INSURANCE COUNCIL OF AUSTRALIA

3 August 2018

The Hon Justice Sarah Derrington
President
Australian Law Reform Commission
GPO Box 3708
Sydney NSW 2001

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

Dear Justice Derrington

Inquiry into Class Action Proceedings and Third-Party Litigation Funders

The Insurance Council of Australia (ICA) welcomes the opportunity to provide a submission in response to the Australian Law Reform Commission's Inquiry into Class Action Proceedings and Third-Party Litigation Funders Discussion Paper (the Discussion paper).

The ICA is the representative body for the general insurance industry in Australia.[1] ICA members provide a range of general insurance products including public liability and professional indemnity insurance. Our members are commonly involved in class action litigation in Australia through their provision of these insurance products.

The ICA's submission responds to a number of the questions and proposals raised in the Discussion paper, in particular those that discuss changes to the way litigation funders are regulated and measures to deal with the inefficiency and uncertainty caused by competing class actions.

The need to review the class action regime in Australia

As identified in the Discussion paper and outlined in the ICA's recent submission to the Victorian Law Reform Commission's (VLRC) review of litigation funding and group proceedings, the landscape in which the class action regime operates has changed dramatically since the current regime was introduced in 1992. Over time, the class action regime and environment in Australia has developed into arguably the most liberal in the world.[2]

In particular, at the time the current regime was developed, there were no litigation funders operating in Australia, no closed class actions and no continuous disclosure obligations for directors and officers of public companies as there currently are in the *Corporations Act (2001).*

[1] Our members represent approximately 95 percent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. December 2017 Australian Prudential Regulation Authority statistics show that the private sector insurance industry generates gross written premium of $44.9 billion per annum and has total assets of $118.6 billion. The industry employs approximately 60,000 people and on average pays out about $132 million in claims each working day. Insurance Council members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).

[2] XL Catlin and Wooton Kearney White Paper, *How did we get here? The history and development of securities Class Actions in Australia;* May 2017; p. 9

Therefore a national review of class action proceedings is timely and arguably overdue.

The impact of the continuous disclosure obligations on directors and officers insurance in Australia (Proposal 1-1)

The ICA endorses the Australian Law Reform Commission (ALRC) Proposal 1-1 in the Discussion paper that the Australian Government should commission a review of the legal and economic impact of the continuous disclosure obligations under the *Corporations Act (2001)* and the *ASIC Act (2001).*

As outlined in the Discussion paper and in the ICA's submission to the VLRC review, it is the design and application of the continuous disclosure and reporting provisions that have become the source of the large growth in high quantum common form 'closed' securities class actions conducted by litigation funders. These actions continue to impact the availability of directors and officers insurance in Australia.

Securities class actions based on a breach of duty of disclosure obligations are exceedingly difficult for a company or director to defend, as a breach and liability to pay millions of dollars in compensation can arise from an honest mistake as opposed to any conduct involving a deliberate intention to withhold information.

Given the practical difficulties and additional legal costs of defending an action to hearing and judgment, securities class actions almost always settle. In fact, no securities class action in Australia has ever reached the stage of a final court judgment.

The statistics on the financial impact of the growth of securities class actions overwhelmingly illustrate the need for a separate review as proposed by the ALRC.

In the period from 2010-2016 there were 42 new securities class actions filed in Australia.[3] This compares to only 13 being filed in the previous 6 years.[4] The average settlement amount for securities class actions is estimated at $50 million, with some actions settling for well over $100 million.[5] By comparison the Australian Directors and Officers premium pool is comparatively small at approximately $280 million.[6]

Consequently the Directors and Officers insurance market has now become unprofitable with the current premium pool being inadequate to cover these increasing and expensive claims, with insurers required to significantly increase premiums or exit this sector of the insurance market.

Common form securities class actions have broader impacts beyond the availability and affordability of insurance. They impact the value of shareholder investments and create a more uncertain and volatile business environment for Australian based companies and international

[3] Ibid.

[4] Ibid.

[5] Ibid.

[6] Insurance Council of Australia, 'Submission No. 29 to the Victorian Law Reform Commission, *Litigation Funding and Group Proceedings';* 22 September 2017.

companies operating in Australia compared to other jurisdictions. This is a further reason why a separate review as proposed by the ALRC should take place.

Regulation of Litigation Funders (Proposals 3-1 and 3-2)

The ICA supports Proposal 3-1 of the Discussion paper that the *Corporations Act (2001)* be amended to require third party litigation funders to obtain and maintain a litigation funding license to operate in Australia.

We also support the obligations outlined under Proposal 3-2 that would be required of litigation funders under a new litigation funding license.

More specifically the ICA agrees that, as litigation funding is in effect the provision of a financial service, the obligations under any new licensing regime for litigations funders should be akin to those of AFSL licensing regime. As such the same general obligations of the Chapter 7 of the *Corporations Act (2001)* should apply.

The implementation of an appropriately designed licensing regime would help ensure there is an appropriate level of protection for class members as well as other parties to litigation, including defendants and insurers.

Litigation funders would arguably be better placed to serve the interests of a class if they are in a sound financial state. To this end there is a strong argument that they should be subject to some form of capital adequacy requirements as is the case for AFSL holders.

Accreditation for lawyers (Proposal 4-3) and other measures to manage conflicts of interest

The ICA supports the ALRC proposal that specialist accreditation for lawyers involved in class action proceedings be developed.

Specialist accreditation has been developed across numerous other legal practice areas to improve the level of standard of service provided. Given the unique nature of class action litigation, there is no reason why similar accreditation should not also be available. As class actions increase and more law firms and practitioners become involved in class action proceedings (which will further increase should the current prohibition on law firms charging contingency fees be removed), the need for specialist training and accreditation will become all the more necessary.

In relation to other proposals outlined in the Discussion paper designed to help address and manage conflicts of interest the ICA, in principle, supports these proposals.

Rates and Legal Fees (Proposal 5)

The ICA does not hold any strong view at this time in regard to the proposals and questions in the Discussion paper concerning rates and legal fees. We do wish to provide the general comment that, for the class action regime to remain legitimate, it must ensure that class members receive an appropriate proportion of any settlement/judgment amount.

We also highlight that, based on the experience of our members, it is our expectation that a removal of the current prohibition on lawyers charging contingency fees will lead to an increase in

class actions, predominately through the take up of more 'risky' class action proceedings that litigation funders have traditionally not pursued.

For example, smaller class actions, that currently do not attract litigation funders due to their size, would be expected to increase should law firms be permitted to charge contingency fees.

As with any reform that results in increased claims frequency, the expansion in the use of contingency fees would therefore be expected to put additional pressure on the cost of insurance premiums in a number of classes of insurance (not just Directors and Officers insurance). Increases in premiums that organisations must pay are likely to ultimately be passed on to consumers.

Competing Class Actions (Proposal 6)

The ICA strongly supports reform to the class action regime to address the inefficiencies and unnecessary enormous expense caused by competing class actions.

As outlined in our submission to the VLRC Inquiry, competing class actions work against the key policy objectives of the current opt-out class action regime in Australia, namely to promote efficiency in the judicial system when dealing with a large number of claims arising out of the same or similar issues.

Competing class actions also create significant issues for defendants who must expend additional time and resources managing multiple claims that could be capable of being dealt with more expediently and efficiently in a single action. Furthermore, competing class actions deprive defendants and their insurers of certainty and finality in addressing all potential claims through the one proceeding.

To this extent the ICA supports the ALRC Proposal 6-1 that, as a matter of policy, all class actions should be open class actions and that where there are two or more competing class actions, the Court determine which of these proceedings will progress and stay any competing proceeding (subject to an overriding discretion to allow competing actions to proceed should it be in the interest of justice).

To allow for the implementation of Proposal 6-1 the ICA also supports the use of an amended Federal Court of Australia Practice Note to allow the Court to identify any competing class actions and resolve which applicant, which lawyer and which funder will lead the single class action.

This process would overcome the current inefficiencies caused by multiple class actions dealing with the same issue, providing respondents and their insurers the ability to more easily resolve claims with certainty and finality. It would also help ensure the law firm and litigation funder chosen to run the class action is best equipped to represent interests of the class.

Similarly the ICA is open to the suggestion that the Federal Court be given exclusive jurisdiction to hear class action proceedings arising under the *Corporations Act (2001)* and *ASIC Act (2001)* as an additional means of addressing competing class actions and forum shopping as well as providing a more consistent and streamlined process.

We trust the ALRC will find this submission useful.

The ICA would welcome the opportunity to discuss our submission with you. We would also welcome the opportunity to be involved in the further roundtables prior to the finalisation of the ALRC's report in September.

If you would like to meet with the ICA or have any questions regarding this submission please contact Tom Lunn, Senior Policy Advisor, Consumer Outcomes [redacted]

Yours sincerely

[redacted]

Robert Whelan
Executive Director & CEO