would require third-party litigation funders to, inter alia, ensure that all communications with class members and potential class members are clear, honest and accurate. This would need to be made to apply to communication of litigation funding charges. There would need to be similar provisions in relation to solicitors' contingency fees as for litigation funders' charges so that the two could be easily compared. There would need to be disclosure of these matters to litigants *before* they decide to contract with a lawyer or litigation funder if litigants are to be able to compare same and there is to be real competition.

Other general issues for contingency fees

Different types of billing

In relation to whether contingency fees should be allowed it can be observed that, though there is the potential for abuse with contingency fees, there is also the potential for abuse in most other types of charging arrangements. For instance time charging creates incentives to spend more times on tasks than may be strictly necessary and may create incentives to 'stretch out' proceedings.[88] Fixed fee arrangements may need to be extremely complicated to deal with the exigencies of litigation and may thus be hard for legal consumers to understand. They may in some cases over or under remunerate depending on those exigencies of litigation.

Thus at the end of the day all types of charging may be abused so that whatever fee arrangement is used, reliance will be placed on lawyers' professionalism, honesty, ethics,

[85] See for instance Vivien Holmes, Tony Foley, Stephen Tang and Margie Rowe, 'Practising Professionalism: Observations from an Empirical Study of New Australian Lawyers' (2012) 15(1) *Legal Ethics* 29.
[86] Duffy above n 11, 186.
[87] Indeed the potential conflict issue arguably arises every time a lawyer drafts a bill as a lawyer is not permitted to charge a client for this – consistent with the view that a lawyer realistically cannot be seen as acting only for the client and oblivious to his/her own interests when so drafting. See Law Society of NSW *How solicitors charge their clients* https://www.lawsociety.com.au/for-the-public/going-court-and-working-with-lawyers/solicitor-client-relationship/how-solicitors-charge-their-clients. See also Victorian Legal Services Board and Commissioner Site http://lsbc.vic.gov.au/?page_id=4319.
[88] VLRC above n 67, 686. See also Michael West, 'Corporate undertaker: the new hip career' *The Sydney Morning Herald* (online) 29 October 2012 http://www.smh.com.au/business/corporate-undertaker-the-new-hip-career-20121029-28f1z.html.

reputation and overriding duties to the court (see above). The latter may be the most important given that lawyers tend to face an unavoidable prima facie conflict in relation to their interest in maximising fees and their clients' interest in minimising fees (though the former is no doubt subject to other restraining factors such as competition and reputational issues). To the extent that restraining factors fail then the focus must be on whether the criteria and systems for assessing fitness for admission to and removal from the profession are adequate.

Contingent fees for witnesses

Whether or not lawyers contingency fees create a conflict for lawyers representing a party and presenting that party's case to a court, witness contingency fees do appear to create a conflict of interest for persons giving evidence to a court – in that the person's remuneration can be partly dependent on the content of their evidence. Thus a general ban on witness fees that are in any way contingent upon outcomes seems overdue (and there is no reason that this should be limited to class actions or funded actions).[89] This issue may have some relevance to the debate over permitting lawyers' contingency fees also as lawyers are often required to give affidavit evidence on minor matters, and in class and major actions, sometimes on more significant matters (e.g. communication with group members,[90] settlement schemes,[91] reasonability of settlement[92] and/or costs[93]). Lawyers giving evidence then, might be a barrier to contingency fees but were they not to do so (which may or may not be practical), one of the arguments against contingency fees may fall away.

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.

Submission

This would seem to be a sensible limitation not least because such 'hybrid' arrangements may be complex and difficult for a litigant to understand.

Contingency fee cannot be recovered in addition to professional fees for legal services charged on a time-cost basis.

Submission

This would seem to be a sensible precaution against double billing for the same work.

[89] See discussion in VLRC above n 67, 510. At present a party to a civil proceeding may apply to the court for an order that an expert witness retained by any party to that proceeding disclose all or specified aspects of the arrangements under which the expert witness has been retained to (a) the court; and (b) all the parties to the proceeding: *Civil Procedure Act 2010* (Vic) s65P. There is obviously also the prohibition on general corruption of witnesses contained in s37 of the *Crimes Act 1914* (Cth) in the form of giving a witness property or a benefit of any kind in return for giving false testimony or withholding true testimony.
[90] *King v AG Australia Holdings Ltd (formerly GIO Australia Holdings Ltd)* [2002] FCA 1560 (16 December 2002).
[91] *King v AG Australia Holdings Ltd (formerly GIO Australia Holdings Ltd)* [2003] FCA 1420.
[92] *Inabu Pty Ltd v Leighton Holdings Limited (No 2)* [2014] FCA 911 (25 August 2014).
[93] *Kelly v Willmott Forests Ltd (in liquidation) (No 4)* [2016] FCA 323 (5 April 2016) .

Under a contingency fee agreement, solicitors must advance the cost of disbursements and indemnify the representative class member against an adverse costs order.

Submission

Providing an indemnity may increase potential conflicts when giving advice as to whether to accept a settlement however it is probably still a reasonable requirement. The potential conflict might be reduced where there is an excess on the indemnity for adverse costs (see above).

Other Safeguards

If contingency fees were to be introduced, some safeguards should include court approval of all contingent fees[94] (see below) by reference to statutory guidelines which should include fairness and reasonableness, some proportionality with work (reasonably) performed and a sliding scale of permissible amounts/caps to prevent unreasonable profiteering.[95]

There arguably should also be a ban on remuneration of expert witnesses (and possibly all witnesses) being in any way contingent on case outcome. This issue may require further consultation however as it is somewhat outside the terms of reference.

ALRC 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.

Submission

As stated above this is supported though the timing of such approval is not alluded to in the proposal. Presumably lawyers will wish to have such approval given near the commencement of proceedings rather than at the conclusion. This is discussed further under 5-3 below.

ALRC 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?

No submission

[94] VLRC above n 67, 686.
[95] Ibid. A range of other safeguards are also suggested in the VLRC report and should be considered.

ALRC 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.

Submission

This would seem to be an appropriate overarching power but again the issue of when it is exercised may need discussion.

It is noted that in funded insolvency actions (funded claims by companies in liquidation), approval of funding agreements pursuant to s477 (2B) of the Corporations Act is often applied for at commencement of litigation.[96] This would increase commercial certainty for lawyers and funders. On the other hand flexibility and fairness might weigh on the side of the power to reject, vary or set rates being exercisable at the settlement approval/conclusion of proceedings stage. It may be that courts should be empowered to give a preliminary approval which will apply in the absence of compelling reasons to vary.

A possible provision may be:

Review of funding fee

(1) In any proceeding under this Part that is funded by a third party litigation funder or a law firm, the Court has power to review the appropriateness and reasonableness of any funding fee, commission, contingency fee or other charge, and if inappropriate and unreasonable, to vary that funding fee, commission, contingency fee or other charge.
(2) Without limiting the generality of (1) the Court may at any stage in the proceeding make a preliminary order approving a proposed funding fee, commission, contingency fee or other charge which approval will stand in the absence of the Court making any further order under s(1)
(3) The court may make an order in relation to (1) or (2) on application by a party or on its own motion.
(4) In exercising the power in (1) and (2), the Court will have regard to any matters that it considers are relevant to the appropriateness and reasonableness of the funding fee, commission, contingency fee or other charge.

ALRC 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*

[96] Re *ACN 076 673 875*(2002) 42 ACSR 296 *Stewart, in the matter of Newtronics Pty Ltd* [2007] FCA 1375

- *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%?*

Submission

Though these suggestions have some perceived appeal it may be that they would in practice be somewhat inflexible and prescriptive. It could be that these could be enacted as guiding principles to be considered in the court's approval or variation of fees discussed in relation to Proposal 5-3 set out above.

A formulation continuing from the above possible provision might be:

> (4) In exercising the power in (1) and (2), the Court will have regard to any matters that it considers are relevant to the appropriateness and reasonableness of the funding fee, commission, contingency fee or other charge which may include whether the funding fee, commission, contingency fee or other charge should be:
>
> > (i) subject to a cap that limits the proportion 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 and;
> >
> > (ii) limited so that the maximum proportion of fees and commissions paid from any one settlement or judgment sum is 49.9%

ALRC 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?

Submission

No submission. This question may require corporate finance evidence from funders and lawyers.

ALRC 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?

Submission

There are no shortage of matters where claims may appear to be meritorious but are currently largely untried and where recovery issues are somewhat uncertain (claims for misconduct, fraud or misleading statements by overseas based websites are an obvious example). Seed funding to break new ground in these areas is something that should be considered.

6. Competing Class Actions

ALRC 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.*

Consumer choice

Before considering the common fund doctrine it is submitted at the outset that a law prescribing that all class actions *must* be open class and *must* proceed under the common fund doctrine seems unduly prescriptive and limiting of consumer choice and contractual freedom. This is not to say that providing that actions *may* be open class and *may* utilise the common fund doctrine (the current position) would be not appropriate where it can be demonstrated to the court that this is the best way to go.

The right to a closed class

The right of a plaintiff to commence closed class proceedings has been noted by a number of commentators as has the utility of that right. It has been suggested that:

- There is an express legislative conferral on a class representative of the discretion to exclude some potential claimants from the ambit of the claim[97] and that the language of s33(C(1)) clearly envisages a group being limited to some subclass of the universe of putative claimants.[98]
- The *Federal Court of Australia Act 1976* (Cth) ('the Federal Court Act') does not seek to dictate the manner in which the representative group is defined/described and which of the potential claimants are included in that group.[99]
- An action limited to a small group of defined individuals with readily provable and quantifiable losses may often be easier to conduct, less expensive and easier to settle than a large case involving substantially larger numbers of group members.[100]
- It may be appropriate to bring a class action for public interest reasons as a test case in the hope that this will bring an end to the conduct in question, rather than for the purpose of recovering compensation or damages for all those affected.[101]

[97] Vince Morabito, 'Class Actions Instituted only for the Benefit of the Clients of the Class Representative's Solicitors' (2007) 29(5) *Sydney Law Review* 5, 13. This point appears clear from the decision of the Full Federal Court in *Multiplex Ltd v P Dawson Nominees Pty Ltd* (2007) 164 FCR 275.
[98] Grave, Adams and Betts above n 56 [13.590].
[99] Morabito above n 97.
[100] Peter Cashman, 'Class actions on behalf of clients: Is this permissible?'(2006) 80 *Australian Law Journal* 738, 738.
[101] Ibid 740

- There may also be circumstances where potential claimants may have similar claims against one or more 'common' defendants and also possible separate individual claims against other non-common defendants who may not be joined in any class action proceeding, in which case 'it may be prudent for the claim(s) of each potential claimant to be evaluated individually and for various legal avenues to be considered'.[102] This 'may result in any class action being limited to persons who have been individually advised, who consent to the commencement of class action proceedings on their behalf and who instruct the one firm of solicitors.'[103]

Removing the closed class option, forcing a plaintiff to run their case on an open class basis and staying all competing actions certainly has some uncertainties:

- What is such a plaintiff's responsibility to sue all possible defendants and utilise all possible causes of action and how does this affect the court's discretion in choosing a particular plaintiff's claim (obviously in conventional litigation the court need not involve itself in these questions as a plaintiff has the discretion to plead their case as they see fit[104]). If there is a single open-class court-mandated action who makes decisions about these issues, including, for instance, the decision not to sue a potential defendant or not to pursue a particular cause of action? Must the court choose the case that joins all possible defendants and utilises all possible causes of action?
- Forcing a plaintiff to run an open class clearly brings in some of the arguments that have been made about forced 'group expansion' including concerns about (a) forcing a representative party to take on the responsibility of conducting an action on behalf of a larger class than they may wish to agree to[105] and (b) possibly also making settlement more difficult, particularly where there is uncertainty as to the number of people within the expanded class definition and difficulty in determining how many will ultimately come forward and be able to establish their individual entitlements.[106]

There is also the continuing problem of unrepresented group members (or at least group members who never come forward) and the principle of a litigant being able to choose their lawyer which is discussed further below.

<u>Open class/common fund</u>

Whilst mandated open classes would appear to widen the access to justice and public interest aspects of class actions it needs also to be recognised that this combination of proposals, especially to the extent that common funds are compelled by statute, tends to amount to substantial state intervention and prescription by the legislature and the judicial arm in private civil litigation in relation to the questions of:

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[102] Ibid.
[103] Ibid.
[104] In England, the right to plead in civil matters seems to have moved subtly from the state (from 'enrolling clerks of courts') to the private legal profession (the bar) during the thirteenth and fourteenth centuries. This first occurred through the bar providing enrolling clerks with drafts of entries that they desired the clerks to make on the court plea rolls. This took place first in common law courts and then in Chancery. See Theodore Pluckett, *A Concise History of the Common Law*, (Fourth Edition Butterworth and Co 1948) 381-385.
[105] VLRC above n 67, 527
[106] Ibid 528

- who is a litigant;[107]
- who will be the lawyer for a litigant;[108]
- how litigants and their lawyers are funded;
- contractual relationships between lawyer and litigant (or lack thereof);
- the statutory creation of other less certain non-contractual and possibly non-fiduciary types of relationships between lawyers and litigants;
- the division and application of litigants' damages.[109]

This is not necessarily a criticism of the proposal but it is something that obviously needs to be recognised.

There may thus seem to be some uncertainties in the common fund doctrine as regards the traditional contractual and fiduciary relationship of the lawyer to his/her client given that under the proposal there may be more group members who will have no solicitor–client relationship with the lawyer in the traditional sense.[110] Whilst it might have been considered that an incentive may remain for the lawyer to recruit clients so as to increase the likelihood that the lawyer and lead plaintiff client will not have their action stayed, numerosity of clients has recently been somewhat discounted as a relevant factor in the court's decision in this regard.[111]

It may be that lawyers will retain some incentive to recruit litigants in the second stage of proceedings so as to act in relation to proof of their individual issues however even this may decline under the common fund doctrine given reduced requirements for a litigant's contractual consent to deduct costs or commissions combined with the ability to get individual issue evidence from a defendant (such as defendant records as to shareholders' holdings and dealings in a shareholder class action) without needing to take instructions from the litigant.

It remains to be seen how this will play out, but if lawyers have no incentive to enter fee and retainer agreements with group members in the first stage of the proceedings (the trial of the common issues) it is not clear why they would do so, particularly if such an agreement heightens their duties to group members. Yet there may be interesting questions as to the fairness of deductions being made from group members' individual damages awards under Federal Court Act s33ZJ for lawyer's costs (not to mention funders' costs) on the common issues if lawyers and funders have had no contact or engagement with and avoid provision of any personal service to those group members.

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[107] Though this obviously derives mainly from the original decision to proceed with an opt-out rather than an opt-in regime in the original enactment of Part IVA of the *Federal Court Act of Australia Act 1976* (Cth).
[108] At least in the common issues stage of the case.
[109] Which damages are litigants' property deriving from their original property in causes of action as proprietary choses in action: see M Duffy, 'Is a cause of action a castle? Statutory choses in action as property and s51 (xxxi) of the Constitution' (2018) *Melbourne University Law Review* (forthcoming).
[110] This has of course been the case since the commencement of Part IV given that the opt out procedure means that persons who have never come forward to a solicitor or anyone to make a claim can nevertheless be group members.
[111] In *Perera v GetSwift Limited* [2018] FCA 732, Lee J considered that how many litigants had entered funding agreements with a litigation funder and retained the recommended lawyer was not a matter which should be given real weight in the court's choice between lawyers ([210]-[213]).

Litigants may or may not have incentives to contract with class lawyers or funders in this situation. They will no doubt balance a desire for personal representation with possible incentives to 'free ride'.

All of this probably means more unrepresented group members and there has to date been considerable uncertainty as to what a lawyer's duties to non-client group members actually are.[112] For instance there are statutory obligations[113] of lawyers to provide clear and timely advice to enable the client litigant to understand the relevant legal issues and to inform them about alternatives to fully contested adjudication of the case. It is far from clear that these obligations will apply to group members who have not signed a retainer agreement with the lawyer yet the lawyer is still representing such people in a real sense.

If there are larger numbers of litigants who go through the court process in the common issues stage without any clear specific relationship to a lawyer this must, at a minimum, heighten the court's responsibility to protect those unrepresented group members. The common fund doctrine certainly gives great protection[114] in the main area where litigants and their lawyers' interests can conflict – legal costs. Yet, besides otherwise generally giving procedural fairness (especially through notices), there is only so much that a court can do to protect (but obviously not 'represent') litigants on one side of a piece of litigation (contradictors can be appointed on specific issues but these do not represent group members generally throughout the proceeding).

Further, under such a regime, the rights of unrepresented group member to give instructions as to the framing and prosecution of claims that will affect that person's rights (see above) seem to be non-existent – their only right being to opt out of the case. This may be an unavoidable aspect of 'mass justice' but it is a consideration that may loom larger with common funds.

It follows that the common fund doctrine, though having certain benefits, is also a step into somewhat uncharted waters for the judicial system.

Competing class actions

Further, a decision by a court allowing one proceeding (with presumably one set of lawyers acting) to proceed while staying all others is significant in other ways and raises a number of matters that deserve consideration.

In *Perera v GetSwift Limited* [115] ('*GetSwift'*) Lee J noted that the focus in this area is on how the Court deals with competing commercial enterprises (lawyers and funders) seeking to use the processes of the Court for profit and the Court's desire to ensure the use of those

[112] It would seem that a lead plaintiff may at least have a tortious duty of care to group members given that s/he must adequately (competently) represent their interests though this may be transmogrified into a duty of the lead plaintiff's lawyer to do this given that the lawyer is, *de facto*, in charge of the proceedings. Fiduciary duties have also been suggested: see Grave, Adams and Betts above n 56 [6.255]. See also Vince Morabito, 'Judicial Supervision of Individual Settlements with Class Members in Australia, Canada, and the United States' (2003) 38 *Texas International Law Journal* 663, 670-678.

[113] [7.1] and [7.2] *Australian Solicitors Conduct Rules* 2015 made pursuant to the Legal Profession *Uniform Law Application Acts 2014.*

[114] *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148 [103]

[115] [2018] FCA 732

processes for their proper purpose.[116] The Court is informed by considerations including: (a) the statutory mandate to facilitate the just resolution of disputed claims according to law and as quickly, inexpensively and efficiently as possible; and (b) the furtherance of the Court's supervisory and protective role in relation to group members.[117]

Economic perspective

The first consideration in *Getswift* of expense and efficiency clearly imports an economic issue. The other aspect of an economic analysis in this situation may be the question of the state awarding to such a commercial enterprise something approaching a monopoly position in the litigation.

Whilst it is the case that efficiency can derive both from economies of scale and lack of duplication (such as occurs in a single proceeding), it can also arise, somewhat conversely, from competition between players (such as might occur in multiple proceedings). This tension is a perennial dilemma in economics and competition theory.

Yet the state awarding of a monopoly is not necessarily inefficient nor is it anything new. It may be that, given the problems and inefficiencies of the other procedural alternatives (consolidation proceedings, permanent stay of proceedings, order declassing some of the proceedings, order closing the class in several proceedings and allowing a joint trial of the proceedings[118]) and the problems of 'chain of command' and decision making, a claim by a litigant can be described in economic terms as having elements of 'natural monopoly'.[119]

A common solution to the problem of natural monopoly is in fact *ex ante* bidding to award the monopoly franchise to the most efficient single bidder.[120] However it should also be noted that some economics scholars advocate recurrent short term awarding of such monopoly franchises.[121] In the litigation context this might suggest that the awarding of the action to one plaintiff and one firm could be periodically reviewed. This may itself have certain inefficiencies however it probably should remain in the court's power to do so under any legislative reforms.[122]

It can also be noted that at least one distinguished (now former) judge has suggested a role for a 'litigation committee' appointed pursuant to s33ZF with whom a judge could consult in the 'auction' or 'tendering' process of awarding the litigation to a particular firm.[123] Analogies might include 'special litigation committees' which operate in the United States in the context of derivative litigation – they are intended to be independent committees of experts appointed to assess whether actions have merit (another analogy closer to home may

[116] Ibid [3], [104].
[117] Ibid.
[118] *Perera v GetSwift Limited* [2018] FCA 732 [46]. A 'test case' may be another option but may require consent to be effective.
[119] I.e. a market situation where technical factors preclude the efficient existence of more than one provider: G Bannock, R E Baxter and E Davis, *Penguin Dictionary of Economics* 291.
[120] Oliver E Williamson, *The Economic Institutions of Capitalism* (Free Press 1985) 40, 326, 327.
[121] Ibid 332-347.
[122] As it probably can be now under *Federal Court of Australia Act 1976* (Cth) s33T and s33ZF.
[123] See *Kirby v Centro Properties Limited* [2008] FCA 1505 (per Finkelstein J). See also M Duffy, 'Class Representation: Choosing the best lawyer for the case' (2009) 83(05) *Law Institute Journal* 31.

be the committee of inspection or committee of creditors to advise an insolvency practitioner[124]).

Such a committee might have an initial role in the awarding of a case to a firm but also an ongoing role in monitoring that award. The need for ongoing independent monitoring also appears to have been the basis for the appointment of a referee or independent costs consultant to monitor legal costs in *GetSwift*[125]

Lastly, it is perhaps less clear that 'natural monopoly' exists after the common issues stage and that there may be benefits of competition between and indeed multiple representation by lawyers at the individual or sub-group issues stage (which may also be a 'settlement administration' stage as noted below) of the proceeding. This issue also may arise in the context of whether the court should approve settlement schemes that award monopolies to lawyers or at least do not allow for some appropriate level of competition within the administrative scheme.

Certainly the awarding of a monopoly to a particular firm and funder should be subject to ongoing liberty to apply of group members and review by the court. Though upsetting prior fee arrangements with a lawyer or funder can have problems and can be inefficient, so can undue bilateral monopoly that can exist under such arrangements.[126]

ALRC 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.

Submission

Insofar as Proposal 6-1 is incorporated in legislation then its implementation may be enabled by case management procedures that are within the power conferred by *Federal Court of Australia Act 1976* (Cth) s59. The proposal does not outline details of the procedure so it is difficult to make any further comment or submission.

ALRC 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?

Submission

[124] *Corporations Act 2001* (Cth) s 436F and s548.
[125] [2018] FCA 732 [226]-[228]
[126] As to the economic aspects of early or premature termination of a lawyer or funder agreement see Duffy above n 11, 197-198. See also generally Williamson above n 119, 53-4.

Though forum shopping is a concern, competition theory might also favour choice (though the application of competition theory to courts should be used with caution).

A better approach might then be that a cross-vesting judicial panel be established as has been put forward by the VLRC.[127]

Lastly, the proposal to amend the Corporations Act may in any event face certain constitutional uncertainties including doubt as to whether the referred power in *Corporations Act 2001*(Cth) s 4(5) is wide enough to cover such an amendment. If not, this would appear to require a separate referral of power from the states.

7. Settlement Approval and Distribution

ALRC 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.

Submission

The submitter supports this proposal but suggests that this power may already exist under *Federal Court of Australia Act 1976* (Cth) s33V or s33ZF. To the extent it does not exist then this may require a legislative provision as it would seem unlikely that the Practice Note can confer a power.

ALRC 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?*

Submission

This raises similar issues to ALRC Proposal 6–1 including economic competition issues and may involve a substantially similar process of judicial decision after an 'auction' or 'tender' process (which might also involve the usage of a litigation committee as discussed above).

ALRC Question 7–2

[127] Victorian Law Reform Commission, *Access to Justice – Litigation Funding and Group Proceedings* (Report 2018) Recommendation 12. See also Vince Morabito, *An evidence-based approach to class action reform in Australia: Competing class actions and comparative perspectives on the volume of class action litigation in Australia*, 11 July 2018, 22.

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?

Given that it is said that 'sunlight is said to be the best of disinfectants'[128], amounts and some detail of plaintiff legal costs and of funding commissions should be disclosed in all court approvals of settlements unless the court finds a compelling reason not to do so. [129] There should be a general presumption that these amounts will be published in reasons for settlement approval.[130] Given the large number of funded class actions which justifiably complain of the evils of nondisclosure to securities markets it would be inconsistent to generally allow nondisclosure of fees to legal and litigation funding markets. Better disclosure will tend to allow for more efficiency in markets for legal services and litigation funding.

There may of course be a similar argument for disclosure of defendant's legal costs as well. Given however that plaintiff legal costs are usually approved as part of the settlement and are to some extent an involuntary exaction through judicial power while defendant legal costs do not usually have this character (unless of course a plaintiff is to pay a defendant's costs which could occur where a misconceived suit was discontinued) and given that disclosure is not the practice in ordinary litigation, it is not suggested that there should be a presumption of disclosure of defendant legal costs at this stage though the issue could be monitored.

A possible amendment to s33V might be to insert s 33V(3) as follows:

> (3) In giving an approval under this section the Court will normally publish in its reasons the amount of any approved third party funding commission or fee and approved plaintiff legal costs unless the Court determines that there are compelling reasons not to do so.

8. Regulatory redress

ALRC 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.

Submission

This proposal is generally unobjectionable insofar as such a scheme would appear to be similar to the Australian Financial Complaints Authority (AFCA) though attempting to aggregate common issues in complaints. Some issues do arise however. It may be that an individual complainant would have little incentive to make themselves a representative of

[128] Louis Brandeis, *Other People's Money-and How Bankers Use It*, Cosimo Classics New York (first ed 1914, 2009).
[129] Federal Court Class Actions Practice Note (GPN-CA) 25 October 2016 contemplates orders for confidentiality of legal costs if appropriate. See [15.4(b)].
[130] Brandeis above n 128.

other complainants. It may also be that a defendant such as a corporate defendant would have little incentive to give redress unless compelled to do so by law (e.g. to do so might, for instance, breach directors duties). Lastly, insofar as compulsion is the answer to the second point it may be that such an authority would need to have judicial power which would effectively mean that it would have to be established as a court and may then merely duplicate existing courts and create jurisdictional complexities.

ALRC Question 8–1

What principles should guide the design of a federal collective redress scheme?

See above.

ANNEXURE ONE

Some possible conflict of interest issues in litigation funding [and possibly insurance] for research, discussion and eventual guidance from the Australian Law Societies

1. Does a lawyer who is paid by a litigation funder [or insurer] and has an agreement with the litigation funder [or insurer] under which the latter has the right to give the lawyer instructions in connection with funded proceedings involving a funded [or insured] litigant owe a fiduciary duty to the litigation funder [or insurer]?
2. If that lawyer also acts for a litigant in the funded proceeding does the lawyer have any conflict of interest where the interests of the litigation funder [or insurer] diverge from those of the litigant?
3. Where there is an agreement between the funder [or insurer] and lawyer where it is agreed that the relationship is not that of lawyer/client, do any fiduciary duties of the lawyer to the funder [or insurer] apply?[131]
4. If there is a relationship between the funder [or insurer] and the lawyer in which the lawyer has incentives to secure further work from the funder [or insurer] or there is a financial relationship between lawyer and funder [or insurer] whereby the lawyer is financially incentivised to act in the funder [or insurer]'s interests, does this put the lawyer in a position of potential conflict where the lawyer's interests diverge or conflict with the litigant's interests?
5. Do situations where there may be a divergence of interest between the funder [or insurer] and the litigant causing a possible conflict for the lawyer include:
    a. Different views of the funder [or insurer] and litigant on the reasonableness of terms of a funding [or insurance] agreement and whether the litigant should sign it?
    b. Different views of the funder [or insurer] and litigant on the reasonableness of terms of a settlement proposal in a proceeding?
6. How far, as a fiduciary, is a lawyer is required to avoid conflicts[132] and how far can liability be avoided in equity if the conflict is fully disclosed to the client litigant and a fully informed consent is obtained? [133] and:
    a. What is required for a fully informed consent?

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[131] It is noted a lawyer may not be permitted to contract out of duties of care and diligence if services are provided. See for instance s7.2.11 of the *Legal Profession Act 2004* (Vic) which provides that a lawyer must not make any agreement or arrangement with a client to the effect that the lawyer will not be liable to the client for any loss or damage caused to the client in connection with legal services to the client and that any such agreement is void. .

[132] Rule 8.2 of the Law Council of Australia *Model Rules of Professional Conduct and Practice* provides that a practitioner must avoid conflict of interest between two or more clients of the practitioner or of the practitioner's firm.

[133] *Parker v McKenna* (1874) LR 10 Ch App 69; *Commonwealth Bank of Australia v Smith* (1993) 42 FCR 390. Fiduciary duty may thus be attenuated in equity but it appears that it may be more difficult for the lawyer to contract out of other duties that could still be breached (at least in Victoria - see Section 7.2.11 *Legal Profession Act 2004* (Vic) – there does not appear to be an equivalent provision in NSW).

b. What circumstances are relevant and in what way[134]?
c. Is there a need for independent legal or other advice (i.e. advice from another lawyer)?[135]

7. Does the briefing of Senior Counsel by a lawyer who perceives a conflict in any of the above circumstances relieve a conflict if any of the circumstances above exist? If it does not, what other cost effective and expeditious alternatives might there be?
8. Apart from conflicts is it also necessary for a lawyer to consider, in deciding to act in a matter where a relationship with a funder exists to have regard to whether a fair minded reasonably informed member of the public would conclude that the proper administration of justice requires that the lawyer not act in the interests of the protection of the integrity of the judicial process and the due administration of justice, including the appearance of justice?[136]

[134] See *Maguire v Makaronis* (1997) 188 CLR 449, 466-7. See also *DPC Estates Pty Ltd v Grey and Consul Development Pty Ltd* [1974] 1 NSWLR 443; *Chan v Zacharia* (1984) 154 CLR 178.
[135] See *Woods v The Legal Ombudsman* [2004] VSCA 247.
[136] See *Kallinicos v Hunt* (2005) 64 NSWLR 561; *Bolitho v Banksia Securities Limited* (No 4) [2014] VSC 582