Current Trends in Australian Shareholder Class Actions

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1 Farrer Place Sydney.

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Associate Professor Michael Legg*

* Associate Professor, UNSW Australia Law and Of Counsel, Jones Day.

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A: Full Federal Court Relaxes Commencement Requirements for Class Actions

Commencing Class Action Proceedings with Multiple Respondents

To commence a class action, the proceedings must comply with s 33C (1) of the *Federal Court of Australia Act 1976* (Cth) which provides:

> *(1) Subject to this Part, where:*
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> *(a) 7 or more persons have claims against the same person; and*
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> *(b) the claims of all those persons are in respect of, or arise out of, the same, similar or related circumstances; and*
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> *(c) the claims of all those persons give rise to a substantial common issue of law or fact;*
>
> *a proceeding may be commenced by one or more of those persons as representing some or all of them.*

Prior to *Cash Converters International Limited v Gray* [2014] FCAFC 111 the law was divided upon the issue of whether the group members must claim against each and every respondent. Sackville J, as part of a Full Federal Court, in *Philip Morris Ltd v Nixon* reasoned that s 33C(1)(a) requires every applicant and represented party to have a claim against the one respondent or, if there is more than one, against all respondents. His Honour relied on the text of the section and the approach of the Australian Law Reform Commission that recommended the introduction of class actions.[1]

Equally, in a judgment of the Full Court of the Federal Court, in *Bray v F Hoffman La-Roche Ltd*, Carr J held that it is only the representative party who must have a claim against every respondent.[2] The group members need only claim against one of the respondents. Finkelstein J, in the same case, considered that conclusion was consistent with the policies of the Act: to reduce costs, enhance access to justice, improve the usage of court resources and determine common issues consistently.[3] Lower courts have been divided as to which Full Court to follow.[4]

Background to Cash Converters Class Action

Ms Gray, the applicant, commenced two class actions related to the provision of consumer credit by Cash Converters franchises through 'personal loan' and 'cash advance' contracts. The respondents are alleged to have engaged in unconscionable conduct in contravention of s 12CB(1) of the

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[1] *Philip Morris (Australia) Ltd v Nixon* (2000) 170 ALR 487 at 514.
[2] *Bray v F Hoffman La-Roche Ltd* (2003) 130 FCR 317 at 345-346.
[3] *Bray v F Hoffman La-Roche Ltd* (2003) 130 FCR 317 at 373-374.
[4] See eg *Hunter Valley Community Investments Pty Ltd v Bell* (2001) 37 ACSR 326 at [33]; *Johnstone v HIH Ltd* [2004] FCA 190 at [38], *Guglielmin v Trescowthick* (No 2) (2005) 220 ALR 515 at [29]; *McBride v Monzie Pty Ltd* (2007) 164 FCR 559 at [4]; *Auskay International Manufacturing & Trade Pty Ltd v Qantas Airways Ltd* [2008] FCA 1458 at [61]; *Kirby v Centro Properties Ltd* (2010) 189 FCR 301 at [11]. In *NSW, Civil Procedure Act* s 158(2) was adopted to overcome the approach in Philip Morris and adopt the approach in Bray.

Australian Securities and Investments Commission Act 2001 (Cth) and the interest/fees charged in the credit contracts and cash advance contracts were in contravention of the *Credit (Commonwealth Powers) Act 2010* (NSW) which caps the maximum annual interest rate on consumer credit contracts.

In the personal loan proceedings, Ms Gray obtained personal loans from both Safrock Finance Corporation (Qld) Pty Ltd and Cash Converters Personal Finance Pty Ltd but the members of the group in that proceeding obtained finance from one or the other but never both. A claim of accessorial liability is also made against Cash Converters International Pty Ltd, the parent company of the other Cash Converter entities, by all group members.

The same representative, this time in proceedings for the cash advance contracts, received credit from only one Cash Converters franchise, Ja-Ke Holdings Pty Ltd, whereas the majority of group members received credit from different franchisees who were not parties to the proceedings. The representative and the group members also made claims for accessorial liability against the same respondents, Cash Converters Pty Ltd and Cash Converters International Pty Ltd.

The respondents in both proceedings argued that neither proceeding complied with s 33C (1)(a) above because the group members did not claim against each and every respondent. The group members in the personal loans proceedings had claims against either Safrock Finance or Cash Converters Personal Finance but not both. The claims of the group in the cash advances proceedings did not comply as they related to many different franchises, not the respondent franchise with which the representative dealt. Thus it did not matter that the representative and the group members had claims for accessorial liability against the same two Cash Converters entities in every case. They were alleged to be accessories as they shared directors and officers with the franchises and had control over the lending system.

Decision at First Instance

Farrell J at first instance preferred the reasoning of Carr and Finkestein JJ in *Bray v F Hoffman La-Roche Ltd* because her Honour believed that it accorded with the policy behind the introduction of class actions into the Federal Court and with the overarching purpose of procedural decisions found in s 37M of the *Federal Court of Australia Act 1976* (Cth): to resolve disputes quickly, efficiently and inexpensively. The overarching purpose has not previously been considered in the cases on this question. As Farrell J preferred the *Bray* approach, both classes complied with the requirement of s 33C(1)(a).[5]

The Full Court

The respondents sought leave to appeal on the basis that s 33C(1) requires that each group member whom Ms Gray represents must have a claim against each respondent to the proceeding and that both proceedings are not properly constituted because this requirement is not met. The Full Court granted leave to appeal but dismissed the appeal.

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[5] *Gray v Cash Converters International Ltd* [2014] FCA 420.

The decision proceeded on the basis that a representative party must have a claim against each respondent.[6] This is required by s 33D which deals with standing of the representative party.

The Full Court posed the question: "does s 33C(1) of the FCA require that *each* group member have a claim against *each* respondent to the proceedings?" The Full Court's answer was no.[7]

The Full Court first sought to construe the statute by reference to its text, context and purpose. The Full Court held that requirements not mandated by the legislation for commencing a class action should not be otherwise imposed.[8] Provided there are seven group members with a claim against one respondent then the proceedings may be commenced. The addition of other group members and other respondents is not prohibited. Indeed joinder may be employed to add other respondents to the proceedings in respect of whom only some group members have claims.[9]

The Full Court considered the earlier decisions of *Philip Morris Ltd v Nixon* and *Bray v F Hoffman La-Roche Ltd.* The Full Court was of the view that the specific issue raised in the current appeal was not in issue in *Philip Morris* because it was not in dispute. The parties had accepted that each group member must have a claim against each respondent.[10] If a point is not in dispute in a case, then the decision lays down no legal rule concerning that decision.[11]

The Full Court considered *Bray* and acknowledged that each of the three judges in that Full Court addressed the issue differently. Carr J stated that it was not necessary to decide the question but he agreed with Finkelstein J's reasons. Finkelstein J, as explained above, disagreed with *Philip Morris.* Branson J was not persuaded that *Philip Morris* was clearly wrong and considered that it should be followed.[12] In the current judgment the Full Court endorsed the reasoning of Finkelstein J without explaining whether the point had needed to be resolved in *Bray*. Finkelstein J stated:[13]

> *It can immediately be acknowledged that a properly constituted representative proceeding must involve a group of seven or more persons each of whom has a claim or claims against one person. But that is all the section requires. It simply does not address the situation where some members of the group, say 10 out of a group of 15, also have claims (that is, causes of action) against some other person, being causes of action which satisfy both s 33C(1)(b) (each claim arises out of the same circumstances) and s 33C(1)(c) (each claim gives rise to common issues of law or fact).*

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[6] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [13].
[7] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [13], [33].
[8] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [19], [23].
[9] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [21].
[10] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [28].
[11] See *Coleman v Power* (2004) 220 CLR 1 at 44-45.
[12] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [29]-[32].
[13] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [32] citing *Bray v F Hoffman La-Roche Ltd* (2003) 130 FCR 317 at 373.

Ramifications

The disagreement over the interpretation of s 33C(1)(a)'s requirement that *7 or more persons have claims against the same person,* as shown by the conflicting positions taken in *Phillip Morris* and *Bray*, has raged for more than 10 years.

The Full Court in *Cash Converters International Limited v Gray* [2014] FCAFC 111 has sought to authoritatively decide the question of the interpretation of s 33C(1)(a) by siding with *Bray* and holding that it is unnecessary for each group member to have a claim against each respondent. Some group members may only have a claim against some respondents.

The Full Court also seems to be saying that it is not necessary for seven or more group members to have a claim against each respondent. Rather, in the entire class action all that is needed is seven group members with a claim against one respondent and the representative party has a claim against each respondent. Other respondents can then be joined to the proceedings.[14] However, as this question was not strictly necessary to be decided on the case before the Full Court it may be regarded as dicta.

The Full Court's decision is likely to lead to larger, less cohesive classes as group members with claims against only some of the respondents may be included. However, compliance with s 33C(1)(b), *same, similar or related circumstances*, and s 33C(1)(c), *a substantial common issue of law or fact* is still required. Nonetheless there are likely to be more individual or sub-group issues than under the *Phillip Morris* approach. Australian class actions may become more protracted. However, the need for multiple class actions to take account of multiple respondents should no longer be needed as a result of s 33C(1)(a).

[14] *Cash Converters International Limited v Gray* [2014] FCAFC 111 at [22].

B: Funding Litigation: Third Party Litigation Funding and Lawyers Fees

GPT Shareholder Class Action Settlement

The GPT class action was brought by shareholders alleging that GPT Management Holdings Limited and GPT Re Limited (collectively 'GPT') had engaged in misleading conduct and breached its continuous disclosure obligations. The class action settled.

On 21 June 2013 the Federal Court approved the settlement sum of $75 million inclusive of interest and legal costs, but refused to approve the sum of $9.3 million claimed in respect of the applicant's lawyer's legal fees and disbursements and the sum of $53,530.85 claimed in respect of the applicant/representative party's expenses in prosecuting the claim on its own behalf and that of group members. Both requests for approval were referred to a Registrar of the Court to conduct an assessment and report back to the Court. The Registrar reported back and a further judgment was delivered on 7 November 2013 with $8.5 million awarded for legal fees and disbursements and $10,000 awarded for the applicant/representative party's expenses.

Further, the litigation funder's attempt to recover a percentage fee from group members who had not entered into funding agreements was rejected. However, an amount equivalent to the fee was deducted from the non-funded group members' recoveries and redistributed to all group members. Interestingly the Court had no difficulty in requiring group members who had not entered into a retainer and costs agreement with the lawyers being required to contribute pro rata to the legal fees upon them being approved.

The GPT class action judgments signal the Federal Court's growing interest, and concern, as to how class action recoveries are divided up amongst lawyers, litigation funders, applicants, funded group members and unfunded group members.

Applicant's Lawyer's Legal Fees

Justice Gordon of the Federal Court stated that there were two aspects to the request for the approval of legal fees. The first was that the amount approved by the Court was to be shared on a pro rata basis by all group members irrespective of whether they executed a Legal Costs Agreement (LCA). The second aspect concerned the quantum of the professional costs and disbursements incurred by the applicant's lawyers which the law firm sought approval from the Court.

The first issue deserves comment because the liability to pay legal costs in a class action in Australia was always thought to be the same as for other litigation – there needed to be a contractual obligation to pay. Admittedly, the issue has rarely arisen because the legal costs usually form part of the settlement to be paid by the respondent. Justice Gordon's approach is similar to the common fund approach used in US class actions,[15] although no reference is made to this

[15] For a discussion of the common fund approach see Michael Legg, "Reconciling Litigation Funding and the Opt Out Group Definition in Federal Court of Australia Class Actions – The Need for a Legislative Common Fund Approach" (2011) 30 *Civil Justice Quarterly* 52.

jurisprudence. Her Honour also suggested that given the increasing number of class actions, perhaps there should be a requirement that any LCA or equivalent between group members and a firm of solicitors should be approved by the Court before it is binding on the group members. This is also a novel approach as the LCA would not normally be binding on group members who are not a party to the LCA.

On the second issue, her Honour expressed concern that the law firm was acting for itself in circumstances where group members were unable to oppose the application and there was no other contradictor before the Court. The group members were unable to oppose the application as they had no notice of the fees and disbursements or how they were quantified.

The applicant's lawyers had engaged a costs consultant to provide an expert opinion on the reasonableness of the legal costs and disbursements incurred. In the judgment, Gordon J was highly critical of the law firm and the costs consultant's report and was not satisfied that the report provided the Court with the basis for approving the law practice's fees. Her Honour noted that the amount claimed by the applicant's lawyers was almost three times the original estimate of $3,500,000 (which the report failed to explain), that the hourly charge out rate seemed to have increased by 5% with no demonstrated notice of that increase to the members, and the costs for discovery (based on a rate of $550/ hour) seemed unreasonable. The LCA signed by (most of) the group members did not seem to be properly referred to and utilised in the assessment of costs by the consultant.

Justice Gordon cited *Redfern v Mineral Engineers Pty Ltd* [1987] VR 518 as to the rationale for the court's "surveillance" over costs between solicitor and client and that the solicitor holds a "position of dominance" in circumstances such as these. The fact that the distribution scheme provided for the law practice's fees and disbursements to be deducted from the settlement sum prior to the individual group members' entitlements being calculated clearly exacerbates such a situation. A conflict of interest arises as the greater the law practice's fees and disbursements, the less compensation that is available for individual group members.

In the second judgment, which considered the Registrar's report, a detailed review of the fees and disbursements disallowed by the Registrar was undertaken which led to the legal fees being reduced by about $800,000. A number of novel issues were also raised by the litigation funder and the applicant's lawyers. The litigation funder, having been granted leave to intervene, submitted that the funder had a role in assessing the reasonableness of the legal fees. Gordon J acknowledged that the funder could be expected to monitor fees but held that the funder could not replace the role of the court which must assess the fees "in the interests of all group members, not the litigation funder".[16] The applicant's lawyers also submitted that the proportionality of legal fees to the recovery was a useful check on the reasonableness of the fee award sought. Here the fees were 12% of the total settlement sum. This was compared with 16% in the Centro class actions. Gordon J rejected this submission.

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[16] *Modtech Engineering Pty Limited v GPT Management Holdings Limited* [2013] FCA 1163 at [137].

Litigation Funder's Fee

Comprehensive Legal Funding LLC (CLF) was the litigation funder in the proceedings. Approximately 92% of group members (including the applicant, Modtech Engineering Pty Ltd) had executed a Litigation Funding Agreement (LFA) with CLF to fund the class action. The LFA provided that CLF was to receive a commission of between 25% and 30% of net recoveries after reimbursement of litigation costs.

The Settlement Distribution Scheme proposed that the funding commission be deducted from the individual entitlements of all group members including the 8% who had not entered into a funding agreement with CLF.

Gordon J rejected this aspect of the scheme as her Honour explained that CLF had made a commercial decision to fund the proceedings by entering into a LFA with just 92% of group members. Her Honour stated that the deduction of the funding commission was not a part of the commercial bargain reached by CLF with the 8% who had not entered into a funding agreement and that it should not be imposed on those members. Gordon J distinguished *Pathway Investments Pty Ltd v National Australia Bank Ltd (No 3)* [2012] VSC 625 where Pagone J had approved a similar provision, as the notice given to group members in that case differed with respect to the timing of the notice and the stage of the litigation. However, her Honour also remarked that "it is difficult to conceive of a circumstance in which it would be appropriate".[17] The differing approaches may become important factors as to where class actions are commenced as the Victorian approach provides a greater return for the funder.

In order to ensure that the unfunded group members would not receive what Gordon J described as a "windfall", her Honour proposed that the amount which would have been deducted and paid to CLF under the scheme should be pooled and distributed pro rata to all group members.

Referred to as the "equalisation factor", the above approach has been used in a number of class action settlements.[18] This ensures that the funder's fee is effectively shared by all group members regardless of whether they are funded or not and as a result, the burden of the funder's fee is shared by all. At the same time, the litigation funder is not able to recover more than they are contractually entitled to.

Whilst her Honour indicated that this would result in an outcome that was "fair and reasonable to all",[19] there are arguments to suggest that unfunded group members' interests need to be further protected. Evidently, unfunded group members will receive less from the settlement fund when the equalisation factor is applied. In the absence of effective regulation overseeing the fees charged by funders, unfunded group members may be penalised for the commercial decision a representative party or a funded group member has made with the funder. It appears prudent for the Court to scrutinise the funding agreements entered into by the funded group members.

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[17] *Modtech Engineering Pty Limited v GPT Management Holdings Limited* [2013] FCA 626 at [60].
[18] See *Paxtours International Travel Pty Ltd v Singapore Airlines Ltd* (Federal Court proceeding NSD 787 of 2007); *Dorajay Pty Ltd v Aristocrat Leisure Limited* [2009] FCA 19.
[19] *Modtech Engineering Pty Limited v GPT Management Holdings Limited* [2013] FCA 626 at [58].

Decision

The Federal Court referred the law practice's legal costs and Modtech's expense claims to a Registrar who was to conduct an assessment and provide a report to the Court. Orders were made on 26 June 2013 approving the amended distribution scheme. The proceedings were listed before Justice Gordon on 19 September in respect of the claims for legal costs and expenses. Orders approving the legal fees in the amount of $8,565,285.13 and applicant/representative party expenses in the amount of $10,000 were made on 15 November 2013.

Melbourne City Investments Pty Ltd (MCI) shareholder class actions against Treasury Wines and Leighton Holdings

MCI was incorporated on 1 November 2012. On the day of its incorporation, MCI purchased 39 shares in Leighton Holdings Limited for $684.06 and 140 shares in Treasury Wine Estates Limited for $693.00. In addition, on 1 November 2012, MCI purchased parcels of shares in another 17 publicly listed companies, each parcel costing a little under $700. In February 2014, MCI purchased further small parcels of shares in another 145 publicly listed companies.

Between October and December 2013, MCI as representative party, commenced shareholder class actions against both companies based on allegations of defective disclosure to the securities market. The solicitor acting for MCI was in all cases Mr Mark Elliott. Mr Elliott was also the sole director and shareholder of MCI.

First Instance Decision

Treasury Wine and Leighton contended that the proceedings against them were brought by MCI for the collateral purpose of generating legal fees for Mr Elliott, and sought a range of relief including that each proceedings was an abuse of process and should be stayed. Alternatively, orders in the exercise of the inherent jurisdiction of the Court to restrain Mr Elliott from acting for MCI in the proceedings whilst MCI is the lead plaintiff.

Justice Ferguson found "it is probable that the reason for MCI's existence is to launch proceedings, such as the present proceedings, to enable its sole director and shareholder to earn legal fees from acting as the solicitor for MCI".[20] The small shareholdings held by MCI meant that the compensation which MCI stood to gain would be less than $700 in each class action. Justice Ferguson inferred that it was therefore unlikely that proceedings were commenced for the purpose of recovering compensation. The inferences or findings may have been rebutted by MCI's director, Mr Elliott, if he had given evidence. No such evidence was given.[21]

The Court has inherent jurisdiction to stay proceedings where they are an abuse of process, which includes where the proceedings are predominantly brought for an improper purpose. However, the power of a stay is only to be used in exceptional circumstances. Justice Ferguson found that as MCI

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[20] *Melbourne City Investments Pty Ltd v Treasury Wine Estates Limited (No 3)* [2014] VSC 340 at [9].
[21] See *Jones v Dunkel* (1959) 101 CLR 298 for the common law principle that where a party fails to tender evidence or call a witness it may be inferred that nothing in that absent testimony or evidence would have assisted the party's case.

had the immediate and legitimate purpose of obtaining orders for compensation, and to stay the proceedings would broaden the abuse of process concept beyond its recognised boundaries, no abuse of process existed.

Rather the concern was with the conduct of the solicitor. The Court also has inherent jurisdiction to make orders to ensure the due administration of justice and to protect the integrity of the judicial process, including restraining a legal practitioner from acting in proceedings. The principles for restraining a legal practitioner are:[22]

- The test to be applied is whether a fair-minded, reasonably informed member of the public would conclude that the proper administration of justice requires that a lawyer should be prevented from acting, in the interests of the protection of the integrity of the judicial process and the due administration of justice, including the appearance of justice.
- The jurisdiction is exceptional and is to be exercised with caution.
- Due weight should be given to the public interest in a litigant not being deprived of the lawyer of his or her choice without due cause.
- The timing of the application may be relevant, in that the cost, inconvenience and impracticality of requiring lawyers to cease to act may provide a reason for refusing to grant relief.

A number of arguments were put forward as to why Mr Elliott should not continue as the solicitor on the record. These include:

- Mr Elliott may be required to give evidence in his role as sole director of MCI,
- that evidence may be 'adjusted' because of Mr Elliott having a personal pecuniary interest in the outcome of the proceedings
- a conflict between Mr Elliott's pecuniary interest and his duty to the court
- a conflict between Mr Elliott's duty to MCI as it's director and the interests of the group members.

The last of these arguments, essentially the possibility of a duty-duty conflict, was relied on by Justice Ferguson who stated:[23]

> *the [hypothetical fair-minded independent observer] would consider that Mr Elliott is compromised in his role as a solicitor such that there would be a real risk that he could not give detached, independent and impartial advice taking into account not only the interests of MCI (and its potential exposure to an adverse costs order), but also the interests of group members.*

A number of arguments were also made for the discontinuance of the class action, but the Court found that that there was nothing irregular about the proceedings. The Court did rely on the power

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[22] *Melbourne City Investments Pty Ltd v Treasury Wine Estates Limited* (No 3) [2014] VSC 340 at [39] citing *Kallinicos v Hunt* (2005) 64 NSWLR 561.
[23] *Melbourne City Investments Pty Ltd v Treasury Wine Estates Limited* (No 3) [2014] VSC 340 at [50].

in the class actions legislation to make orders it thinks "appropriate or necessary to ensure that justice is done in the proceeding".

The Court ordered that Mr Elliott be restrained from acting for MCI whilst it is the lead plaintiff and that the proceedings not be permitted to continue as group proceedings whilst MCI and Mr Elliott act in tandem as plaintiff and solicitor.

Victorian Court of Appeal

Treasury Wine appealed the finding that there was no abuse of process. Central to the appeal was the finding below that the reason for MCI's existence was to launch proceedings to allow Mr Elliott to earn legal fees and the inference that the current proceedings were launched for the purpose of Mr Elliott earning legal fees.[24] The Victorian Court of Appeal, by majority (Maxwell P and Nettle JA, Kyrou JA dissenting), held that the commencement of litigation for the purpose of generating legal fees, rather than vindicating legal rights, was an abuse of process. The majority stated:[25]

> *The processes of the Court do not exist — and are not to be used — merely to enable income to be generated for solicitors. On the contrary, they exist to enable legal rights and immunities to be asserted and defended. In the common form of class action, that is the sole purpose of the proceedings. The members of the class wish to vindicate their rights. The fact that success will result in the solicitors' fees being paid does not affect the propriety of the proceeding.*

Special Leave Application Denied

MCI applied for special leave to appeal to the High Court from the Victorian Court of Appeals decision. The application was heard by Hayne and Keane JJ. The application was denied on 15 May 2015.[26]

Allco shareholder class action

Background

In the Allco shareholder class action, an application was filed by the two applicants/representative parties seeking court orders pursuant to ss 23 and 33ZF of the *Federal Court of Australia Act 1976* (Cth) (FCA) and Rule 1.32 of the Federal Court Rules 2011 (Cth) (FCR) (or any of them) for the appointment of International Litigation Funding Partners Pte Ltd (ILFP) as the funder of the class action on the terms of the litigation funding agreement into by some group members. Clause 9 of the funding agreement provided for group members to reimburse the funder the amount of legal fees and disbursements paid by the funder and to pay a percentage of the Resolution Sum determined as follows:

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[24] *Treasury Wine Estates Ltd v Melbourne City Investments Pty Ltd* [2014] VSCA 351 at [4]-[6].
[25] *Treasury Wine Estates Ltd v Melbourne City Investments Pty Ltd* [2014] VSCA 351 at [14].
[26] *Melbourne City Investments Pty Ltd v Treasury Wine Estates Limited* [2015] HCATrans 116 (15 May 2015).

Number of Shares Held	Resolution on or by 30 June 2014	Resolution on or by 30 June 2015	Resolution after 30 June 2015
< 1,000,000	25%	30%	35%
> or = 1,000,000	22.5%	27.5%	32.5%

If the Funder funds an appeal of a final judgment, or the defence of an appeal from a final judgment, a further 5% of the Resolution Sum in respect of the appeal so funded is payable by group members.

Orders Sought

The orders sought by the applicants (for the benefit of the funder) were that the Court approve the amounts payable by the applicant and group members to ILFP pursuant to clause 9 of the funding agreements on the basis that they are "reasonable consideration payable to ILFP and expenditure incurred by the Applicants in prosecuting the proceeding" in exchange for the funding and an indemnity as to costs. Further, that the applicant was entitled to withhold the above amounts from any settlement or judgment and pay them to ILFP. [27]

The making of the orders would have the result that all group members would be liable to pay the funder's fees (costs incurred by the funder and a percentage of any recovery) without having entered into any agreement.[28] The orders, if made, would remove the need for a litigation funder to contract with a group member to be paid and therefore allow for an open rather than a closed class to be employed. The application would create a funding regime similar to the common fund approach employed in the United States for the payment of lawyers' fees in class actions.

Applicants' Argument

The Applicants advance six reasons for why the Court should make the orders in the exercise of its discretion under either s 33ZF or s 23 of the FCA Act:

1. the order is analogous to other situations where a person has incurred expenses in recovering property for the ultimate benefit of others and has been held to be entitled to recover their costs, expenses and fees out of the recovered fund. For example, a liquidator is entitled to recover, as a first charge or priority on a fund, the expenses incurred by the liquidator in the realisation of the fund: *In re Universal Distributing Company Ltd (in liq)* (1933) 48 CLR 171. The expenses recoverable may include amounts paid to a litigation funder who funded proceedings commenced by the liquidator to recover or realise an

[27] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [51], [53], [59]-[60].
[28] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [130] ('The effect of the proposed order is also to impose the commercial funding terms agreed to by the Applicants on all group members, despite the fact that they have not entered into, or even been invited to enter into, any such agreement.')

asset: *IMF (Australia) Ltd v Meadow Springs Fairway Resort Ltd (in liq)* (2009) 253 ALR 240 at [73]

2. proposed order ensures an equal and equitable outcome between all group members, regardless of whether or not they have entered into a funding agreement with ILFP.

3. the proposed order will secure a beneficial outcome for all group members by allowing for an open class that includes all group members rather than a closed class where the group is limited to those persons who have entered into a funding agreement with ILFP.

4. the proposed order is consistent with the policy objectives of Pt IVA of the FCA Act. Those policy objectives are said to be to enhance access to justice, reduce the costs of proceedings and promote the efficiency of court resources. An open class is more efficient and provides access to justice better than a closed class.

5. the proposed order appropriately protects the rights of group members because group members retain the right to opt out of the proceeding, the amount that ILFP may receive is reasonable having regard to funding premiums paid in other representative proceedings, and because the Court retains control over any settlement because of the need to secure the approval of the Court under s 33V of the FCA Act.

6. the proposed order is consistent with orders made in similar proceedings in Australia, the United States (which employs the common fund doctrine) and Canada. In relation to Australia, the cases cited were *Pathway Investments Pty Ltd v National Australia Bank Ltd (No 3)* [2012] VSC 625, the consideration of similar orders in *Re Timbercorp Securities Ltd (in liq) (Application for the Approval of Compromises)* [2012] VSC 590 and *Farey v National Australia Bank Ltd* [2014] FCA 1242.

The Court then considered whether it had power to make the orders sought.

Section 33ZF

Section 33ZF(1) provides:

> *In any proceeding (including an appeal) conducted under this Part, the Court may, of its own motion or on application by a party or a group member, make any order the Court thinks appropriate or necessary to ensure that justice is done in the proceeding.*

Section 33ZF confers a broad power on the Court to make orders in relation to representative proceedings. It should not be given a narrow construction, but rather should be construed as liberally as its terms and context permit: *McMullin v ICI Australia Operations Pty Ltd* (1998) 84 FCR 1 at 4; *Courtney v Medtel Pty Ltd* (2002) 122 FCR 168 at [48]-[49]. Wigney J explained that a provision conferring a broad power on the Court should generally not be read down by making implications or imposing limitations which are not found in the express words: *The Owners of the Ship "Shin Kobe Maru" v Empire Shipping Company Inc* (1994) 181 CLR 404 at 421; *Wong v Silkfield Pty Limited* (1999) 199 CLR 255 at [11]. The only express limitation or requirement in s 33ZF is that the Court thinks the order is appropriate or necessary to ensure that justice is done in the proceeding. An

order which has been found not to be appropriate or necessary to ensure that justice is done in the proceeding for the purposes of s 33ZF is unlikely to be appropriate in the sense required to engage the Court's power under s 23 of the FCA Act.

Reasoning

Wigney J considered each of the 6 arguments put forward by the applicants from the perspective of whether they engaged the requirements of s33ZF. His Honour found that none did.

A representative party or applicant is not in an analogous position to a liquidator. In particular, while a representative party can commence proceedings on behalf of group members they have no authority to promise to pay the litigation funder a commission based on a percentage of any amounts recovered on behalf of other group members.[29]

Further, it is neither appropriate nor necessary to impose the Applicants' commercial bargain in relation to the payment of commission on the group members as a whole, at least at the beginning of proceedings. The fact that orders that have this effect have been made in the context of anticipated settlements, which require the approval of the Court under s 33V of the FCA Act, was said to not assist the Applicants. At the stage of settlement the court is in a better position to determine the settlement sum and the payment to be made to the litigation funder. The lack of information as to the amount that may be payable to the funders also went against the making of an order.[30]

Wigney J stated that the only real rationale for making the order at this stage was to ensure the commercial viability of the proceeding from the perspective of the litigation funder, but that had nothing to do with ensuring that justice was done in the proceeding.[31] Wigney J also observed that:

> *Justice "in the proceeding" would not ordinarily involve any consideration of the commercial interests of a litigation funder unless they gave rise to some issue or problem that has, or is likely to have, some direct impact on the proceeding.*[32]

The court also rejected the argument that there would be an inequality between group members if some may benefit from the funding without contributing to its cost. Wigney J recounted the history of the search for funding for the class action and indicated that the funder knew of the difficulties in convincing sufficient potential group members to sign funding agreements when it determined to commence proceedings with an open class definition. Further the issue of unfunded group members not being advantaged or able to 'free-ride' could be dealt with should a settlement arise. The Federal Court has recognised, in the context of making orders facilitating or approving settlements, that fairness may require that group members who have entered into funding

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[29] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [129].
[30] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [133]-[134].
[31] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [135]. See also [160].
[32] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [113].

agreements should not end up in a worse position than group members who have not entered into funding agreements.[33]

Wigney J then turned to consider the rights and interests of group members and the argument that the orders were consistent with the policy of Pt IVA. His Honour was not convinced that the order sought was in the interests of group members, at least at such an early stage of proceedings when so little was known about the possible outcome. The applicants' argument that without the order a closed class would be commenced which would shut out some group members contrary to the policy of Part IVA was seen as being driven by the interests of the funder rather than group members.[34]

Litigation funders frequently use a closed class definition, or when an open class proceeding is settled both parties seek to have the class closed. The submissions in the Allco class action should cause judges to ask more searching questions about whether group definitions and settlements disadvantage some group members and should not be permitted.

Wigney J considered the fact that notice had been given to group members and none had objected to the orders that were sought. While notice clearly had to be given, the fact that no objections were received is not determinative. The right to opt out does afford protection to group members but here the proceedings had been commenced very close to the expiry of the statute of limitations. When this is combined with group members having small claims it is likely that opting out would equate with being unable to bring an action and so its protective force was diminished.[35]

Wigney J also considered how the requested order would interact with s 33V and the requirement for the court to approve any settlement. While the applicants accepted that the court would retain the power to vary the orders sought as part of a settlement, Wigney J was concerned at how a court could practically do that if it had previously found the amounts payable to the funder as reasonable. His Honour also thought that the order may conflict with s33ZJ which allows for costs reasonably incurred by an applicant to be reimbursed out of any damages awarded to group members where those costs cannot be recovered from a respondent.

His Honour reviewed the case law in the US and Canada but found it unhelpful due to differnces between those jurisdictions and Part IVA.

His Honour then turned to the discretionary aspect of s 33ZF. Even if the power was engaged his Honour would not have exercised his discretion to make the orders because so much was unknown: the number of group members, the value of the damages claims in question, the amount of the commission that the Court is asked to approve as reasonable consideration payable to ILFP,

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[33] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [142]-[149].
[34] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [172]-[173].
[35] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [181]-[182].

although it "could run into the tens if not hundreds of millions of dollars, even if the matter settles at an early stage", the likely length and complexity of the trial, the legal costs that would be incurred.[36]

Law Reform

Although his Honour declined to make the sought after orders he did observe that there may be a case for legislative law reform to take account of the role of litigation funders.[37] In particular, "there would need to be specific provision for scrutiny and court approval of the amounts payable to the litigation funder at the determination of the proceeding".[38]

Lessons

The current decision demonstrates the growing and significant role that litigation funding plays in relation to class actions. This can be a positive development through providing the necessary financial resources to seek access to justice for those with small claims. However, the judgment recognised explicitly that funders structure class actions and their funding arrangements in their own self-interest. Litigation funders aim to make profits for their investors, they are not a benevolence fund looking to do good.

The law around class actions has been developed by funders seeking to advance their interests through favourable precedent development. The closed class that was approved in the Multiplex class action is a clear example. Wigney J examined the sought after orders from the perspective of their impact on group members as a whole and found that while the orders may assist the funder they were not in the interests of group members. It must not be forgotten that the function of class actions is to pursue remedies for those allegedly wronged – not to make profits for litigation funders.[39]

The Allco decision means that litigation funders will in the short term continue to either employ a closed class definition or seek orders as part of any settlement to address the existence of unfunded group members. The latter gives rise to a continuing debate as to how unfunded group members should be dealt with. Two broad approaches have been adopted to date. First is an equalisation order whereby unfunded group members have their recovery reduced by the amount the funded group members have paid to a litigation funder. This amount is redistributed across all group members. The second is the imposition of the funding agreement terms on unfunded group members so that they must pay the funder's fee to the funder. The former ensures equality amongst group members but without a direct payment to the funder. The second ensures equality but with funder receiving a greater fee. In the GPT shareholder class action Gordon J rejected the second approach observing that "it is difficult to conceive of a circumstance in which it would be

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[36] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [220].

[37] The call for law reform was previously raised by Michael Legg, "Reconciling Litigation Funding and the Opt Out Group Definition in Federal Court of Australia Class Actions – The Need for a Legislative Common Fund Approach" (2011) 30 *Civil Justice Quarterly* 52 at 69-72.

[38] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811 at [227]-[228].

[39] See *Treasury Wine Estates Ltd v Melbourne City Investments Pty Ltd* [2014] VSCA 351 at [14].

appropriate"[40] and employed the first, in keeping with the approach adopted in the Aristocrat and Multiplex class actions. However, the second approach has been employed in two NAB class actions – a shareholder claim in the Supreme Court of Victoria and a bank fees claim in the Federal court.[41]

[40] *Modtech Engineering Pty Limited v GPT Management Holdings Limited* [2013] FCA 626 at [60].
[41] *Pathway Investments Pty Ltd v National Australia Bank Ltd (No 3)* [2012] VSC 625; *Farey v National Australia Bank Ltd* [2014] FCA 1242.

C: Causation and Shareholder Class Actions

The provisions that allow shareholders to seek compensation for contravention of the continuous disclosure regime and prohibitions on misleading conduct contain the statutory wording "resulted from", "because" and "by" which have been interpreted as necessitating proof of causation.[42] However, the pleadings initiating shareholder class actions have sought to prove causation in a number of ways: direct reliance, indirect reliance and through the fraud on the market theory.[43]

Direct reliance is the traditional or conventional test for causation and in the shareholder class action context would require each group member to prove that they relied on the misleading disclosure in deciding to buy securities.[44] Causation is an individual issue.

The fraud on the market theory is a United States legal application of the efficient market hypothesis and assumes that the price of shares in an open and developed market reflects all publicly available material information about those shares, including misleading statements or omissions. The theory presumes that shareholders rely on the integrity of the market price in making their investment decisions such that a misleading statement or omission affects all shareholders through the share price, meaning that individual reliance does not need to be proved. US law requires that a number of pre-requisites be met for the theory to be relied on, namely:

(a) the defendant made public misrepresentations (publicity);

(b) the misrepresentations were material;

(c) the shares were traded on an efficient market (market efficiency); and

(d) the plaintiff traded the shares between the time the misrepresentations were made and the time the truth was revealed.45

Indirect reliance (also called third party reliance) is based on the proposition that causation exists if it can be demonstrated that the contraventions caused the market, as a whole, to inflate the price of a company's securities so that group members suffered losses by acquiring shares at an inflated price. Indirect reliance, like fraud on the market, assumes an efficient market. This approach has been put forward through reasoning by analogy with cases like *Janssen-Cilag Pty Ltd v Pfizer Pty Ltd* (1992) 37 FCR 526, or by reference to statutory construction of the provisions dealing with continuous disclosure.

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[42] *Corporations Act 2001*(Cth) ss 1041I, 1317HA, 1325; *Wardley Australia Ltd v Western Australia* (1992) 175 CLR 514 at 525.

[43] See *P Dawson Nominees Pty Ltd v Multiplex Ltd* [2007] FCA 1061 at [11]; *P Dawson Nominees Pty Ltd v Brookfield Multiplex Ltd (No 4)* [2010] FCA 1029 at [15]-[17]; *Hobbs Anderson Investments Pty Ltd v Oz Minerals Ltd* [2011] FCA 801 at [9]-[10]; *Kirby v Centro Properties Ltd (No 6)* [2012] FCA 650 at [4]; *Pathway Investments Pty Ltd v National Australia Bank Limited (No. 3)* [2012] VSC 625 at [11]-[12].

[44] Jonathan Beach, 'Class Actions: Some Causation Questions' (2011) 85 *ALJ* 579 at 584.

[45] See Michael Legg, 'Shareholder Class Actions in Australia - The Perfect Storm?' (2008) 31 (3) *UNSW Law Journal* 669 at 681-683; Michael Legg and John Emmerig, 'United States Supreme Court Revises Fraud on the Market Presumption for Securities Class Actions' (2014) 88 *Australian Law Journal* 856.

Attempts to rely on indirect reliance or the fraud on the market theory have been the subject of judicial comment as set out below.

Downer EDI Limited class action

In *Camping Warehouse Australia Pty Ltd v Downer EDI Ltd* [2014] VSC 357 the plaintiffs pleaded that reliance was not necessary or that causation may be satisfied by indirect reliance or through the fraud on the market theory. Particular emphasis was placed on the remarks of Finkelstein J in *P Dawson Nominees Pty Ltd v Multiplex Ltd* [2007] FCA 1061 where the role of the efficient market hypothesis and the existence of a rebuttable presumption of reliance in United States "fraud-on-the-market" cases was explained:

> *It seems the way the case will be put is based on the hypothesis (in some quarters an article of faith) that had the Corporations Act and ASX listing rules been complied with the market in Multiplex securities would have been open and efficient and the price of the securities would be determined on the basis that all material information regarding the company was publicly available. The consequence of this hypothesis is the premise that the market price of the securities would have been negatively affected if there had been proper and not misleading disclosure about the Wembley Stadium project.*
>
> *It may also be argued that there is a rebuttable presumption of reliance (if it is necessary to establish reliance) on the existence of an open and efficient market for Multiplex securities. In the United States this is referred to as the fraud-on-the-market theory. In Basic Inc v Levinson (1988) 485 US 224 the Supreme Court of the United States held that securities class action plaintiffs are entitled to a presumption of reliance that the market for the securities in question was efficient and that the plaintiffs traded in reliance on the integrity of the market price for those securities. …*

By reference to the text of the Act, the context of the legislation and relevant case law, the plaintiff submitted that it was not necessary to plead reliance. Although the judgment refers to the plaintiff relying on fraud on the market, it would also seem that statutory interpretation is relied on to support some form of indirect reliance.

The defendant referred to the decisions of the New South Wales Court of Appeal *Digi-Tech (Australia) v Brand* (2004) 62 IPR 184 and *Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd* (2008) 73 NSWLR 653 to argue that as the plaintiff was not a passive investor, but actively acquired shares, direct reliance was necessary because the conduct of the plaintiff and in particular the inducement of the plaintiff forms a link in the causation chain and that without such inducement there was no link between the misleading conduct or failure to disclose and the plaintiff's loss. However neither case dealt specifically with the statutory provisions in issue.

Justice Sifris stated:[46]

> *I have not been referred to and have been unable to find any case precisely on point or that deals with causation in the context of a breach of the continuous disclosure requirements set out in Div*

[46] *Camping Warehouse Australia Pty Ltd v Downer EDI Ltd* [2014] VSC 357 at [59]-[60].

6CA of the Act. The obligations are different in nature to those proscribing misleading or deceptive conduct and there is much to be said for the view expressed by Finkelstein J in P Dawson. Reliance may well be artificial in cases of this kind. The extent to which the provisions differ and the precise formulation and matters that underpin or evidence the causation requirement are matters of some complexity that require comprehensive and detailed analysis, undesirable in the case of a strike out application.

The plaintiff has pleaded that the conduct in breach of the Act caused the loss in the sense of the reduced value of the shares. The essence of the claim is that the shares when acquired were overpriced directly because of such conduct. It cannot be accepted that this formulation is plainly hopeless or bound to fail.

As a result the Statement of Claim was not struck out and the proceedings were allowed to proceed.

Arasor International Limited class action

In *Caason Investments Pty Limited v Cao* [2014] FCA 1410 the applicant sought to amend its pleadings to delete reliance from causes of action based on misleading conduct in relation to financial products, financial services and disclosure documents so as to employ 'market based causation'. The Federal Court in determining whether to grant leave revisited the law on causation.

The Court explained that causes of action based on misleading conduct in relation to financial products or financial services were based on s 82 of the *Trade Practices Act 1974* (Cth) which had been subject to extensive judicial interpretation. The case law accepts that causation can be proved without direct reliance by the person who suffered loss, but there must be reliance in some form, usually by a third party. Her Honour went on to allow the amendment of the pleading: [47]

despite the strength of intermediate appellate court authority which requires reliance to be demonstrated as an element of causation where an investor has entered into a transaction to which the claim of misleading or deceptive conduct is relevant, recent High Court authority on s 82 of the TPA and the fact that market based causation claims relying on ss 1041H and 1041I and their analogues in the ASIC Act in the context of Chapter 6CA have not been considered by the High Court suggest that the state of the law cannot be regarded as so settled that an appropriately pleaded claim would have no reasonable prospect of success.

However, in relation to the claims based on a misleading prospectus the deletion of reliance was rejected as the court found that the current pleading did not set out any other causal connection and the weight of authority was against the viability of such a claim.[48]

The applicants appealed Farrell J's decision to the Full Federal Court.

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[47] *Caason Investments Pty Limited v Cao* [2014] FCA 1410 at [106].
[48] *Caason Investments Pty Limited v Cao* [2014] FCA 1410 at [111], [114].

Babcock & Brown

The history of Babcock & Brown's fall is well known – with shares trading as high as $34.63 before being suspended from trading with the share price at 33 cents. The plaintiff shareholders sued for their alleged investment losses and relied on contraventions of the continuous disclosure regime. Their claim was ultimately unsuccessful but, in the course of the trial, the issue of what causation test should apply to market non-disclosure claims was argued. Babcock & Brown submitted that the plaintiff shareholders could not succeed unless direct reliance was shown. Conversely, the plaintiff shareholders asserted that they were entitled to recover on a theory of indirect causation and that they did not each need to prove individual reliance to jump the causation hurdle.

As events transpired, because of the grounds on which the plaintiffs failed, the Federal Court concluded it was unnecessary for it to rule on which causation test should apply. Nonetheless, the judge (in obiter) expressed the following view:

> *[219] Consequently, no issue about causation arises. It is unnecessary to decide, therefore, whether the plaintiffs could recover when it is alleged they bought shares at an inflated price caused by a listed company's failure to disclose information to the market. Had it been necessary to reach a view, it is likely I would have agreed with the plaintiffs' submissions. Shortly, the reasons for this are:*
>
> *(i) the relevant statutory questions appear in s 1317HA ('the damage resulted from the contravention') and s 1325 ('loss or damage because of conduct') of the Act;*
>
> *(ii) provisions of this kind import a notion of causation;*
>
> *(iii) whilst reliance is a sufficient condition for establishing causation it is not a necessary one. Cases involving diversion of customers from one trader to another caused by misleading conduct are one obvious example of this: Janssen-Cilag Pty Ltd v Pfizer Pty Ltd [1992] FCA 437; (1992) 37 FCR 526 per Lockhart J;*
>
> *(iv) it is relevant to take into account the underlying context of the alleged infringement. Here s 674 requires disclosure of market sensitive information where it would be expected to affect price (and where the listing rules also require disclosure). The provision assumes the existence of a price effect on the market in general;*
>
> *(v) a plaintiff may not recover where it knows of the misleading nature of the alleged conduct: Ingot Capital Investments Pty Ltd v Macquarie Equity Capital Markets Ltd [2008] NSWCA 206; (2008) 73 NSWLR 653 at 661-662 [19]- [22] and 731-732 [612]-[619] (CA); Digi-Tech (Australia) Pty Ltd v Brand [2004] NSWCA 58; (2005) 62 IPR 184 at 212 [159] (CA). But those observations by the Court of Appeal do not preclude a case brought by a council against a ratings agency where the agency had communicated information to the financial services arm of a Council association about particular financial instruments and the council had then relied on what the financial services arm had said. The Full Court held that such a case could be maintained: ABN AMRO Bank AV v Bathurst Regional Council [2014] FCAFC 65; (2014) 309 ALR 445 at 727 [1376] (FC) ('ABN AMRO'). See also Cahill v Kenna [2014] NSWSC 1763 at [264]- [265] per*

McDougall J; McBride v Christie's Australia Pty Ltd [2014] NSWSC 1729 at [258]- [266] per Bergin CJ in Eq; Caason Investments Pty Ltd v Cao [2014] FCA 1410 at [87]- [92] per Farrell J.

(vi) ABN AMRO establishes that, at least in principle, where A misleads B and B in consequence misleads C, C is not necessarily precluded from recovering from A;

(vii) the facts on this case are different to those in ABN AMRO to this extent: here it is alleged A misled the market (i.e. many B's) which then bid up the price which then caused loss to C. This is not the same factual situation as arose in ABN AMRO but I do not think it relevantly differs;

(viii) whilst I accept that generally a plaintiff must show in a misleading conduct case that they would have acted in a particular way but for the conduct (see, e.g., Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd (No 1) [1988] FCA 40; (1988) 39 FCR 546 at 559 (FC); Metalcorp Recyclers Pty Ltd v Metal Manufactures Ltd [2003] NSWCA 213; [2004] ATPR (Digest) 46-243 at [50] (CA)) it is artificial to speak of reliance in non-disclosure cases such as the present: Campbell v Backoffice Investments Pty Ltd [2009] HCA 25; (2009) 238 CLR 304 at 351-352 [143].

Justice Perram indicated that, with qualifications, he would accept that "a party who acquires shares on a stock exchange can recover compensation for price inflation arising from a failure to disclose material required by [the continuous disclosure regime] to be disclosed".[49] The qualifications included that the relevant statement or omission must be material or have a price effect (a precursor to disclosure being required) and that a plaintiff shareholder could not recover if it knew of the misleading nature of the alleged conduct.

Iluka Resources Limited

Bonham v Iluka Resources Limited [2015] FCA 713 dealt with an application for preliminary discovery by Mr Bonham to assist him to decide whether or not to commence a class action against Iluka Resources Limited. Kerr J denied the application. However, as part of the argument Kerr J was presented with an argument that the fraud on the market theory could be used to satisfy the requirements of causation and proof of loss or damage. His Honour explained:

[71] … The fraud on the market doctrine theory is premised on the "efficient market hypothesis" and the notion that:

... shareholders rely on the integrity of the market price in making their investment decisions such that a misleading statement or omission affects all shareholders through the share price, meaning that individual reliance does not need to be proved.

(Cashman P and Abbs R, Prospects and problems for investors in class action proceedings in Lindgren KE (ed), Investor Class Actions, Ross Parsons Centre of Commercial Corporate and Taxation Law Monograph 6, (University of Sydney, 2009), 61-100 at 79 citing M Legg,

[49] *Grant-Taylor v Babcock & Brown Limited (In Liquidation)* [2015] FCA 149 at [220].

Shareholder Class Actions in Australia – The Perfect Storm? (2008) 31 University of New South Wales Law Journal 669 at 678-680).

[72] The doctrine was endorsed by the US Supreme Court in Basic v Levinson [1988] USSC 36; 485 US 224 (1988) but there has been resistance to its application in Australia (see for example Black A, "Investor class actions seminar 10 March 2009 - Commentary on all four papers" (pp 101-109) in Lindgren K E (ed), Investor Class Actions, (University of Sydney, 2009)). To date there has been no instance of which the Court is aware, where the doctrine has been given effect in Australia to establish causation. In my view it goes too far to treat the obiter remarks of Perram J in Grant-Taylor v Babcock & Brown (In Liquidation) [2015] FCA 149 at [219]- [220] as doing more than endorsing the efficient market hypothesis as an available mechanism to measure loss.

However, Kerr J found that he did not need to determine if fraud on the market as a way to prove causation was arguable because Mr Bonham had relied on announcements by Iluka Resources thus allowing for causation to be proved in the traditional way by direct reliance.[50]

Uncertainty continues

The Downer EDI and Arasor cases were interlocutory judgments dealing with pleading issues where the defendant's bore the usual higher burden of proof compared to the standard burden applicable at the trial stage. Neither case determined causation after a trial. In contrast, the Federal Court's observations in the Babcock & Brown shareholder litigation attracted more attention because they were made in the context of a final (as opposed to interlocutory) judgment.[51] Nonetheless, the observations in Babcock & Brown on indirect reliance are obiter and not binding on subsequent courts.[52]

Nonetheless, even if indirect or third party reliance is accepted as being available to prove causation in shareholder class actions it still remains unclear as to how that form of reliance will be proved. In the US reliance through the fraud on the market presumption depends on acceptance of the efficient capital markets hypothesis and proof of an efficient market. A body of case law exists around how the presumption comes about and is rebutted. In Australia it is uncertain as to what must be shown in shareholder class action where the market is alleged to have been misled.

[50] *Bonham v Iluka Resources Limited* [2015] FCA 713 at [75].
[51] *Grant-Taylor v Babcock & Brown Limited (In Liquidation)* [2015] FCA 149.
[52] See *Bonham v Iluka Resources Limited* [2015] FCA 713 at [72].

D: The Role of Institutional Investors and Common Questions in Shareholder Class Action Trials

The front page of the *Australian Financial Review* on 28 July 2006 reported that institutional investors were signing up to participate in shareholder class actions.[53] Since then it has become common knowledge that litigation funders and plaintiff's lawyers have developed close links with many institutional investors as the investors' large shareholdings make class actions economically viable. However, institutional investors are usually not the applicant whose claim forms the basis of the litigation and who has various responsibilities as outlined in figure 1. Rather they have sought to be group members so as to avoid costs, the media spotlight and the need to give discovery of their investment strategies, at least prior to the determination of their individual claims. Yet it is the institutional investors' claims which typically make up the bulk of the compensation sought from the listed corporations that are the respondents in shareholder class actions. Consequently there have been questions about what role institutional investors should play.[54] In the Newcrest Mining Ltd class action the respondent sought to challenge the typical approach by seeking an order for two institutional investors, who were amongst Newcrest's top 20 shareholders, to participate in the trial of the common issues.

Background

Earglow Pty Ltd, as trustees for Boorne Super Fund Account and the Boorne Holdings Family Trust, commenced a class action in the Federal Court of Australia against Newcrest Mining Ltd.

The class action alleged that in the period 13 August 2012 to 6 June 2013, Newcrest breached its continuous disclosure obligations under s 674 of the *Corporations Act 2001* (Cth) and the prohibition on misleading and deceptive conduct in s 1041H of the *Corporations Act* in:

- Failing to disclose to the ASX certain material information known to Newcrest in relation to expected total gold production and expected capital expenditure; and
- Making statements that mislead or deceived shareholders about profit forecasts and performance for the 2012 financial year.

Prior to the commencement of these proceedings, ASIC brought its own proceedings against Newcrest for contraventions of s 674(2) of the *Corporations Act*. Newcrest admitted the contravention and consented to the declarations made and pecuniary penalties imposed.[55]

The common issues to be determined at the first stage of the trial included:

(a) Whether Newcrest made the representations and, if made, whether they were misleading or deceptive or likely to mislead or deceive;

(b) Whether the representations were continuing representations;

[53] Annabelle Hepworth, "Big Funds in Class Act", The *Australian Financial Review*, 28 July 2006, p 1.
[54] See eg Michael Legg, "Institutional investors and shareholder class actions: The law and economics of participation" (2007) 81 *Australian Law Journal* 478.
[55] *Australian Securities and Investments Commission v Newcrest Mining Ltd* [2014] FCA 698.

(c) Whether Newcrest had reasonable grounds for making the representations;

(d) Newcrest's knowledge, if any, of the material information throughout the class period;

(e) Whether any or all of the material information was generally available in the market;

(f) Whether the material information was known to Newcrest and of a kind required to be disclosed during the class period.

Arguments for Institutional Investor Participation in the First Stage Trial

The respondent, relying on s 33ZF of the of the *Federal Court of Australia Act 1976* (Cth) (FCA Act), sought an order for two institutional investors, who were amongst Newcrest's top 20 shareholders and had signed litigation funding agreements with Comprehensive Legal Funding LLC, to partake in the first stage of the trial.

The respondent advanced the following submissions in support of the order:

(a) Evidence of institutional shareholders will significantly impact in the determination of questions of reliance, causation and loss. Findings in the initial trial unique to the applicants case will be unhelpful in assessing these questions in relation to the majority of the group who are made up of institutional investors and are likely to have employed a different methodology in making investment decisions.

(b) The applicant's individual claim alone will not adequately facilitate the adjudication of the issues and is not truly representative of Newcrest's investors. The applicant acquired only a very small number of Newcrest shares within a very limited temporal window, in circumstances where at least 80% of Newcrest's shareholder base was made up of institutional investors.

(c) There is no principle that the initial trial in a representative action must be confined to common issues.

(d) Recent case law demonstrates that group members, particularly those who have signed litigation funding agreements, are not entitled to remain passive.

Federal Court Declined to Make Orders

Justice Beach declined to exercise his powers under s 33ZF of the *FCA Act* for the following reasons:

Interpretation of s 33ZF

Section 33ZF provides that:

> *(1) In any proceeding (including an appeal) conducted under this Part, the Court may, of its own motion or on application by a party or a group member, make any order the Court thinks appropriate or necessary to ensure that justice is done in the proceeding.*

Justice Beach made the following observations concerning s 33ZF. Firstly, it was accepted that PtIVA does not provide an entitlement that group members may remain passive. Secondly, while s 33ZF is a wide power, it must nonetheless satisfy the requisite statutory test, namely that the exercise of power is "appropriate or necessary, to ensure, that justice is done in the proceedings".

Thirdly, the statutory test under s 33ZF will not be satisfied solely on the basis that the orders sought will assist or contribute to an efficient resolution. Fourthly, courts should be cautious in accelerating the individual claims outside the contemplation of s 33Q and s 33R. Finally, s 37M of the *FCA Act* which requires the court to interpret and apply the civil practice procedures provisions in a way that promotes the overarching purposes cannot be used to give broader meaning or scope to s 33ZF.

Examples of active participation

Newcrest advanced the following case law examples of instances where individual group members' claims have been adjudicated at the first stage trial (see *Johnson Tiles Ltd v Esso Australia Pty Ltd & Abir (No 3)* [2001] VSC 372; *Woodcroft-Brown v Timbercorp Securities Ltd (in liq)* 253 FLR 240; *Mathews v SPI Electricity Pty Ltd (Ruling No 5)* (2012) 35 VR 615; *Rowe v AusNet Electricity Services (formerly SPI Electricity Pty Ltd)* (S CI 2012 04538)). Justice Beach distinguished these examples from the present case emphasising that unlike the cases advanced, the applicant has not acquiesced to the procedure put forward by Newcrest and had instead pursued a different forensic strategy. Furthermore, Justice Beach determined that cases presented were not analogous as they involved significant differences between individual group members in terms of liability as group members were distinguished from one another on the basis of the different legal duties owed.

Representation of the group

Justice Beach rejected Newcrest's submission that, as a non-institutional investor, the applicant and its claim were not representative of the group. Firstly, when examining the number of different shareholders rather than the percentage of shareholdings, the vast majority of the shareholders within the group were not institutional investors. Secondly, it is common in Australian shareholder class actions to have a retail investor as the representative party, whose individual claim is determined at the first stage. Finally, given the variations in size, client base and investment parameters, identifying and adjudicating the case of just two institutional investors would not be entirely representative of the group.

Relevance of evidence

Despite accepting that evidence of the role and behaviour of institutional investors will generally be relevant in determining the common issues, Justice Beach held that such evidence was not therefore automatically "necessary". Justice Beach held that questions of evidence and forensic strategy are matters to be determined by the applicant and that s 33ZF does not exist as a coercive power to compel the applicant to file evidence that may be necessary to support its claim.

Impediments, costs or delay

Justice Beach accepted that the orders sought would not give rise to significant practical impediments nor cause excessive costs or delay. Notwithstanding this position, Justice Beach concluded that the class action regime in the *FCA Act* did not command such an intrusive role and was of the opinion that the circumstances did not justify *"stretching modern case management to*

such an extent as to endorse some Continental idea of in effect coercing a party to file evidence of a particular type against its wishes".[56]

Ramifications

Section 33ZF has been recognised as conferring a wide power on the court in representative proceedings. In *McMullin v ICI Australia Operations Pty Ltd*, Wilcox J interpreted the provision as follows:[57]

> *Section 33ZF appears in Div 6 of Pt IVA which is headed "Miscellaneous". It bears the marginal note "General power of Court to make orders". These two features support the conclusion, that would in any event arise from its wording, that s 33ZF(l) was intended to confer on the Court the widest possible power to do whatever is appropriate or necessary in the interests of justice being achieved in a representative proceeding.*

Similarly, in *Courtney v Medtel Pty Ltd* Sackville J acknowledged the breadth of the power, stating that:

> *There are good reasons to give s33ZF a generous interpretation. The section is couched in broad terms. Moreover, the Court is given power to act on its own motion. The language, which is described in the Explanatory Memorandum as "wide", doubtless reflects the drafter's perception that the new statutory procedure for representative proceedings was likely to throw up novel problems that would require close supervision by the Court.*[58]

Justice Beach appears to have adopted a much stricter interpretation of s 33ZF. Although accepting that "appropriate" is a lower threshold than "necessary", his Honour then raised the threshold by placing emphasis on the need "to *ensure*" that justice is done. Further, a finding that steps may be "merely convenient or useful *per se*" is not sufficient for the power to be exercised.[59] This is not to say that following the earlier decisions would have necessarily resulted in the orders being granted. Section 33ZF provides the court with a discretion that it still could have chosen not to exercise in favour of the orders sought.

The outcome reached by Justice Beach is consistent with two factually similar cases where the court declined to invoke its power under s 33ZF. In *Kirby v Centro Properties Limited* the respondents sought an order that the claims of at least one institutional/trustee group member be heard in the initial trial. The respondents advanced similar submissions to those put forth by Newcrest. In rejecting the application Justice Middleton held that it was unlikely that the order would assist in the determination of causation as an institutional investor *"will have its own peculiarities in relation to reliance and other claims"*. [60] In *National Australia Bank Ltd v Pathway Investments* the trial judge

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[56] *Earglow Pty Ltd v Newcrest Mining Ltd* [2015] FCA 328 at [132].
[57] *McMullin v ICI Australia Operations Pty Ltd (No 6)* (1998) 84 FCR 1 at 4.
[58] *Courtney v Medtel Pty Ltd* (2002) 122 FCR 168 at [48].
[59] *Earglow Pty Ltd v Newcrest Mining Ltd* [2015] FCA 328 at [33].
[60] *Kirby v Centro Properties Limited* (Federal Court of Australia, Proceeding No VID 366 of 2008) (transcript of proceeding dated 13 April 2011) at 28.

dismissed the respondents application for an order identifying the 20 largest shareholders and requiring them to give discovery. The Court of Appeal dismissed the respondents appeal on the basis that although the documents and particulars sought may have been relevant to the common issues, it was within the primary judge's power to determine that the submissions advanced by the respondents were not sufficient to justify exercising its discretion.[61]

[61] *National Australia Bank Ltd v Pathway Investments* (2012) 265 FLR 247.

E: Settlement of Class Actions

Settlement Must be Approved by the Court

Settlements are usually viewed as a form of contract in which the parties can confidentially settle their dispute in whatever way they agree upon. The fairness of the settlement amount is not examined provided the parties are competent and not under any disability. In class actions the settlement is argued to require judicial oversight because the lawyer for the group is potentially an unreliable agent of the group and the group is unable to effectively monitor the lawyer. In terms of principal (group) and agent (lawyer), the principal has too little at stake to expend resources monitoring the agent and the agent has superior information. Traditional adversarial positions dissipate in the settlement approval context and the judge must be alive to the possibility of conflict and collusion – the applicants' lawyers may collude with respondents and there may be conflict between the representative party and other group members or between sub-groups.[62] In the Australian context the advent of litigation funding adds to, or alters, the above concerns because the funder may be able to monitor the lawyers but it may also collude with those lawyers and be an unreliable agent for group members. Consequently, it is essential that the court exercise a critical supervisory role to ensure that a settlement is in the interest of all the group members.[63]

The the *Federal Court of Australia Act 1976* (Cth) therefore provides the Court with the power, indeed the responsibility, to examine the terms upon which a representative proceeding is being settled or discontinued.[64] Section 33V provides:

> *(1) A representative proceeding may not be settled or discontinued without the approval of the Court.*
>
> *(2) If the Court gives such an approval, it may make such orders as are just with respect to the distribution of any money paid under a settlement or paid into the Court".*

Consequently, the representative proceeding may not be settled or discontinued without the approval of the court. In addition the notice provision, section 33X provides:

> *Unless the Court is satisfied that it is just to do so, an application for approval of a settlement under section 33V must not be determined unless notice has been given to group members.*

Reference should also be made to section 33ZF as this provision is relied upon by the Court to allow it to address novel issues that arise as part of a settlement.[65]

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[62] Michael Legg, "Judge's Role in Settlement of Representative Proceedings: Lessons from United States Class Actions" (2004) 78 *Australian Law Journal* 58 at 68 cited in *Courtney v Medtel Pty Ltd (No. 5)* (2005) 212 ALR 311 at [38]. See also *Mercedes Holdings Pty Ltd v Waters (No 1)* [2010] FCA 124 at [9].
[63] *Australian Securities and Investments Commission v Richards* [2013] FCAFC 89 at [8].
[64] *Taylor v Telstra Corporation* [2007] FCA 2008 at [56]; *Mercedes Holdings Pty Ltd v Waters (No 1)* [2010] FCA 124 (dealing with discontinuance); Practice Note CM17 at [10].
[65] Michael Legg, *Case Management and Complex Civil Litigation* (2011) Federation Press pp 234-235.

Settlement approval steps

Settlement usually involves a three-step process. First a settlement agreement is negotiated and executed. This will contain essential caveats such as approval by the Court pursuant to section 33V.[66] It may annexe the orders to be sought from the Court as part of the settlement process. The second step is usually approaching the Court for the approval of a notice to group members advising of the terms of the settlement and the date for the subsequent settlement approval hearing. Alternatively, and much less common, the court may be approached for an order that notice be dispensed with. The third step is the settlement approval or fairness hearing at which group members can provide objections and the settlement is formally approved or disapproved. In some settlements, the court may retain jurisdiction while the settlement is allocated and distributed so as to be able to monitor this process.

Notice

The practice of the Federal court is to require the applicant to give prior notice to group members advising of the application.[67] Although notice may be dispensed with if just to do so.[68] Practice Note CM17 provides guidance as to the content of the notice by specifying that it should usually include:[69]

(a) a statement that the group members have legal rights that may be affected by the proposed settlement;

(b) a statement that an individual group member may be affected by a decision whether or not to remain as a group member (where the opt-out date has not already passed or where there is a further opportunity to opt out);

(c) a brief description of the factual circumstances giving rise to the litigation;

(d) a description of the legal basis of the claims made in the proceedings and the nature of relief sought;

(e) a description of the group on whose behalf the proceedings were commenced;

(f) information on how a copy of the statement of claim and other legal documents may be obtained;

(g) a summary of the terms of the proposed settlement;

(h) information on how to obtain a copy of the settlement agreement;

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[66] *Jarra Creek Central Packing Shed Pty Ltd v Amcor Ltd* [2011] FCA 671 at [17] and *Paxtours International Travel Pty Ltd v Singapore Airlines Ltd* [2012] FCA 426 at [16]. There may also be other caveats such as the settlement amount not exceeding a specified amount: *Dorajay Pty Ltd v Aristocrat Leisure Ltd* (2008) 67 ACSR 569; [2008] FCA 1311 at [3], [7].

[67] Federal Court of Australia Act 1976 (Cth) ss 33X(4) and 33Y; *Pharm-a-Care Laboratories Pty Ltd v Commonwealth (No 6)* [2011] FCA 277 at [18]; *P Dawson Nominees Pty Ltd v Brookfield Multiplex Ltd (No 4)* [2010] FCA 1029 at [5]; Practice Note CM17 at [10.2].

[68] Federal Court of Australia Act 1976 (Cth) ss 33X(4); *Vernon v Village Life Ltd* [2009] FCA 516 at [42], [76].

[69] Practice Note CM17 at [11.5]. See also Peter Cashman, *Class Action Law and Practice* (Federation Press, 2007) at 351 and Michael Legg, "Judge's Role in Settlement of Representative Proceedings: Lessons from United States Class Actions" (2004) 78 *Australian Law Journal* 58 at 67-68.

(i) an explanation of who will benefit from the settlement;

(j) where all group members are not eligible for settlement benefits -- an explanation of who will not be eligible and the reasons for such ineligibility;

(k) an explanation of the Court settlement approval process;

(l) details of when and where the Court hearing will be and a statement that the group member may attend the Court hearing;

(m) an outline of how objections or expressions of support may be communicated, either in writing or by appearing in person or through a legal representative at the hearing;

(n) an outline of any steps required to be taken by persons who wish to participate in the settlement (in the event that affirmative steps are required);

(o) an outline of the steps required to be taken by persons wishing to opt out of the settlement if that is possible under the terms of the settlement; and

(p) information on how to obtain legal advice and assistance.

The Court's have observed that it is of importance that any notice be both accurate[70] and expressed in as plain and simple language as is consistent with the information sought to be communicated,[71] because a misleading or inaccurate notice may impact the decision of a group member.[72] The form of the notice is also important as it will impact whether group members have the content of the notice brought to their attention.

Consequently, the form and content of the notice will be frequently subject to close attention by the parties and the Court.[73]

Application for Approval

An application for approval of a proposed settlement is made by motion on notice supported by affidavit.[74] This can be made at the same time that notice is sought or after the court has approved the giving of notice. If the former, the application will need to be stood over to the date of the settlement approval hearing.

The orders which are commonly sought include: (a) approval of the proposed settlement, (b) approval of legal fees and disbursements, (c) approval of the reimbursement of costs incurred by the applicant or nominated group members, (d) approval of any scheme for distribution of the settlement payment (e) confidentiality of evidence provided in support of the settlement; and (f) disposing of the proceeding (eg by dismissing the application).[75] The affidavit in support will usually state:[76]

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[70] *Williams v FAI Home Security Pty Ltd* (No 3) [2000] FCA 1438 at [24].
[71] *McMullin v ICI Australia Operations Pty Ltd* (1998) 156 ALR 257 at 260; *Courtney v Medtel Pty Ltd* [2001] FCA 1037 at [10]–[11].
[72] *King v GIO Australia Holdings Ltd* [2001] FCA 270 at [14]–[15].
[73] *Pharm-a-Care Laboratories Pty Ltd v Commonwealth (No 6)* [2011] FCA 277 at [11].
[74] *Pharm-a-Care Laboratories Pty Ltd v Commonwealth (No 6)* [2011] FCA 277 at [7].
[75] Practice Note CM17 at [11.3].
[76] Practice Note CM17 at [11.4].

(a) how the settlement complies with the criteria for approving a settlement;

(b) why the proceedings have been settled on particular terms;

(c) the effect of those terms on group members (ie the quantum of damages they are to receive in exchange for ceasing to pursue their claims and whether group members are treated the same or differently and why);

(d) the means of distributing settlement funds;

(e) the terms of fee and retainer agreements including the reasonableness of legal costs;

(f) a response to any arguments against approval of settlement raised by group members;

(g) any issues that the Court directs be addressed;

(h) a hearing of the application for settlement approval, including consideration of any group members' objections to the settlement and an order dealing with costs.

(i) Additional affidavits may be needed to respond to such matters as group member objections or issues raised by the court.

Settlement Approval Hearing

There will be a settlement hearing for the judge to consider the evidence in relation to s 33V and to determine if the orders sought should be made. If the settlement is approved there will follow various steps to administer the settlement, including identifying the group members if this has not previously occurred, calculating each group members claim and distributing payments.

Leightons Holdings Limited Shareholder Class Action Settlement

Inabu Pty Ltd, as trustee for the Alida Superannuation Fund, commenced a class action in the Federal Court of Australia against Leighton in relation to two major construction projects, the Brisbane Airport Link project (BAL Project) and the Victorian Desalination Plant project (VDP Project), and a Dubai based property construction joint venture, the Al Habtoor Leighton LLC (Habtoor Leighton).

The class action alleged that in the period 16 August 2010 to 11 April 2011, Leighton had breached its continuous disclosure obligations under s 674 of the *Corporations Act 2001* (Cth) and various prohibitions on misleading or deceptive conduct because it:

(a) failed to disclose that there were material matters arising either individually or collectively from the BAL Project and VDP Project and likely impairments on the Habtoor Leighton investment which made it likely that Leighton would not achieve its profit forecasts for the 2011 financial year; and

(b) made statements that misled or deceived shareholders about the profit forecasts and performance for the 2011 financial year and performance.

Proceedings were commenced on 30 October 2013. By mid-May 2014 a settlement, subject to the approval of the court as required for class actions, had been reached. This was before any defence

was filed. The settlement provided for Leighton to pay an amount of $69.45 million, including $3.9 million for the applicant's legal costs. The amount that each group member would actually receive depended on the number and quantum of claims that participated in the settlement.[77]

Leighton had previously settled an Australian Securities and Investments Commission investigation into the BAL Project, VDP Project and Habtoor Leighton. This settlement required Leighton to pay $300,000 in fines and enter into an enforceable undertaking to improve continuous disclosure policies and procedures.[78]

Settlement Prior to Opt Out

The settlement reached in the Leighton's class action occurred prior to the mandatory requirement that group members be given an opportunity to opt out, or exclude themselves, from the proceedings.[79] As a result Jacobson J was asked to approve notices that combined the separate forms of notice that would ordinarily be sent in the case of a proposed settlement with those which give notice of group members' entitlement to opt out of the proceeding.

It was also determined that there needed to be two different forms of the relevant notices because of the different status of funded group members (who had entered into a funding agreement with International Litigation Funding Pte Ltd) and other unfunded group members. Funded group members as part of the obligations under the funding agreement had agreed to take part in the proceeding and provided the necessary information in relation to the purchase and sale of Leighton shares for the relevant period.

[77] A Loss Assessment Formula was devised to calculate payments to individual group members but was ordered to be treated as confidential by the Court.
[78] ASIC, "Leighton Holdings complies with three ASIC infringement notices for alleged continuous disclosure breaches and ASIC accepts compliance enforceable undertaking", Media Release 12-53MR, 18 March 2012.
[79] *Federal Court of Australia Act 1976* (Cth) s 33J.

The steps in the settlement process were:

Date	Step
6 March 2014	Mediation
16 May 2014	Settlement agreement executed
6 June 2014	Hearing for approval of opt out and settlement notices by the court
Before 4pm on 10 June 2014	Notices to be displayed on the website of the Applicant's solicitor
Before 4pm on 13 June 2014	Mailing of notices to funded and unfunded group members and publication of notices in newspapers
18 July 2014	Persons wishing to opt out must return form Unfunded group members must register to participate in settlement
1 August 2014	Group members wishing to oppose settlement must provide notice Unfunded group members must provide a statutory declaration verifying their shareholdings in Leighton
15 August 2014	Settlement approval hearing
25 August 2014	Orders made approving settlement

Leighton's Ability to Withdraw from the Settlement

The timing of the settlement meant that a group member who did not want to be bound by the settlement on offer could opt out of the class action. To guard against Leighton reaching a settlement that did not in fact settle the claims against it, the settlement agreement provided that Leighton may issue a withdrawal notice where a group member who held a sufficiently large number of shares in Leighton elects to opt out of the proceedings. Presumably this terminated the settlement agreement.

The settlement agreement also allowed for the issue of a large shareholder opting out of the settlement to be dealt with by Leighton being able to require an amount in respect of such a group member to be held in escrow for a period of two years. If the shareholder did not make a claim against Leighton in respect of the matters the subject of this proceeding during the escrow period, then the escrow amount would be distributed to participating group members according to the terms of the settlement scheme. This approach allows for a settlement to go ahead but also protects a respondent against additional claims by shareholders who opt out of the class action.

The withdrawal and escrow conditions were not subsequently enlivened as only seven opt out notices were received and they did not cover a sufficient number of shares.

Identification of Group Members

To identify unfunded group members who had not previously come forward, a two-step procedure was adopted.

First, Leighton provided a mail house distribution service with the details of all shareholders recorded on the Leighton share register who purchased securities in Leighton between 16 August 2010 and 11 April 2011 (inclusive). The mail house then communicated the notices by email, or if no email address existed or the email failed to send, by prepaid ordinary post to the shareholder at the address recorded on the share register. The information from the share register was not to be disclosed to the applicant, applicant's solicitor or the litigation funder.

Second, the notices were also communicated through being displayed on the website of the Applicant's solicitor and through publication in one weekday edition of the *Australian Financial Review* and one weekday edition of *The Australian*. The applicant's solicitor was also permitted to publish notices in any further newspaper or on any website that it considered appropriate to bring the notices to the attention of group members.

The court's orders also made provision for notices to be communicated to funded group members by email and prepaid ordinary post. Contacting funded group members would be more straightforward as they were known having communicated with the lawyer and funder previously.

Class Closure

A common feature of Australian class actions that reach a settlement is that the court is asked to "close the class"[80] which entails establishing a process for group members to identify themselves so they can participate in the settlement. In the Aristocrat Leisure shareholder class action Stone J observed that when an opt out group definition is used it will eventually be necessary to close the class because:[81]

> *Until the class of participating group members is closed and the members of the closed class identified, there can be no final settlement and no distribution of settlement monies to members of the class.*

However, in addition to requiring group members to come forward, courts have also made orders that group members who do not come forward lose their claims. In the Leighton class action Jacobson J explained:[82]

> *... that if the group member does nothing and the settlement is approved, the group member will not receive compensation but will be bound by the settlement and will not be able to claim compensation from Leighton in the future in relation to the circumstances giving rise to the present proceeding.*

Class closure means that group members face a "use it or lose it" situation in relation to their claims. Jacobson J was prepared to make orders closing the class here because it was necessary for an

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[80] The closing of the class is a step that occurs in an open or traditional opt-out class action. The process is to be compared with a closed class where the group is defined from the outset in a manner that limits the group to ascertainable persons. See *Matthews v SPI Electricity (Ruling No. 13)* [2013] VSC 17 at [18]-[24].

[81] *Dorajay Pty Ltd v Aristocrat Leisure Limited* (2008) 67 ACSR 569 at [13].

[82] *Inabu Pty Ltd v Leighton Holdings Ltd* [2014] FCA 622 at [17].

efficient and orderly distribution of funds, the class action had attracted extensive media coverage and there is sufficient time from when the notices are given for group members to come forward.

After the time for group members to register their participation in the class action had closed the court recorded that 6000 people had registered, 3000 of which were unfunded group members. Group members who registered after the deadline were not entitled to participate in the settlement. However Jacobson J amended his earlier orders to include those group members in the settlement.

Approval of the Settlement

As explained above a class action may not be settled or discontinued without the approval of the Court.[83]

In the Leighton class action the main concerns discussed by Jacobson J were the availability of information to determine the fairness of an early settlement and the unknown numbers of unfunded group members.

However, the settlement was after a mediation before an experienced mediator in the light of an extensive exchange of information between the parties including discovery of agreed categories of documents, and the exchange of expert loss reports and position papers.

The affidavit supplied by the applicant's solicitor explained that usually where there were funded and unfunded group members, the funded group members are protected from dilution of their claims by a minimum amount being reserved for them. This had not happened in the current settlement. However, while the number of unfunded group members that registered was high the quantum of their claims was relatively low compared to the claims of funded group members.

His Honour also noted a number of other issues including the unsettled law on causation and calculation of damages, an independent costs consultant's report on legal costs and a claim for the applicant to be reimbursed.

[83] *Federal Court of Australia Act 1976* (Cth) s 33V.

Figure 1

Anatomy of Shareholder Class Action

The key features of a shareholder class action are:

1. The litigation is commenced by an applicant who is also the representative party. The applicant can be an individual or a corporation.
2. The applicant brings the class action on behalf of group members. The applicant and the group members, who do not opt out of the class action, are bound by its outcome.
3. The pleadings set out the issues to be determined that are common to the applicant and group members – the common questions.
4. The pleadings define who is a group member – usually a person who purchased shares in the respondent corporation between certain dates and suffered loss as a result of the corporation's alleged contraventions of the law. It may also be a condition of group membership that the person has entered into a litigation funding agreement with a named funder.
5. The applicant is responsible for making the decisions about the litigation and instructing the lawyers. The applicant will be responsible for paying the lawyer's fees and disbursements unless some other arrangement is put in place. A litigation funder may pay the costs in return for a share of any recovery. A lawyer may act on a "no-win no-fee" basis.
6. The applicant, but not group members, are liable for an opponent's costs if the litigation is unsuccessful. A litigation funder may indemnify the applicant against these costs in return for a share of any recovery.
7. The applicant is a party to the litigation. Group members are usually not parties. The applicant, but usually not group members, may need to provide discovery.
8. The trial of the class action usually proceeds in two stages. In stage 1 the applicant's claim is tried as a vehicle to determine the common questions.
9. In stage 2 the non-common or individual issues are resolved. This may require group members to prove individual issues such as causation and loss, which may in turn require the provision of discovery and exposure to an adverse costs order if unsuccessful.
10. However, most shareholder class actions settle, which depending on the timing of the settlement, may mean that stage 1 and/or stage 2 of the trial do not occur.