MinterEllison

30 July 2018

Australian Law Reform Commission
GPO Box 3708
Sydney NSW 2001
Email: class-actions@alrc.gov.au

Dear Commissioner

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

1. Introduction

1.1 Thank you for the invitation to provide submissions in response to the Australian Law Reform Commission's (Commission) discussion paper *Inquiry into Class Action Proceedings and Third-Party Litigation Funders* dated June 2018 (**Discussion Paper**).[1]

1.2 We provide our Submission in response to the questions and proposals raised in the Discussion Paper although we do not address them all.

2. Introduction to the Inquiry

> **Proposal 1–1** The Australian Government should commission a review of the legal and economic impact of the continuous disclosure obligations of entities listed on public stock exchanges and those relating to misleading and deceptive conduct contained in the Corporations Act 2001 (Cth) and the Australian Securities and Investments Commission Act 2001 (Cth) with regards to:
>
> - the propensity for corporate entities to be the target of funded shareholder class actions in Australia;
> - the value of the investments of shareholders of the corporate entity at the time when that entity is the target of the class action; and
> - the availability and cost of directors and officers liability cover within the Australian market.

2.1 MinterEllison had carriage of the drafting of this section of Law Firms Australia's Submission on Proposal 1-1 so there is likely to be some overlap.

2.2 We support this proposal, as do many of our clients. While there has examination of the issues raised by the increasing number of funded shareholder class actions commenced in Australia over the past twenty-five years,[2] there has been no in-depth, empirically-based research examining the impact of the *Corporations Act* continuous disclosure and misleading or deceptive conduct regimes on corporate Australia when coupled with exposure to an increasing number of funded shareholder class actions.

2.3 As the Discussion Paper observes, the Commission did not anticipate the developments in the law relating to class actions that have occurred since 1998.[3] Nor did the drafters of Australia's continuous disclosure and misleading or deceptive conduct laws. We agree with the need to

[1] Australian Law Reform Commission, *Inquiry into Class Action Proceedings and Third-Party Litigation Funders,* Discussion Paper (2018) (**Discussion Paper**).
[2] See e.g. Vince Morabito, *The First Twenty-Five Years of Class Actions in Australia: An Empirical Study of Australia's Class Action Regimes, Fifth Report* (July 2017).
[3] [1.84] of the Discussion Paper.

regulate market disclosures, and the need to regulate them by reference to high standards of accuracy and timeliness, but none of the designers of Australia's market disclosure laws foresaw today's 'model' shareholder class action, how market disclosure laws would be used in that context, with, among other things, a serious impact on the price, and the availability, of directors and officers liability (**D&O**) insurance.

2.4 It is therefore an open question as to whether in the context of shareholder class actions these laws are best serving shareholders and Australia's investment environment more generally.

2.5 Such a review might, for example, canvas the compliance burden impact of the laws (again in the context of a risk that a shareholder class action might be commenced as a result of boards 'getting it wrong'). Relevantly, it has been said that Australia's continuous disclosure laws "*are best practice, if one is not actually a director*." The risk of being targeted in a shareholder class action is an increasingly considerable concern of boards and executives of listed entities facing a dilemma as to whether there is a continuous disclosure requirement concerning a particular piece of information.

2.6 While, again, it is hardly inappropriate for Australian boards of listed entities to consider their market disclosure obligations on an ongoing basis, the guidance available to boards for identifying whether a matter requires disclosure requires directors and executives to weigh difficult and in many cases subjective predictions about the certainty or completeness of the relevant information, and the likely reaction of investors. Directors and executives do not have the benefit of hindsight – that is, the knowledge of how the share price in fact reacted, nor several months of leisurely analysis and review of documents discovered in court proceedings by reference to case theories that have in turn been developed over the course of several months.

2.7 In our experience, the boards of our ASX-listed clients typically take their continuous disclosure obligations extremely seriously. Challenges often arise even before the information percolates to them – in most organisations, the information that leads to a material decision comes from a wide range of places, levels and personnel. Certain pieces of information, for example, revenue streams, are likely to be composed of multiple inputs each requiring investigation and verification. This creates huge pressure on the boards of listed entities to understand, clarify, and disseminate what might be complex information as quickly as possible. Once it gets to the board, directors must agonise over questions about the timeliness of disclosure, whether disclosure might be premature, or whether it might be too late.

2.8 Such decisions have to be made "*promptly and without delay*" in circumstances where directors will need to be given sufficient information at appropriate levels and need time to make an informed decision about a piece of information. Often this process will require the making of further enquiries within the company and seeking independent advice if necessary. While the ASX notes that it will recognise the circumstances which may cause a delay, such recognition is not always afforded to a corporate respondent by applicants in class actions.

2.9 A review ought to consider whether the challenges set out above are in fact best practice, or whether they create unnecessary distraction and stress for the boards of ASX-listed entities. That stress is amplified by the price of getting the relevant assessments wrong, namely, the risk that a class action will be commenced against the company as a result of a disclosure of negative information. The damages resulting from a shareholder class action will usually dwarf any penalties or fines that are applied by ASIC for infringement of section 674 in particular.

2.10 It is trite to observe that any significant share price drop following an announcement will be closely examined by a class action 'promoter' to consider whether the drop provides sufficient grounds to commence an action. As summarised at [1.77]-[1.78] of the Discussion Paper, "*the standard approach*" to shareholder actions is to:

(a) identify a significant drop in the value of securities; and

(b) undertake an analysis to determine 'whether it is likely that the relevant drop had been occasioned by the late revelation of material information'.

2.11 Underpinning that analysis is an assumption (the robustness of which applicants and respondents routinely dispute) that if the market has reacted negatively to a piece of information, that information may be at least prima facie indicative of a prior omission/non-disclosure by the company respondent,

in breach of the company's continuous disclosure obligations.[4] The strict liability fault requirements relating to continuous disclosure and misleading or deceptive conduct mean that there is no need to consider (or plead) the motivations and incentives or state of mind of the corporate respondent. Michael Legg has noted:

> *A shareholder, individual or institution, now has better prospects of success in litigation due to the broad statutory causes of action based upon misleading or deceptive conduct and contravention of continuous disclosure requirements. The statutory provisions focus on consequences so that there is no need to prove a particular state of mind as in fraud or establish a specified degree of fault as in negligence*.[5]

2.12 Any review of the market disclosure laws would consider other jurisdictions' approach to this issue. For instance, the disclosure regime in the United States is based on the quarterly reporting system.[6] While the listing rules in the United States impose continuous disclosure requirements on publicly listed companies, there is no statutory backing for these requirements.[7] Therefore, the statutory framework does not require continuous disclosure.[8] Further, the listing rules do not give private enforcement rights to investors in relation to disclosure obligations.[9]

The value of the investments of shareholders of the corporate entity at the time when that entity is the target of the class action

2.13 The economic impact of class actions on corporate Australia is also relatively unexplored, and should be canvassed as part of any review. The Discussion Paper notes at [1.73];

> *… there is growing evidence of unintended adverse consequences caused by the existing framework of the Australian class action regime, coupled with the peculiar characteristics of the Australian statutory provisions concerning continuous disclosure obligations (as compared with some other cognate common law jurisdictions) and those relating to misleading and deceptive conduct. Those consequences include the impact on the value of the investments of those shareholders (including the investments of the class members themselves) of the company at the time the company is the subject of the class action, and the impact on the availability of directors and officers insurance (D&O insurance) within the Australian market.*

2.14 There are several potential negative economic impacts which ought to be considered as part of any review:

(a) **Payment or contribution to payment of settlements:** It is not the case that every listed ASX entity has sufficient insurance cover to respond to the damages claimed in a shareholder class action. We are aware of settlements in which the company respondent has been required to pay a significant proportion of the settlement amount due to insufficient insurance funds (either because coverage for shareholder class action claims was too low, or the policy had been eroded to an extent that the remaining insurance funds were insufficient).

(b) **Impact on the value of existing shareholdings:** Leaving aside a shareholder class action's less tangible impact on the operations of a corporate respondent in the form of management distraction and/or adverse reputational issues, any direct payment by company respondents of some or all of a settlement sum may affect the value of the investments of shareholders who hold a shareholding in the target company as at the time of such settlement payment (or subsequently). Among other things, the review should consider whether the payment of some or all of the settlement sum by respondent companies cause them to alter their treatment of current shareholders – for example, by withholding dividend payments for a particular period.

---

[4] See, e.g. *Structural and Forensic Developments in Securities Litigation*, transcript of the speech given by the Honourable Justice Jonathan Beach, delivered at the International Commercial Law Conference (Inner Temple, Inns of Court, London), June 2016.
[5] Michael Legg, *Shareholder class actions in Australia—the perfect storm?* (2008) 31 UNSW Law Journal 669, 706
[6] Brown, Stephen and Shekhar, Chander, *Continuous Disclosure in Australia and the United States: A Comparative Analysis* (August 2016).
[7] Ibid.
[8] Ibid.
[9] Ibid.

There is anecdotal evidence that the announcement of class actions can create downward pressure on the share price of the target company.[10] Any review should explore the impact of the announcement/filing of class actions, on the share price of the corporate respondent. Any negative impact on the share price will affect shareholder investment value.

(c) **Inability to access equity markets:** The spectre of a shareholder class action commenced as a result of share price drops following negative market announcements, means that there may be categories of corporate entities that are simply 'unlistable', with the result that such entities are confined to seeking funding from debt markets, and attendant sub-optimal financing costs. For example, an entity with particularly 'lumpy' or irregular-large-project based income is at risk of undermining guidance given to the market several months earlier if, say, a particular project has a costs blow-out too close to the end of the financial year to be able to salvage any negative impact upon the overall year's results. Where that entity is well-covered by sell-side analysts, it is no answer simply to assert that the entity shouldn't therefore give guidance. And one might query whether entities should be discouraged from giving guidance in any event. All of these issues could be usefully canvassed in the review proposed in the Discussion Paper.

The availability and cost of D&O liability cover within the Australian market

2.15 While insurers are perhaps best placed to respond to this, clients report an increase in the price of D&O insurance (particularly primary and first excess layers) and/or a decrease in the availability of such cover.[11] Anecdotal evidence from our clients suggests premiums in the last year have increased in the order of 50-60%.

2.16 The Discussion Paper notes at [1.74]:

> *The ALRC has heard there has been chronic under-pricing of D&O business by insurers since at least 2011 and that the indications are that the current D&O market premium pool is thoroughly inadequate to meet the current and projected levels of insured securities class action losses. The cost of D&O insurance has increased more than 200% in the last 12 to18 months. At least one significant insurer has recently left the Australian D&O market and there is some (anecdotal at this stage) evidence that the hardening of the market environment for D&O insurance is leading some Australian companies to contemplate relocation offshore where conditions are more favourable.*

2.17 The increased cost of obtaining and maintaining D&O insurance ultimately inhibits shareholder returns. Further, to the extent that Side C cover becomes a scarcity, with the potential result that directors and officers are directly targeted as respondents in class actions in order to access Side A or B cover, then this brings with it serious risks that high quality director candidates become less inclined to involve themselves in directorships of listed companies. Such an outcome would be extremely unfortunate, and ought be taken into account in the review proposed.

3. Regulating Litigation Funders

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

3.1 We strongly support the Commission's Proposal 3-1, for the policy reasons noted by the Commission at [3.23] and [3.24] of the Discussion Paper.

3.2 We endorse the view of the Productivity Commission and the Commission, noted in the Discussion Paper at [3.32] and [3.33], that a self-regulatory model for litigation funders may be insufficient in the Australian context to protect the position of all interested parties including group members, applicants and respondents.

3.3 Further, while the courts scrutinise funding terms and may be asked by a respondent in a class action to consider the financial viability of a funder when considering the issue of security for costs, as the Commission notes at [3.28]:

[10] See, e.g. '*Squire Patton Boggs' $300m claim 'misleading' says GetSwift*', Australian Financial Review (18 July 2018).
[11] See e.g. *Show me the money! The impact of securities class actions on the Australian D&O Liability insurance market* – XL Catlin/ Wotton + Kearney – September 2017.

> *The courts have limited capacity to view the totality of a funder's commitments to litigants at any given time and much less so over time. The courts cannot directly supervise litigation funders for the proper adherence to good governance and legal compliance more generally. The licencing regime can do this, particularly through the auditing requirement.*

3.4 The Victorian Law Reform Commission (**VLRC**) has also called for stronger national regulation and supervision of the litigation funding industry.[12]

3.5 Australia's largest and most experienced litigation funder, IMF Bentham, has long supported the introduction of a licensing regime for litigation funders. In its submissions to the Productivity Commission, IMF Bentham stated that:[13]

> *Litigation funders provide financial support to cases claiming billions of dollars. They make financial promises which extend over many years and which, if broken, will cause much heartache and financial distress to their clients. It is important to the clients, defendants and the courts that funders have both longevity and ongoing financial capacity. Funders play, for the plaintiff, a similar role to that played by insurers for the defendant. Insurers are required to be licensed and the same must surely apply to litigation funders.*

3.6 In their submissions to the Productivity Commission, Maurice Blackburn contended that increased regulation of litigation funders would stifle competition and impose barriers to entry into the litigation funding market.[14] Other opponents of a licensing regime for litigation funders put forward similar arguments.

3.7 We disagree, and endorse the Commission's assessment (at [3.26]) that a licensing regime can be implemented without reducing access to justice. IMF Bentham has argued that barriers to entry would only occur if the cost or administrative burden of holding a licence would deter potential funders from entering the litigation funding market.[15] IMF Bentham previously held an Australian Financial Services Licence (**AFSL**) and noted that (at that time) the costs of obtaining and administering a licence were minimal (around $10,000 for obtaining a licence and less than $50,000 a year for administering the licence).[16]

3.8 Nevertheless, even if a litigation funding licensing regime would impose some barriers to entry into the litigation funding market, we support the Productivity Commission's view that:[17]

> *While the Commission understands that licensing and capital requirements could create some barriers to entry and advantage incumbents in the market, it nevertheless considers these are justified to ensure that only reputable and capable funders enter the market.*

Licence scheme

3.9 At [3.4] of the Discussion Paper, the Commission proposes a unique litigation funding licence that would sit outside the AFSL regime.

3.10 We agree that a litigation funding licence should sit outside the AFSL regime for the reasons set out in the Discussion Paper at [3.6], enabling a bespoke regulatory regime to be designed and implemented to address the specific nature of the litigation funding business and the risks associated with litigation funding.

3.11 The litigation funding licensing regime should be tailored to address the specific services provided by litigation funders and the significant role that they play in funded class action proceedings. This is discussed below.

3.12 We agree that ASIC is the appropriate regulator for administering and monitoring the litigation funding licence regime.

---

[12] Victorian Law Reform Commission, *Access to Justice – Litigation Funding and Group Proceedings* (March 2018) (**VLRC 2018 Report**).
[13] IMF (AUSTRALIA) LTD, *Submission to the Productivity Commission: Access to Justice Arrangements* (18 November 2013).
[14] Maurice Blackburn Lawyers, *Submission to the Productivity Commission: Response to Access to Justice Arrangements Issues Paper* (8 November 2013).
[15] IMF Bentham, *Regulation of the Litigation Funding Industry – to License or not to License* (24 May 2013).
[16] Ibid.
[17] Productivity Commission, Access to Justice Arrangements (Inquiry Report No 72, Vol 2, 2014) (**Productivity Commission Report**).

3.13 We support the Productivity Commission's recommendation that the courts should continue to play a role in monitoring the ethical conduct of litigation funders,[18] including in relation to conflicts of interest and inappropriate conduct of proceedings.

Obligations of litigation funding licensees

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.

3.14 At [3.5] of its Discussion Paper, the Commission proposes that a litigation funding licence would impose on licensees obligations comparable to the AFSL regime. The Commission does not consider that a more onerous regime is required.

3.15 We agree with this proposal, but suggest that, in addition to the obligations set out in Proposal 3-2, litigation funders should also be subject to a breach reporting obligation akin to the obligation that applies to AFSL holders under section 912D of the *Corporations Act 2001 (Cth)*.

3.16 The Commission notes at [3.42] of the Discussion Paper that it is not necessary to regulate litigation funders similarly to legal practitioners as a litigation funder's involvement in the court process is mediated by legal practitioners.

3.17 In our experience litigation funders play an active role in assessing the merits of a case, developing the case strategy, selecting the lead applicant/s, managing and directing proceedings, and driving settlement negotiations.

3.18 Given that litigation funders play such an active role in the conduct of class action proceedings, we consider that litigation funders should be subject to additional obligations, similar to aspects of the obligations imposed on lawyers under the Legal Profession Uniform Law:

(a) Rather than an obligation only to *manage* conflicts of interest, as proposed, we consider that funders' integral involvement in the litigation justifies imposing a statutory duty to *avoid* conflicts of interest.

(b) Similarly, we consider that litigation funders should have a statutory paramount duty to the court and the administration of justice.

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

3.19 We agree with the Commission's comments as noted at [3.39] and [3.34] of the Discussion Paper that the skills and knowledge requirements of a litigation funding licensee would cover both financial skills and legal skills and an ability to assess the legal merits of a case.

3.20 In terms of character requirements, applicants for a litigation funding licence or their responsible managers should, at a minimum, satisfy ASIC that they are of good fame and character[19] and are 'fit and proper' persons to engage in the litigation funding business. The 'fit and proper' person test

[18] Productivity Commission Report.
[19] See for example section 913B of the *Corporations Act 2001* (Cth).

should address both the character and qualifications required of the responsible managers of litigation funders.

3.21 In determining whether litigation funders and/or their responsible managers are 'fit and proper' persons, ASIC should have regard to the criteria set out in ASIC Regulatory Guide 204 – *Applying for and varying a credit licence* (**RG 204**)[20] and the Legal Profession Uniform Law system.

3.22 Mirroring the criteria set out in RG 204 and the Legal Profession Uniform Law, we consider that to be a 'fit and proper' person to engage in the litigation funding business an applicant must:

(a) be competent to operate a litigation funding business and have the legal skills to understand civil litigation (including an understanding of court rules and processes) and assess the legal merits of a case (as demonstrated by the responsible manager's knowledge, skills and experience). We agree that the five options for demonstrating knowledge and skills set out in ASIC Regulatory Guide 105 – *Licensing: Organisational competence* are appropriate;

(b) have the attributes of good character, diligence, honesty, integrity and judgement;

(c) not be disqualified by law from performing their role in their litigation funding business;

(d) if our proposal that funders should avoid conflicts of interest is accepted, have no conflict of interest in performing their role in their litigation funding business; otherwise, ensure that any conflict that exists will not create a material risk that the person will fail properly to perform their role in their litigation funding business;

(e) disclose whether the person is or has been a bankrupt or subject to an arrangement under Part 10 of the *Bankruptcy Act 1966* (Cth) or has been an officer of a corporation that has been wound up in insolvency or under external administration;

(f) disclose whether the person has been the subject of disciplinary action, howsoever expressed, in another profession or occupation that involved a finding adverse to the person; and

(g) disclose any convictions, including spent convictions.

3.23 Only funders that are able to meet these minimum requirements should be allowed to enter, or remain in, the Australian litigation funding market.

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

3.24 We strongly agree that ongoing financial standards should apply to litigation funders to protect applicants and respondents in relation to adverse costs.

3.25 The Discussion Paper notes at [3.49] that the security for costs mechanism does not negate the need for a capital adequacy requirement as part of the licensing regime. We strongly agree with this view.

3.26 A security for costs order does not provide satisfactory protection to a respondent that a litigation funder holds adequate capital to meet any adverse costs order made if the proceedings are decided in favour of the respondent.

3.27 There is a significant risk that a litigation funder will be unable to pay a respondent's costs. In our experience:

(a) a security for costs order is generally made in the early stages of proceedings (when the likely costs are not clear);

(b) the amount of security required is generally significantly less than the costs incurred by the respondent (and likely to be recoverable on a successful defence); and

[20] Section B1 [204.175] and following.

(c) the court's power to order security for costs is discretionary. Therefore, there is a risk that a respondent may be unsuccessful in obtaining security for costs.

3.28 There is also a risk that a litigation funder will be unable to pay an applicant's costs or fulfil their obligations under a funding arrangement.

3.29 While we agree with the Commission (at [3.51]) that prudential regulation of litigation funders by APRA is unnecessary, given that there are serious and damaging consequences for applicants, group members and respondents if a litigation funder is unable to fulfil its financial obligations, we consider that it is appropriate that licensed litigation funders should be subject to a modified version of the financial requirements that exist under the current AFSL regime including capital adequacy requirements.

3.30 Under the AFSL regime licensees must have available adequate resources (including financial, technological and human resources) to provide the financial services covered by their licence.[21] ASIC Regulatory Guide 166 – *Licensing: Financial requirements* explains the financial requirements required of AFSL holders.

3.31 While the AFSL requirements provide a useful starting point, we consider that in order adequately to protect the position of interested parties in class action proceedings they should be augmented, as proposed by the US Chamber Institute for Law Reform in its submissions to the VLRC:[22]

> *It is proposed that the applicable prudential requirements should include those that already exist under the AFSL regime in addition to further obligations set out below:*
>
> *(a) satisfy the 'Base Level Financial Requirements' set out in ASIC Regulatory Guide 166;*
>
> *(b) comply with the minimum financial requirements that apply to specific classes of AFSL holders. For example, a litigation funder will be subject to adjusted surplus liquid fund and liquid fund requirements in circumstances where the arrangement under which it conducts business means it is obliged as principal to claimants for an amount in excess of $1,000,000, or where the litigation funder otherwise holds property on trust for the claimants in the sum of $100,000 or more;*
>
> *(c) satisfy ASIC that it has sufficient assets to cover the potential liabilities associated with an unsuccessful case; and*
>
> *(d) maintain liquid capital reserves equal to at least twice the amount of its investments in litigation. ASIC should conduct an annual audit of the funder to ensure its financial soundness. This would ensure that a litigation funder is capable of paying legal fees, disbursements and any adverse costs order.*

Overseas funders

3.32 The entry of overseas litigation funders into the Australian market further highlights the need for imposing capital adequacy requirements (especially when these funders hold their assets overseas).

3.33 The Commission considers (at [3.62]) that overseas litigation funders which are prudentially regulated overseas should be exempt from meeting specific Australian requirements provided that they meet comparable obligations in their home jurisdiction.

3.34 We support this proposal, and suggest that overseas litigation funders that are prudentially regulated overseas should be required to provide certification that evidences that they are meeting the capital adequacy requirements and minimum prudential requirements that apply in their home jurisdiction.

3.35 We also agree (Discussion Paper at [3.63]) that overseas funders who are not regulated in a comparable manner should be required to meet a capital adequacy standard in Australia.

[21] *Corporations Act 2001* (Cth) s 912A(d).
[22] US Chamber Institute for Law Reform, *'Submission No 19 to Victorian Law Reform Commission, Litigation Funding and Group Proceedings'* (22 September 2017).

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

3.36 We agree with the Commission that third-party litigation funders should be required to join the Australian Financial Complaints Authority (**AFCA**) scheme, and to provide a dispute resolution system that consists of:[23]

(a) an internal dispute resolution procedure that meets ASIC's standards and requirements; and

(b) membership of the AFCA scheme.

3.37 As the one stop shop to deal with financial system complaints,[24] we consider that AFCA is the appropriate external dispute resolution scheme for providing group members with an independent forum for raising complaints that cannot be resolved internally.

3.38 In addition, we consider that, prior to entering into a litigation funding agreement with group members, litigation funder licensees should be required to issue a financial services guide (or similar) that informs group members of the dispute resolution procedures available to them. The financial services guide should include that free access to the AFCA scheme is available.

4. Conflicts of Interest

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

4.1 As the Discussion Paper notes at [4.1]:

> *Class action proceedings, especially those that are funded by third-party litigation funders, give rise to particular circumstances likely to result in actual or perceived conflicts of interests and duties for funders and for solicitors who represent class members.*

4.2 The interests and aims of the three main players in funded class actions can vary significantly. As identified in the *Post-Implementation Review: Litigation Funding Corporations Amendment Regulation 2012 (No 6)* (October 2015) prepared by Treasury (at page 6):

> …*the funder has an interest in minimising the legal and administrative costs associated with the scheme and maximising their return; lawyers have an interest in receiving fees and costs associated with the provision of legal services; and the members have an interest in minimising the legal and administrative costs associated with the scheme, minimising the remuneration paid to the funder and maximising the amounts recovered from the defendant or insolvent company.*

4.3 In addition to receiving remuneration for the provision of legal services, legal practitioners must also:

(a) seek to meet their fundamental obligations to both the court and their clients including fiduciary duties; and

(b) as the Discussion Paper notes at [4.20] and based on our experience in class action proceedings, manage and meet the expectations of litigation funders.

4.4 In our experience litigation funders increasingly hold a unique role in class action proceedings and appear to wield a prominent and powerful voice in relation to the control and direction of the applicant's case, in particular during the settlement phase and discussions.

[23] *Corporations Act 2001* (Cth) s 912A.
[24] Media release by the Hon Kelly O'Dwyer MP, Minister for Revenue and Financial Services, *Consumers win as a one-stop-shop for financial complaints passes through parliament* (14 February 2018).

4.5 The Discussion Paper further identifies at [4.9] a series of additional potential conflicts of interests between class members, litigation funders and legal practitioners which can arise in class action proceedings.

4.6 The conflicting interests noted above are not novel and were identified in the July 2017 VLRC *Access to Justice – Litigation Funding and Group Proceedings* consultation paper and in ASIC's Regulatory Guide 248 – *Litigation Schemes and Proof of Debt Schemes: Managing Conflicts of Interest*.

4.7 While we appreciate, as noted in [4.63], [4.18] and [4.19] of the Discussion Paper, that the courts have, in certain cases, intervened to manage conflicts of interest and that various contractual arrangements, court practices and statutory regimes also seek to manage these conflicts, we agree with the concerns raised at [4.62] of the Discussion Paper that the existing disclosure mechanisms are impractical to satisfy and therefore effectively manage conflicts of interests.

4.8 Accordingly, we concur with the Commission that there is a clear need actively to identify, disclose, manage and regulate a party's actual and potential conflicts within class action proceedings.

4.9 For these reasons, we support Proposal 4-1 to augment the requirements of ASIC Regulatory Guide 248.

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.

4.10 We support Proposal 4-4 on the basis that the proposed expansion of the Australian Solicitors' Conduct Rules:

(a) is practical and sensible;

(b) imposes little to no additional regulatory burden on legal practitioners; and

(c) codifies a practice already approved by both the Federal Court and the Victorian Supreme Court (as detailed in [4.63] and footnotes 75 and 76 of the Discussion Paper).

4.11 As noted above at [4.4], in our experience litigation funders hold an increasingly central role in funded class action proceedings and can often be a powerful voice in key decision junctions in the proceeding (including the scope of the pleadings, procedural steps and in settlement decisions). Further, we agree with the view expressed by Michael Legg, noted at [4.7] of the Discussion Paper, that litigation funders have interests that do not necessarily align with those of the class members.

4.12 In light of this, it is our view that legal practitioners and/or firms should not, in any circumstances, hold financial interests in litigation funders involved in proceedings where the legal practitioner and/or firm acts for the class members. Having such interests could result in direct conflicts between the interests of legal practitioners and their clients. If legal practitioners and/or law firms want to enter the litigation funding business, they are entitled to do so, but must do so in a manner which does not create, or potentially create, conflicts of interest with their primary duties (including to the court, justice and their clients).

4.13 We also consider that the proposal is made at an opportune time when (as noted at [4.64] of the Discussion Paper) the Law Council of Australia is currently undertaking a comprehensive review of the Australian Solicitors' Conduct Rules.

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.

4.14 We also support Proposal 4-6 of the Discussion Paper in relation to amending the Federal Court of Australia's Class Action Practice Note (GPN-CA) (**Practice Note**) to facilitate early disclosure to potential class members by legal representatives of legal practitioners' and litigation funders'

obligations concerning conflicts of interests, and identifying those that exist in that particular proceeding.

4.15 In line with our support of Proposal 4-4, we consider that Proposal 4-6 is sensible to facilitate class members being in a position to make informed decisions about their involvement in the proceeding.

4.16 Careful consideration needs to be given to the appropriate timing and mechanism for this disclosure as early as possible in the proceedings. One option is to include the disclosure with the opt out notices. In our experience, in shareholder class actions, opt out notices may be an efficient method of providing all relevant class members with key information relevant to the proceeding. However, opt out notices are increasingly complex and lengthy documents and may be confusing. Including further potentially complex information may only exacerbate misunderstanding. Further consideration should be given to how and in what form disclosure notices are issued, particularly in other types of class actions, for example, those more dependent on media or less reliable sources of identification and contact. Judicial oversight and approval of the content of the disclosure notices is critical to ensure that notices:

(a) sufficiently set out legal practitioners' and funders' obligations to avoid conflicts;

(b) provide for effective management regime of conflicts; and

(c) appropriately disclose identified conflicts.

4.17 While we concede that Proposal 4-6 will not operate to eliminate actual or potential conflicts of interest, the required disclosure ought to have a beneficial regulatory and oversight effect .

5. Commission Rates and Legal Fees

Proposal 5–1 Confined to solicitors acting for the representative plaintiff in class action proceedings, statutes regulating the legal profession should permit solicitors to enter into contingency fee agreements.

This would allow class action solicitors to receive a proportion of the sum recovered at settlement or after trial to cover fees and disbursements, and to reward risk. The following limitations should apply:

- an action that is funded through a contingency fee agreement cannot also be directly funded by a litigation funder or another funding entity which is also charging on a contingent basis;
- a contingency fee cannot be recovered in addition to professional fees for legal services charged on a time-cost basis; and
- under a contingency fee agreement, solicitors must advance the cost of disbursements and indemnify the representative class member against an adverse costs order.

5.1 The introduction of contingency fees is a controversial national issue that has been considered by the Productivity Commission[25] and more recently by the VLRC.[26] Both support allowing lawyers to charge contingency fees.

5.2 Introducing contingency fees may increase access to justice for prospective class members of medium-sized actions and lower value claims, as these are not always readily funded by litigation funders.[27] These are sometimes conducted by solicitors on 'no win/no fee' arrangements with or without group members contributing to disbursements, but neither solicitors nor representative applicants are likely to be able to fund disbursement costs or take on the risk of adverse costs orders.[28] This appears to be a key limitation on the current class action system as there is a gap in services for these cases that are 'uneconomic' for litigation funders.[29] The expansion of the funding

[25] Productivity Commission Report rec 18.1; See also Victorian Law Reform Commission, *Civil Justice Review*, Report No 14 (2008) [7.8].
[26] VLRC 2018 Report.
[27] Ibid citing Contingency Fee Working Group, Law Council of Australia, 'Percentage Based Contingency Fee Agreements' (May 2014) (**Contingency Fee Report**) 20, 21; Productivity Commission Report, 625–626; VLRC 2018 Report [8.15]; Vince Morabito, *Submission 35 to the Victorian Law Reform Commission, Litigation Funding and Group Proceedings* (29 November 2017) 25 (**Morabito Submission**).
[28] Discussion Paper, citing Victorian Law Reform Commission, *Access to Justice—Litigation Funding and Group Proceedings* (Consultation Paper, July 2017) question 26 (**VLRC 2017 Consultation Paper**).
[29] VLRC 2018 Report [3.5].

market that may be triggered by the permissibility of contingency fees could, in turn, promote competition and lower costs to applicants to create a more level playing field.[30]

5.3 It has also been suggested that existing regulation of solicitors would be adequate to prevent misconduct in contingency fee arrangements[31] and contingency fees could align the interests of the solicitor with those of the client/class such that there is a greater incentive to maximise the return to the class at the earliest possible time.[32]

5.4 Despite the possible advantages of contingency fees, the Law Council of Australia has suggested that this type of charging may be inappropriate for the legal profession and could foster a culture of greed that could increase the number of unmeritorious claims brought.[33] Commentators have expressed concerns that solicitors may encourage vulnerable applicants to agree to contingency fees that do not reflect the amount of work required to resolve the claim or the risk that it is not successful.[34] The VLRC suggests that the possibility of a large payout will only augment existing conflicts of interest, increasing the likelihood of solicitors recommending that representative applicants accept offers to settle for the commercial purposes of the solicitor/firm, rather than for the benefit of the client/s.[35]

5.5 Access to justice and competition may not be practically affected by the introduction of contingency fees because: solicitors charging on a contingency fee basis would not take on risky matters and would take on more low risk matters generating a higher premium with no commensurate increase in risk;[36] 'public interest' cases may not benefit from the introduction of contingency fees as they may not generate a significant enough monetary return; and solicitors and funders are unlikely to compete for the same types of matters as law firms may be priced out by exposure to the risks of adverse costs.

5.6 On balance, there are advantages and disadvantages to permitting solicitors to enter into contingency fee agreements. If the current ban is lifted, we submit that it is vital that appropriate regulation and safeguards should be put in place to prevent misconduct in contingency fee arrangements. A starting point is the Commission's proposals in Chapter 4 of the Discussion Paper dealing with conflicts of interest.

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.

5.7 If contingency fees are to be allowed for solicitors, then we would agree with Proposal 5-2 as a sensible safeguard to limit the possibility of misuse by solicitors or to avoid further confusion for class members.[37]

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.

5.8 We support Proposal 5-3, as this issue has already been considered by the court but remains unresolved.[38] The court has considered whether it has the power to interfere with contractual arrangements to vary the amounts that would be payable by group members pursuant to funding agreements, but expressed doubt, relying instead on the court's discretion to refuse to approve a

[30] Contingency Fee Report 20; Morabito Submission 25; Vicki Waye, *Submission 2 to the Victorian Law Reform Commission, Litigation Funding and Group Proceedings* (18 July 2017) 6.
[31] Contingency Fee Report, 21.
[32] Michael Legg, *Contingency Fees – Antidote or Poison for Australian Civil Justice?* (2015) 39 Australian Bar Review 244, 250 (**Legg Article**).
[33] Contingency Fee Report 84.
[34] Contingency Fee Report 20, 21; Legg Article 253; Productivity Commission Report 613.
[35] VLRC Paper 2018 [8.38]–[8.48].
[36] Legg Article 250; Simone Degeling, Michael Legg and James Metzger, *Submission 9 to Victorian Law Reform Commission, Litigation Funding and Group Proceedings* (22 September 2017) 19; US Chamber Institute for Legal Reform, *Submission 19 to the Victorian Law Reform Commission, Litigation Funding and Group Proceedings* (29 July 2017) 43.
[37] Discussion Paper 89.
[38] Justice M B Lee, *Varying Funding Agreements and Freedom of Contract: Some Observations* IMF Bentham Class Actions Research Initiative with UNSW Law (Speech, June 2017).

settlement if dissatisfied with the commission rate, and granting common fund orders only if funding terms are varied.[39] In these circumstances, we support statutory amendment to remove this uncertainty.

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

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

5.9 In our view judges are taking an increasingly active role in scrutinising fees and commission rates and requiring them to be justified. The court's current powers, supplemented as proposed, provide appropriate powers to enable judges to ensure that fees and commissions are proportionate to the settlement sum or judgment and the risks undertaken by the funder in the circumstances of the particular case before the court.

5.10 We advocate against fixing a statutory cap or maximum proportion: if this is fixed at 49.9% (or some other %) – which is higher than most levels that have been reported – there is a danger that this becomes the default. First, this may result in group members having to pay a higher proportion than might otherwise be agreed by the applicant's lawyers on behalf of the group as a whole. Secondly, with higher legal fees and commission rates, this puts upward pressure on settlement sums without group members reaping the benefit, making cases harder to settle. Thirdly, there may be circumstances, particularly where the damages recovery (whether by settlement or judgment) is relatively small where a higher proportion of fees and commission may be appropriate. While this is unfortunate, it is a litigation risk.

6. Competing Class Actions

6.1 As the Discussion Paper notes at [6.41] the class action regime under Pat IVA was built on the premise that everyone with related claims should be involved in the proceedings and should be bound by the result unless they actively choose to opt out. Multiple class actions undermine the economy and certainty that the class action regime was designed to provide.

6.2 As the Commission notes at [6.18] of the Discussion Paper the recent reinvigoration of open class actions apparently prompted by the willingness of the court to make common fund orders has not resulted in a reduction in the prevalence of competing class actions, leading to multiple class actions with overlapping class members.

6.3 Judges of the Federal Court have tools and powers at their disposal to manage the issues that arise with competing class actions. Based on our experience working within the current regime, notwithstanding strategies implemented by the court such as case management orders designed to reduce duplication of costs (as made, for example, by Justice Beach in *McKay*[40]) and cooperation between parties, in our view respondents are still likely to incur significant additional legal costs in having to deal with two or more class actions rather than one. For example:

(a) In shareholder class actions, the respondent will incur significant costs in analysing the group member share trading data for each group;

(b) There will be some duplicated costs associated with attending a mediation and negotiating with different applicants represented by different firms of solicitors with different litigation funders;

(c) It is inevitable that each applicant will seek its respective legal costs – and each funder will have a minimum amount that it seeks to recover – to be paid out of any settlement sum.

[39] Ibid citing *Earglow Pty Ltd v Newcrest Mining Ltd* [2016] FCA 1433; *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (in liq) (No 3)* [2017] FCA 330; and *Mitic v OZ Minerals Limited (No 2)* [2017] FCA 409.
[40] *McKay Super Solutions Pty Ltd (Trustee) v Bellamy's Australia Ltd* [2017] FCA 947 (**McKay**) [113]-[116] and orders dated 13 September 2017.

This means that the minimum settlement figure is likely to be higher than if there was only one class action with one firm of solicitors and one litigation funder; and

(d) If a settlement figure is agreed, there will be some duplication of costs associated with negotiating and finalising settlement terms for each proceeding and seeking court approval of each settlement given the differing class membership, different funding terms, and other differences such as where one class has a portion of the class who are unfunded group members subject to a common fund order, but this is not the case in the other class(es) (as is the case in the *McKay* and *Basil* class actions against Bellamy's).

6.4 And notwithstanding the existing powers and tools available, there does not at present appear to be any clear policy direction (notwithstanding the overarching policy of facilitating the just resolution of disputes according to law as quickly, inexpensively and efficiently as possible) to guide the court and parties when faced with competing class actions, leading to uncertainty for litigants.

6.5 For these reasons, we support the Commission's single class action policy position and its proposals to implement this policy as consistent with the objectives of the legislation, although there may be issues (discussed below) that may need to be addressed.

6.6 However, we have concerns about the suggestion in Question 6-1 that the Federal Court should have exclusive jurisdiction for class actions arising under the *Corporations Act 2001* (Cth) and *Australian Securities and Investments Commission Act 2001* (Cth), having regard to the experience and expertise of Supreme Court judges, and the risk that this unduly burdens the Federal Court. We deal further with this suggestion below.

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.

6.7 If implemented, in our view Proposal 6-1 would go a long way to address the costs and complexity issues inherent with competing class actions.

(a) Requiring all class actions to be initiated as open class actions supports the objective to secure single, binding decisions for all affected persons, and early case management, as proposed, should significantly reduce undue, duplicative costs.

(b) Predicating the enforceability of litigation funding agreements on court approval will give the court control over the fees and returns charged by lawyers and funders, ensuring they are fair and in the interests of group members. Requiring a common fund order to be made will ensure that costs and funding commission are borne equally by all group members. In our view, these two facets of the proposal mitigate the effects of loss of choice of lawyer and/or funder.

6.8 We do not share Professor Vince Morabito's concerns[41] that the Commission's one class action policy represents a 'one size fits all' approach. The express retention of the court's discretion to do otherwise if it is satisfied that it would be inefficient or otherwise antithetical to the interest of justice to choose one and stay the other(s) militates against this. Professor Morabito also suggests that the 'compromise' of retaining the discretion "*will most likely result in no significant change in this area*" other than "*creating uncertainty for several years*." We do not share this pessimism. In our view the proposal, combined with the case management Proposal 6-2, signals that the expectation is that the court will take steps to eliminate the duplication and inefficiency inherent in multiple

[41] V Morabito *Competing class actions and comparative perspectives on the volume of class action litigation in Australia*, report dated 11 July 2018 (**Morabito July 2018 report**) at 20.

proceedings being run together. Further, we do not see that the proposal will lead to any greater uncertainty than already exists.

6.9 In our view, the retention of the court's discretion not to stay a competing class action in the types of circumstances discussed by the Commission at [6.31] of the Discussion Paper strikes the right balance between the aim of efficiency and the paramount interests of group members.

6.10 We agree with the Commission's position that reducing costs and complexity outweighs any loss of choice that Proposal 6-1 entails, and therefore support this proposal.

6.11 However, we perceive an issue in relation to the consequences of the right to opt out that needs further consideration as the right to opt out at a later stage means that the possibility of subsequent proceedings regarding the same dispute cannot be eliminated. We return to this issue in the discussion at [6.17] and following below under Proposal 6-2.

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.

6.12 We also support Proposal 6-2 to implement Proposal 6-1 through a further case management procedure to address and manage competing class actions as early as possible in the proceedings. We agree that 'front-loading' the case management of competing class actions should reduce costs and supports the overall objectives of the class actions regime. It also provides all parties with greater certainty and reduces their overall costs exposure.

6.13 Professor Vince Morabito inquires[42] whether the Commission's case management proposal and selection of lawyer and funder requires the trial judge to choose one law firm only notwithstanding any agreement by the relevant solicitors to consolidate their respective proceedings and both represent the applicants and class members. It is not our interpretation of the proposal that this outcome is inevitable in all circumstances, although we would suggest that it is likely to be the desirable outcome in most cases. There is nothing in the proposal to suggest that the court's discretion regarding these matters will be (or needs to be) curtailed. In appropriate circumstances, the court may agree to two firms representing the class, provided of course, that this serves the best interests of group members and the administration of justice, and does not lead to higher legal costs. Perhaps the Practice Note could specify that in these circumstances the court should give consideration to making a costs capping order.

6.14 Professor Morabito is also troubled by the proposal that any competing class actions must be filed within a specified time. He makes the following comments: [43]

> *Another troubling aspect of the ALRC's proposed regime is the requirement that once one or more competing class actions are filed, any subsequent competing class actions must be filed within a specified time. As a leading class action expert correctly mentioned to me, the practical effect of this requirement is to impose a more restrictive time requirement for subsequent competing class actions, than what is provided for in statutes of limitation. ….*
>
> *It is also not difficult to think of unfair scenarios generated by this requirement. For instance, a single proceeding is filed and, for whatever reason, this fact discourages other lawyers who had expressed an interest in filing a class action. After the relevant period in which competing class actions must be filed expires, the class action comes to an end without a judicial determination on the substantive merits of the proceeding. Other law firms that were interested in bringing a class action at the time that the first class action was filed or, that had no interest at that time, but are now interested in seeking legal redress for the claimants in question will be prevented from doing so. …*
>
> *….*
>
> *… If these class actions were regulated under the ALRC's proposed regime and an order had been made, after the first class action was filed, that other class actions with respect to*

[42] Ibid 19-20.
[43] Ibid 20-21.

the same dispute had to be filed within say two years, the result would have been to deprive the shareholders in question of access to the court. …

6.15 We are sure that this is not intended by Professor Morabito, but the concerns he expresses in these paragraphs regarding other interested lawyers being discouraged from commencing proceedings within the specified period, but some time later do wish to do so, have the tendency to give an impression that the interests of the lawyers require protection. Whereas the single class action policy aim of the Commission's proposals is – as Justice Lee put it in *GetSwift*[44] – aimed at dealing with:

> *competing commercial enterprises which seek to use the processes of the Court to make money and the role of the Court in ensuring the use of those processes for their proper purpose and informed by considerations including: (a) the statutory mandate (s 37M(3) of the Federal Court of Australia Act 1976 (Cth) (Act)) 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.*

6.16 More substantively, we do not share Professor Morabito's concerns in their entirety, as two important points should mean that no group member is deprived of access to the court:

(a) In respect of limitation periods, these are effectively suspended for individual group members' individual claims while they are a member of the class – they resume only if the proceeding is discontinued without the claim being dealt with or the group member opts out of the class.

(b) As Proposal 6-1 is that all class actions be commenced as *open* classes, the scenario posited by Professor Morabito resulting in group members being deprived of access to the court should not arise.

Opt outs and discontinuance

6.17 There is an issue however that is revealed in Professor Morabito's comments. If the chosen class action comes to an end without judicial determination, no group member's claim will have been determined and group members should (at least in theory) retain their substantive rights. However, this point, and the potential consequences of the exercise of the right to opt out, has not obviously been addressed in the Discussion Paper and does raise issues that we think need to be resolved in order to promote the single class action policy position.

6.18 In *McKay* Justice Beach made these observations:[45]

> *The unstated premise of the respondent's preferred option [where one of the group proceedings is allowed to go forward with the other stayed] is that it will only face one set of proceedings if there is a stay of one of the proceedings. But of course the group members in the stayed proceedings, who may otherwise have overlapped with the other group proceedings, may then opt out of the proceedings that are allowed to continue and bring their own proceedings. In such circumstances, the respondent may then be faced with many more proceedings than just the two group proceedings under the first scenario [two group proceedings with duplication in group membership eliminated and both proceedings going forward]. In other words, the respondent may be more vexed or oppressed by the consequences flowing from the second scenario. And this scenario is not so unlikely in the present case. If I stay one of the proceedings, there will be over 1000 group members in those stayed proceedings who have entered into contractual relationships with their chosen funder and solicitors firm. They may not consider the funding arrangements and solicitors for the non-stayed proceedings attractive and instead choose to opt out of the non-stayed proceedings and run their own actions, perhaps as individual actions or with the joinder of over 1000 individual applicants in one proceeding or indeed new group proceedings. None of this would be satisfactory. Now the respondent says that if this occurred I could then lift the stay on the other proceedings, but this contention is against its primary argument for a permanent stay. In my view none of this would be a desirable outcome.*

[44] *Perera v GetSwift Limited* [2018] FCA 732 (**GetSwift**) [3], quoted in the Discussion Paper [6.21].
[45] *McKay* above note 40, [39].

6.19 The right to opt out is a substantive right that should not be curtailed. Depending on the reason for the selected class action being discontinued without judicial determination of the group members' substantive rights, this scenario should not prevent those group members from having their claims judicially determined. These issues have the potential to lead to the conundrum referred to by Justice Beach quoted above.

6.20 The Discussion Paper and proposals do not clearly or completely deal with these scenarios. The question is what should be the policy response to this conundrum in order to promote the single class action policy? Some possibilities may be:

(a) **Opt outs**: at [6.46] the Commission states that '*Individuals would still be able to opt out, with any **individual actions** stayed until the class action is resolved*' (emphasis added). The proposal does not refer to subsequent *class* actions. We do not know the statistics but we are not aware of opted out group members bringing a subsequent class action in respect of the same dispute being a significant problem at this point (although we believe that it has occurred), but that does not mean that it may not become one. To promote the one class action policy, we suggest two options for dealing with subsequent litigation by group members who have opted out, without curtailing the right to opt out of the selected class action but managing the consequences. Either by legislation or through the Practice Note, it needs to be made clear that group members who have opted out either (i) are prohibited from initiating another class action in respect of the same dispute, but retain the right to bring an individual claim (which will then be stayed), or (ii) any subsequent litigation in respect of the same dispute by group members who have opted out, whether an individual claim or a class action, will be stayed pending the resolution of the selected class action.

(b) **Discontinuance**: to avoid the unfortunate scenario of the group members being deprived of access to justice, the legislation could be amended to make it clear that the single class action policy does not of itself prohibit a properly constituted class action in respect of the same dispute being initiated where the originally selected proceeding has been discontinued. Depending on the reasons for the discontinuance it should also be clear that the court retains the discretion to use the powers it already has to stay any subsequent class action if it is an abuse of process. Alternatively, a group member may elect to apply to the court to lift the permanent stay of the (or one of the) prior competing class action(s) as an avenue for obtaining redress, if they can convince the court that proper grounds exist for lifting the stay.[46] We envisage that these options enable the court to retain the flexibility to deal with varying scenarios and developments in this area.

6.21 The above suggestions are not ideal. Nor do we think that multiplicity of class actions or competing class actions can be eradicated without doing too much violence to important substantive rights of access to justice that are the paramount policy aim of Part IVA. But we think they perhaps go some way to striking the right compromise between those rights and the policy aims of the single class action policy of reducing costs and complexity.

Timelines

6.22 At [6.48] of the Discussion Paper the Commission seeks views on the appropriate timelines to give effect to the proposed process. In order to preserve flexibility to deal with unforeseeable future developments, in our view the time limit should be left to the discretion of the court to be determined as appropriate to do justice in the particular circumstances before the court, rather than to be fixed by statute.

Selection criteria

6.23 We support the multifactorial approach applied by Justice Lee in *GetSwift*,[47] which provide balanced and fair criteria to ensure the interests of applicants, group members, respondents and the administration of justice are served. These implicitly cover many of the relevant factors developed by the Canadian courts noted by the Commission at [6.25] of the Discussion Paper, but we suggest that the criteria encompass expressly factors (5) disqualifying conflicts of interest, and (10) selection

[46] A permanent stay is not equivalent to a discontinuance and may be removed if proper circumstances are shown: *Cooper v Williams* [1963] 2 All ER 282 at 286-7, [1963] 2 QB 567 at 580, 582; *Break Fast Investments Pty Ltd v Gravity Ventures Pty Ltd* [2016] VSC 30, [4]; *Mao v AMP Superannuation Ltd; Mao v BT Funds Management Ltd (No.4)* [2016] NSWSC 722 [43]-[46]; *Brookfield v Davey Products Pty Ltd* [2001] FCA 104, [27]

[47] *GetSwift* above note 44 [306]-[324], referred to in the Discussion Paper [6.51].

of defendants (respondents) referred to in that list. We also advocate for the inclusion of a criterion to examine the respective applicants' proposed arrangements for provision of security for the respondent's costs, an issue that is relevant to our next point.

Respondent involvement in selection hearing

6.24 We do not concur with the Commission's view (at [6.54]) that the respondent should play *no* part in any selection hearing. We believe that there may be situations in which it would be appropriate for a respondent to be involved in the process: for example, where there are questions concerning the financial ability of a funder – whether to fund the litigation or to provide security for the respondent's costs – a respondent should be able to make submissions to draw these concerns to the court's attention and to comment on the respective applicants' proposed security for costs arrangements.

6.25 We do not think it should be assumed that the lawyers for one applicant will make a full throated critique of the funding arrangements of the competing applicant(s): the commercial reality is that those lawyers may have existing – or may hope to have in future – funding arrangements with those competing funders for other disputes.

6.26 In our view, leaving an unhappy respondent with only the option to issue a subsequent separate application would be counterproductive to the policy aims of reducing costs, delay and inefficiency. Likewise, if the issue of security for costs is deferred until the first case management hearing after the selection hearing, any inadequacies exposed by the respondent's input at that stage may have the unfortunate effect of derailing the proceeding that has been selected to proceed, to the detriment of group members.

6.27 For these reasons, we believe the issue, and extent, of a respondent's involvement should be left to the court, to be determined on a case-by-case basis, but the Practice Note should provide that ordinarily the respondent should be given an opportunity to comment on such matters as security for costs. We do however recognise that the applicants would not wish to disclose to the respondent any information that might give it a tactical advantage in the litigation. This however can be managed appropriately by the court, as it does presently in respect of funding terms.

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?

6.28 We agree that procedural 'arbitrage' is undesirable. However, we do not support the suggestion that the Federal Court be given exclusive jurisdiction for class actions arising under the *Corporations Act 2001* (Cth) and *Australian Securities and Investments Commission Act 2001* (Cth).

6.29 Choice of forum is a legitimate and valuable right for litigants, and parties should be able to choose their preferred court for initiating class action proceedings.

6.30 However, the current spectacle involving five competing class actions brought against AMP Limited in different jurisdictions – in the NSW Supreme Court and the Federal Court – aptly demonstrates the difficulties faced for the efficient administration of justice where parties cannot agree in which court the proceedings should proceed.

6.31 On this point we agree with Professor Morabito.[48] The better solution to these issues, in our view, which preserves the right to choose the forum in which to initiate a claim, is Recommendation 12 in the VLRC 2018 Report. The VLRC's recommendation is that '*the Attorney-General of Victoria should propose to the Council of Attorneys-General that a cross-vesting judicial panel for class actions be established. The judicial panel would make decisions regarding the cross-vesting of class actions, where multiple class actions relating to the same subject matter or cause of action are filed in different jurisdictions*.' We endorse this recommendation, with the caveat that a referral to the judicial panel should only be made where the parties are unable to reach agreement on the forum in which the competing actions should proceed; and if they are unable to agree, all parties should have the opportunity to make submissions to the judicial panel advocating for their preferred forum.

[48] Morabito July 2018 report above note 41, 22.

Class closure

6.32 At paragraph [6.29] of the Discussion Paper, the Commission notes that:

> *the court already has the necessary powers to order class closure immediately prior to mediation so as to facilitate a settlement and provide finality. The Commission considers that there is merit in providing for class closure at mediation to be final so that the potential for the class to re-open is not used for tactical advantage*.

6.33 This issue seems to us to be only tangentially relevant to Proposal 6-1, but it is relevant to the policy aim of the proposal, being to reduce costs and complexity in class actions. Based on our experience, there does not appear to have been any consistency in the approaches taken by the court in determining whether the class closure prior to mediation will be final or not (although we have not undertaken a full survey of class closure orders).

6.34 We agree with the sentiment expressed by the Commission – class closure orders made to facilitate settlement discussions should be final, for three reasons:

(a) In our experience, where the orders leave open the potential for the class to be re-opened in the event of an unsuccessful mediation this has been raised during settlement negotiations in an attempt to apply pressure on the respondent to agree to a higher settlement figure. That is, as the Commission infers, it is deployed to the tactical advantage of the applicant.

(b) Irrespective of any tactical advantage, the process of re-opening, re-closing, registration, and opt out leads to increased costs and delay, to the detriment of the applicant, group members, the respondent and the court.

(c) All parties would benefit from a consistent approach that avoids uncertainty and reduces the potential for argument about the terms of the orders. To ensure the court retains the discretion to alter the usual approach in appropriate circumstances, we suggest that the vehicle to implement this proposal be amendments to the Practice Note: it should provide that the class closure will be final, but on subsequent application (usually at some point after an unsuccessful mediation) the court may in its discretion permit the class to be re-opened if satisfied that it is in the interests of justice to do so.

7. Settlement Approval and Distribution

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

7.1 We note Recommendation 16 in the VLRC 2018 Report, which proposes a similar insertion to the Victorian Supreme Court's Practice Note SC GEN 10 Conduct of Group Proceedings (Class Actions), and agree with Proposal 7-1.

7.2 We propose the following additional clause be inserted into Part 15 of the Practice Note:

> [*i*]*f the Applicant (or any party) disagrees with any part of the referee's findings in respect of the amount of the Applicant's legal costs, the objecting party must explain to the Court the basis of the disagreement(s) and provide reasons why it says the legal costs in dispute were reasonably required to be incurred in the prosecution of the class action, at least 7 days before any settlement approval hearing*.

7.3 In our experience, and as the court has observed in recent judgments, in situations where an applicant engages a costs expert to assess and justify the reasonableness of the applicant's legal costs, the following issues may arise:

(a) there may be actual or perceived bias as to the independence of the costs expert, as the applicant is giving instructions to and is briefing the costs expert;

(b) the costs of briefing the costs expert are treated as legal costs as part of the settlement approval, which would also be deducted from the settlement sum and, therefore, further reduce the settlement sum available for distribution to group members;

(c) the respondent (and the court) typically does not challenge evidence from the applicant's costs expert; and

(d) some group members object to proposed settlements on the basis of the applicant's legal costs, for the reasons at (a)-(c) above.

7.4 The court has the power to appoint an independent referee under section 54A of the *Federal Court of Australia Act 1976* (Cth) and has done so in recent settlement approvals. We agree that this practice should be adopted into the Practice Note. In doing so:

(a) actual or perceived bias as to the independence of the costs expert would be eliminated;

(b) the costs of briefing the independent referee would still be deducted from the settlement sum and there would be no change to the status quo; and

(c) therefore, the concerns at [7.3(a)-(c)] above would be adequately addressed and group members would be less likely to object to the settlement approval on the basis of the applicant's legal costs.

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?

7.5 In our experience, finalisation of the settlement distribution process can take well in excess of 12 months from the date of settlement approval, depending on the complexities of the settlement distribution scheme and the number of group members who stand to benefit from the settlement. This certainly does not help achieve a 'just, quick and cheap' distribution, and arguably does not benefit group members.

7.6 We note the comment at [7.28] of the Discussion Paper that there are some instances where fees charged by law firms to administer the settlement distribution to group members are, on average, less than 3% of the settlement sum. We also note the proposal in [7.29] of the Discussion Paper that an accounting firm, share registry service, or a claims administration company could undertake such work as competently as and more cheaply than the applicant's solicitors.

7.7 As it stands, administration of the settlement distribution scheme is typically undertaken by the applicant's solicitors. There is no competition for this work. A tender process would encourage competition, and if a tender process is adopted it should be run by the court and start from the date on which the settlement is approved by the court. The court should also make an order that the settlement distribution costs should not exceed an amount fixed by the court, and this fixed amount would vary depending on the circumstances of each class action.

7.8 In relation to the tender process, we propose the following:

(a) the court would open a confidential tender process for an appropriate period. In doing so, the court would make available to the bidding parties (pursuant to a suitable confidentiality regime), documents evidencing the applicant's loss assessment formula and any supporting documentation; and

(b) in drawing a parallel with the court's reasoning in *Getswift* in deciding the most favourable class action to proceed, the court would use similar considerations to decide on the successful tender in the 'beauty parade', with its overriding consideration to be the most favourable benefit to group members. In doing so, the court may have regard to the following factors:

(i) relevant expertise;

(ii) shortest proposed settlement distribution time;

(iii) cheapest settlement distribution costs (which must be lower than the settlement distribution costs fixed by the court, with the difference going to group members);

(iv) most accurate proposed distribution based on the approved loss assessment formula;

(v) most appropriate dispute resolution process to resolve disputed distributions; and

(vi) proposals for regular status updates to group members and to the court, and to the respondent if final orders dismissing the claims is dependent on final distribution of the settlement fund.

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

7.9 Confidentiality incentivises settlements, which in turn reduces the burden on already limited court resources. We also agree with [7.34] of the Discussion Paper, in that confidentiality can afford reputational protection to respondents who decide to settle a case for commercial reasons without incurring further time and expense to defend the case to trial, but also say that it affords reputational protection to applicants, who for example, realise during the course of the case, that their case is not as strong as was initially believed and now wish to settle for a compromised amount without having to face embarrassment, if the case were to proceed to trial.

7.10 If settlement documents were made public, we consider that class action settlements would be less readily negotiated and achieved. For example, as part of the settlement approval application, in our experience, it is common for Senior Counsel for the applicant to provide to the court a confidential opinion regarding the merits of the case and a recommendation that the proposed settlement be approved (**Senior Counsel's Opinion**). If Senior Counsel's Opinion were made public, for example, where the applicant's case was not as strong as what was initially believed, then the applicant (and its legal advisors) may suffer reputational damage. There is a risk that it would then be difficult for Senior Counsel to be as full and frank to the court as possible, to assist the court in determining the reasonableness of the proposed settlement.

7.11 We accept that the primary reason why class action settlements require court approval is to protect the interests of non-active group members (**NGMs**). While NGMs may not have a say in settlement negotiations, they already have the ability to protect and advance their interests under the existing regime. NGMs can access confidential documents in the class action, subject to signing a confidentiality undertaking in accordance with an appropriate confidentiality regime. Further, if NGMs are not satisfied with the proposed settlement, they have the opportunity to oppose the proposed settlement at the settlement approval hearing.

7.12 In any event, and based on our review, most settlement approval judgments already publicly disclose some aspects of the settlement, including:

(a) the aggregate settlement sum;

(b) the applicant's legal fees;

(c) the litigation funder's commission and the percentage of any common fund order made by the court; and

(d) the settlement distribution scheme costs.

7.13 However, for the reasons discussed above, the following documents are already available to NGMs (subject to an appropriate confidentiality regime) but should not be made public:

(a) the settlement deed;

(b) any affidavits in support of the settlement approval; and

(c) Senior Counsel's Opinion with views regarding the merits of the case and recommendation that the proposed settlement be approved.

8. Next Steps

8.1 We welcome the opportunity to answer any queries the Commission may have in relation to our Submission. For further information, please contact:

Beverley Newbold
Partner
T +61 2 9921 4894
beverley.newbold@minterellison.com

David Taylor
Partner
T +61 2 9921 4450
david.taylor@minterellison.com

Julia Avis
Special Counsel
T +61 3 8608 2131
julia.avis@minterellison.com