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RESEARCH PAPER #7: CLASS ACTIONS: COMMERCIAL FUNDING, REGULATION AND CONFLICTS OF INTEREST

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Class actions: commercial funding, regulation and conflicts of interest.

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> *The named plaintiff is no ordinary client. The lawyer's clients include persons not named in … the proceedings. The judicial role takes on aspects of inquisitorial legal systems. And the lawyer is zealous advocate, venture capitalist, and private attorney general in equal measure.*[3]

Since the introduction of the Part IVA regime in 1992, class actions in Australia have been the subject of considerable controversy. In recent years, the forensic focus has been on litigation funding of class actions. The commercial litigation funding market evolved to fill the void left by the failure of successive governments to implement the recommendations of numerous independent law reform bodies at state and federal levels calling for the establishment of a public fund.

Thus, the commercial funding of class actions has become the subject of a multitude of interlocutory disputes and appeals by respondents seeking to de-rail litigation against them; divided views among members of the state and federal judiciaries;[4] polarised political and media debate; several further major investigations and reports by law reform agencies; a current inquiry by the Parliamentary Joint Committee on Corporations and Financial Services (the Joint Committee) and recent regulatory and legislative reforms at state and federal levels.

Much of this could have been avoided if a publicly-funded class action fund had been established. Such a fund would have required little public funding as it would be likely to become self-financing. Furthermore, the funding of cases by a public body would have enhanced access to justice in matters not considered sufficiently profitable to attract commercial funders, as well as significantly reducing funding commissions and overall transaction costs in funded cases.

The increasing commercialisation of both litigation funding and the private practice of law has led to very substantial costs and delays in resolving class actions and a diminishing return to class members. This has important policy implications for access to justice and the operation of the civil justice system.

In this Research Paper we focus on (a) the benefits and disadvantages of commercial litigation funding; (b) recent regulatory changes and other possible reform options; and (c) the pervasive problem of conflicts of interest in the conduct of class action litigation.

Before proceeding to the detail, we make a number of observations about the changing landscape of legal practice and class action litigation.

1. The changing nature of legal practice.

In recent years, there has been a familiar pattern of law firm expansion and merger at a national level and international level. As we note below, this has had a marked impact on the incidence and character of class action litigation.

Many large Australian commercial law firms have relatively recently entered into various forms of arrangement with other large international law firms in order to have a larger global presence, and to achieve greater penetration into lucrative emerging markets for legal services in Asia and in China in particular.[5]

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[3] Jasminka Kalajdzic, 'Self Interest, Public interest, and the Interests of the Absent Client: Legal Ethics and Class Actions Praxis' (2011) 49 *Osgoode Hall Law Journal* 1.

[4] Including both the Federal Court and the High Court.

[5] The 'internationalisation' of legal practice has a number of other dimensions. To reduce costs to clients and/or increase profits earned by lawyers, many firms in countries where the cost of lawyers is high, outsource

For example, former leading Australian commercial law firm Mallesons Stephen Jaques changed its name and formed a new international business with China's biggest law firm, King & Wood. In March 2012, King & Wood Mallesons became the largest law firm in the Asia-Pacific region. At that time, the new firm had 380 partners, 1800 lawyers, 11 offices in China, and 5 offices in Australia. Previously, Mallesons had 176 partners and 740 lawyers. According to the firm's current website, the firm has 2400 lawyers in 28 locations throughout the world.

This international trend has not been confined to commercial firms who act predominately for the business community. Australian plaintiff law firm Slater & Gordon initially acquired the UK law firm Russell Jones & Walker[6] for around $80 million. Slater & Gordon established a wholly-owned subsidiary company in the UK to manage its operations. The acquisition included the claims management entity 'Claims Direct' which acts as a marketing cooperative for several UK law firms.

Slater & Gordon was the first law firm to become a listed public company and, following a number of acquisitions of other personal injury law firms, the firm previously had about 50 offices throughout Australia. At the time when Slater & Gordon sought to list on the stock exchange, certain 'regulatory requirements' were adopted in order to address ethical issues, and in particular the potential tension or conflict between corporate obligations to shareholders and professional duties of a law firm to clients.

Subsequently, serious financial problems arose after the firm in the UK acquired the professional services division of London based Quindell for approximately $1.3 billion in 2015. Substantial debt and an increasing dependence on high-volume, low-cost cases were exacerbated when proposals were announced in the UK to remove various rights for people injured in motor accidents to obtain compensation for pain and suffering in minor soft tissue injury claims and to increase the threshold for cases heard in the Small Claims Court.

Decreasing profitability, concerns about the method of accounting for 'work in progress', a major drop in market capitalisation and a dramatic drop in the share price led to further problems including the commencement of a number of class action proceedings against Slater & Gordon and various advisers in Australia.

Slater & Gordon, like its main competitor Maurice Blackburn, had historically focused on personal injury claims and industrial law. Various tort reforms introduced throughout Australia undermined the financial viability and profitability of traditional personal injury work and both firms embarked upon an expansion into the area of class actions.

The increasing size and geographical reach of both firms in Australia, combined with the maturation of the class action regime, led to a considerable expansion of class action litigation. In 2000, Melbourne and Brisbane based Maurice Blackburn merged with the Sydney based firm of Cashman & Partners which had specialised in product liability and class action litigation for a decade. In recent years, Maurice Blackburn established its own litigation funding entity, based in Ireland.

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work to countries where the cost of legal labour is significantly lower. These developments parallel those occurring in the corporate world where the production of goods and the provision of services by many companies have been relocated to countries with cheaper labour and materials. This often gives rise to adverse effects on employment and the economy in the countries from which production and services are re-located. See generally: Milton C Regan Jr and Palmer T. Heenan, 'Supply Chains and Porous Boundaries: The Disaggregation of Legal Services' (2010) 78 *Fordham Law Review* 2137.

[6] Russell Jones & Walker was reported to have about 425 staff across 10 locations in the UK and generated about 60% of its profit from personal injury litigation.

While traditional plaintiffs' firms continued to mainly represent plaintiffs in class action litigation the international mega firm Quinn Emanuel Urquhart & Sullivan LLP established offices in Australia and has developed an extensive practice acting for both plaintiffs and defendants in class action litigation. It purports to be 'the largest law firm in the world devoted solely to business litigation and arbitration' with more than 800 lawyers and 23 offices in ten countries. According to the firm's website, it has recovered over US$70 billion for plaintiffs and won 88% of trials and arbitrations.[7] According to its Facebook page, since 2011 profits per equity partner have been the second highest in the world.

The increasing commercialisation of the practice of law and the rise of 'mega law firms' has attracted some attention, including from legal ethics scholars.[8]

Professional associations vary from jurisdiction to jurisdiction as to whether they support law firms being able to become incorporated, multidisciplinary practices, or publicly listed traded entities owned by non-lawyers.

An American Bar Association (ABA) Commission, some time ago, recommended that non-lawyers be allowed to have an equity stake in law firms for which they work while proposing that existing bans be maintained in relation to outside investment in law firms of a type that became permissible in Australia and the United Kingdom.[9] Moreover, the ABA Commission on Ethics 20/20 considered various alternative business structures and opposed any move that would permit law firms to become listed entities or multidisciplinary partnerships.[10] There has also been litigation in the United States challenging laws that preclude external funding of law firms[11]

The private practice of law continues to evolve; from the provision of legal services by individual professionals or small scale professional practices to large scale national and international commercial entities focused on maximizing profit. Increasing numbers of small-scale professional partnerships have developed into incorporated legal practices, multi-disciplinary commercial entities and public listed companies. Various international law firms have opened their own offices in Australia or entered into collaborative arrangements with Australian firms.

1.1 *The changing nature of civil litigation*.

Nowhere is the changing face of legal practice more apparent than in the area of class action law. Traditional civil litigation, in which the only participants are the individual parties with personal claims and defences, has been superseded, in some Australian jurisdictions, by large, complex, expensive and protracted class action proceedings in which the legal interests of hundreds, thousands, or millions of people may be directly affected.

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[7] See <https://www.quinnemanuel.com/>.

[8] See, e.g., Nancy Moore, 'Regulating Law Firm Conflicts in the 21st Century: Implications of the Globalization of Legal Services and the Growth of the Mega Firm' (2005) 18 *Georgetown Journal of Legal Ethics* 521.

[9] For a detailed review of arguments and policy positions in respect of non-lawyer ownership of law firms, see Andrew Grech and Tahlia Gordon, *Should Non-lawyer Ownership be endorsed and encouraged?* May 2015, <http://www.creativeconsequences.com.au/non-lawyer-ownership.pdf>.

[10] The Commission operated for a period of three years and made various recommendations on numerous topics.

[11] Perhaps not surprisingly, one United States law firm, Jacoby & Meyers, instituted litigation to challenge laws in three United States jurisdictions that prevented law firms from utilising outside funding.

In recent years, class action litigation in Australia has encompassed shareholder actions, claims arising out of investment and property schemes, product liability claims, cartel class actions, proceedings against governments; industrial class actions, consumer class actions and proceedings arising out of environmental and other disasters.[12] From the introduction of the statutory class action regime in the Federal Court on 4 March 1992 to 3 March 2014, 329 class actions were commenced, an average of almost 15 per year.[13] Many were related proceedings, filed in relation to the same legal dispute. In the most recent calendar year for which data are available (2019), a total of 59 class actions were commenced.[14]

Statutory class action procedures were designed to facilitate access to justice and to provide for the resolution of multiple claims in an efficient and cost-effective manner. They have, however, been bedevilled with procedural complication, delay, interlocutory warfare, appeals and inordinate cost in many instances. In other Research Papers, we provide empirical data in respect of transaction costs and delay, analyse a number of the factors which have contributed to these problems and outline various suggested solutions and reforms.

1.2 *The changing nature of funding for civil litigation.*

Australian class action litigation has confronted funding and financing difficulties since the introduction of statutory 'opt-out' class action procedures.

Such difficulties relate to both the means of financing the conduct of proceedings and the vexed issue of potential liability for adverse costs in the event that the class action is unsuccessful. The Australian Law Reform Commission recognized these potential difficulties and recommended that a class action fund should be introduced. This recommendation was not taken up by the Commonwealth Parliament. Moreover, although Part IVA of the *Federal Court of Australia Act 1976* (Cth) was implemented following the ALRC report, the Government did not accept all of the Commission's recommendations, including the recommendations concerning contingency fees.[15]

The statutory immunity of class action members from costs orders[16] places the representative party (and a successful respondent) in an invidious position. Because a representative party is potentially liable for the costs of an unsuccessful action (or the costs of part of the action even where there is a successful outcome[17]) there is a considerable disincentive (and no financial incentive) to take on the representative role.

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[12] Examples of each are cited in Law Council of Australia, Federal Court of Australia, *Case Management Handbook* (2011) chapter 13 on 'Representative Proceedings-Class Actions' added in 2014, [13.13]. For a classification of the types of claims encompassed by class actions commenced in the Federal Court, see Vince Morabito, An empirical study of Australia's class action regimes: third report, *Class Action Facts and Figures-Five years later*, November 2014, Tables 3-5, 10-12.

[13] Ibid 2.

[14] Vince Morabito, 'Shareholder class actions in Australia - myths v facts' (12 November 2019) 12 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3484660>.

[15] See *Senate Debates* 12 September 1991 at 1448. The Commission did not recommend percentage-based fees but was of the view that a higher than 'normal' fee should be permitted to compensate for the risk.

[16] *Federal Court of Australia Act 1976* (Cth) s 43(1A).

[17] See, e.g., *Peterson v Merck Sharpe & Dohme (Aust) Pty Ltd (No 5)* [2010] FCA 605 (18 June 2010). The primary judgment on liability was overturned on appeal and an application for special leave to the High Court was unsuccessful.

In Federal proceedings, at least, any legislative constraint on the recovery of costs against a representative party receiving legal aid[18] is inapplicable. In any event, due to budgetary constraints and the dramatic cuts in federal funding of legal aid, it is presently unrealistic to expect any Australian legal aid authority to provide adequate funding or adverse costs protection in class action proceedings. Legal aid bodies may, however, play an important role in funding or conducting test cases that may have an important bearing on class action litigation, such as the successful case in the Federal Court in Victoria arising out of the *Robodebt* saga.[19]

As noted, the respondent is also in an invidious position given the statutory protection of group members in relation to costs. If the action fails (in whole or in part) any costs order would normally be made only against the unsuccessful representative party who may not have the financial means to pay it.

In the absence of some form of statutory fund, the options for the financing of class action litigation include the following:

- funding and/or adverse costs indemnity by group members themselves
- funding and/or costs indemnity by the law firm(s) conducting the proceeding
- funding and/or costs indemnity by legal aid
- funding and/or costs indemnity by a third party on a philanthropic (non-profit) basis
- third party funding and/or costs indemnity by a commercial party or entity for profit
- funding and/or costs indemnity by an organization (e.g. a trade union[20]) of which the class members are part
- funding and/or costs indemnity by a public interest organisation or by a philanthropic funding body[21]
- reliance on 'opt-in' class action proceedings brought by regulators (the ACCC or ASIC) on behalf of claimants who agree to proceedings being brought on their behalf
- costs indemnity through 'after the event' commercial insurance.

Some combination of these options may be adopted.

Whatever the advantages and disadvantages of each of these options, in practice third-party funding by commercial litigation funders has become the primary means of financing most class action litigation in Australia in recent years.[22] As noted in the *Case Management Handbook* in 2014: 'litigation funding has proven to be the life-blood of much of Australia's representative proceeding litigation at federal and state level.'[23]

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[18] Such constraints arise pursuant to state or territory legal aid legislation. See, e.g., s 47 *Legal Aid Commission Act 1979* (NSW). The provisions of the *Legal Aid Bill 1974*, which would have conferred a degree of immunity from adverse costs orders on parties in receipt of Commonwealth legal aid, lapsed with the demise of the Whitlam Government and has not been resurrected since.

[19] *Amato v Commonwealth of Australia* (VID611 of 2019) conducted by Victoria Legal Aid.

[20] See Jane Caruana and Vince Morabito, 'Australian Unions- the Unknown Class Action Protagonists' (2011) 4 *Civil Justice Quarterly* 382.

[21] Such as the Grata Fund. See <https://www.gratafund.org.au/>.

[22] Although the first shareholder class action was conducted on a speculative basis by the law firm acting for the representative party (Maurice Blackburn Cashman) without any arrangement in place to cover any adverse costs ordered against the representative party had the case been unsuccessful: *King v AG Australia Holdings Ltd (formerly GIO Australia Holdings Ltd)* [2003] FCA 980 (17 September 2003).

[23] Law Council of Australia, Federal Court of Australia, *Case Management Handbook*, (2011), chapter 13 on Representative Proceedings-Class Actions added in 2014 [13.12].

Thus, coupled with the abovementioned trends towards the commercialisation of the practice of law and the expanded use of class actions, there has been a dramatic increase in the commercial funding of civil litigation by 'third party' entities seeking to maximise profits by obtaining a share of the amount recovered by the funded party. In Australia to date, the commercial funding of civil litigation has concentrated on class action proceedings but extends to other areas, including insolvency litigation.

According to Geisker and Luff,[24] the Australian litigation funding market was estimated to be worth around $3 billion in 2015, compared with a total Australian litigation market of $21.1 billion. A survey of lawyers and in-house counsel in 2018 found that more than 70% of participants cited legal finance as a growing and essential business tool for law firms and reported that there was widespread use of single case funding. The authors also noted that there was increasing use of litigation funding in a broad range of class actions. According to the Victorian Law Reform Commission,[25] by 2017 almost half of all class actions commenced in the Federal Court were supported by commercial litigation funders. By 2019, funded class actions were said to comprise 72% of all class actions commenced across all state and federal jurisdictions.[26] We provide up to date empirical data on the funding of class actions in Research Paper #5.[27]

Commercial litigation funding arrangements have also emerged in other jurisdictions and have attracted considerable professional interest and judicial scrutiny.[28] The changing nature of commercial litigation and its expanding scope is apparent from the merger of the Australian litigation funder IMF with Omni Bridgeway to form the multinational entity Omni Bridgeway Limited. The company now has 18 offices in Australia, the United States, Canada, Singapore, the Netherlands, Germany, Switzerland, Dubai, Hong Kong and London, employing over 160 'specialists' in law and finance.[29]

As noted by Duffy, the impact of the 'seismic shift' in civil litigation brought about by third-party funding 'is a topic of considerable and sometimes fierce debate.'[30]

The advantages and disadvantages of commercial litigation funding from various perspectives are set out in Research Paper #1[31] which summarises the written and oral submissions to the Joint

[24] Jason Geisker and Dirk Luff, 'Australia' in Leslie Perrin (ed.) *The Third Party Litigation Funding Law Review* (Law Business Research Ltd, 3rd ed, 2019) ch 1.
[25] Victorian Law Reform Commission, *Access to Justice and Group Proceedings*, Consultation Paper (July 2017) 8 [1.47].
[26] VLRC, *Access to Justice and Group Proceedings*, Report (March 2018) xiv [12]-[14].
[27] Peter Cashman and Amelia Simpson, 'Costs and funding commissions in class actions' Research Paper #5 (26 October 2020).
[28] See generally: Rachael Mulheron and Peter Cashman, 'Third-Party Funding of litigation: A Changing Landscape' (2008) 3 *Civil Justice Quarterly* 312; Jasminka Kalajdzic, Peter Cashman and Alana Longmore, 'Justice for Profit: A Comparative Analysis of Australian, Canadian and U.S. Third Party Litigation Funding' (2013) 61 *The American Journal of Comparative Law* 93; Rachael Mulheron, 'England's unique approach to the self-regulation of third-party funding: a critical analysis of recent developments' (2014) 73 *The Cambridge Law Journal* 570. For a recent review of litigation funding developments in various jurisdictions, see Leslie Perrin (ed.) *The Third-Party Litigation Funding Law Review* (Law Business Research Ltd, 3rd ed, 2019).
[29] See <https://omnibridgeway.com/about/overview>.
[30] Michael Duffy, 'Two's Company, Threes a Crowd? Regulating Third-Party Litigation Funding, Claimant Protection in the Tripartite Contract, and the Lens of Theory' (2016) 39 UNSWLJ 165.
[31] Peter Cashman and Amelia Simpson, 'Class actions and litigation funding reform: the rhetoric and the reality' Research Paper #1 (1 December 2020). This paper is a revised version of two research papers provided to the

Parliamentary Committee. We set out our perspectives on the advantages and disadvantages of commercial litigation funding in the following section.[32]

2. Commercial funding

2.1 *Advantages of commercial funding*

The primary advantage of commercial litigation funding is that it has facilitated access to justice by enabling the pursuit of claims that might not otherwise have been pursued.

Importantly, the fact that commercial litigation funders usually assume liability for any adverse costs order (or order for security for costs) made against a funded party removes the economic disincentive for persons to take on the mantle of representative party. It is also in the economic interests of successful respondents. Moreover, the willingness of litigation funders to finance the conduct of the litigation has facilitated the involvement of law firms that were hitherto reluctant to take on the conduct of such cases on a 'no win no fee' basis.

Furthermore, many funders employ commercial lawyers with litigation experience. Cases are carefully screened and extensive due diligence investigations are usually conducted. Only cases which appear to have substantial merit are funded. This serves as an important filter to prevent unmeritorious claims from being pursued.

Funders often seek out potential class members through various means, including media publicity and through social media and other websites, so as to maximize the number of persons who may benefit from the funded litigation.

Funders are usually concerned to reduce the transaction costs of the litigation and thus often impose budgetary constraints on lawyers. They may also organise for some of the work to be undertaken by paralegals or other legal staff with lower charge out rates, resulting in lower costs than if such work was handled by the law firms at commercial charge out rates. They also generally exercise a degree of control over the costs of the litigation.

Funders are also often proactively involved in the conduct of the litigation and in attempts to settle the proceedings.

The fact that a case is being funded by a commercial funder may have an impact on the assessment of the merit of the claim by both the respondent and the court. It is well known that reputable commercial funders engage in extensive due diligence processes, and seek expert advice, before agreeing to fund class action litigation.

Moreover, the support of a litigation funder will usually level the litigious playing ground and may preclude the respondent from engaging in a forensic war of attrition in the hope that the applicant will either be deterred from pursuing it to the end or will accept a cheap settlement.

Joint Parliamentary Committee in the form of supplementary submissions: Research Papers #1 (16 July 2020) and #2 (14 August 2020).

[32] Views of stakeholders on the advantages and disadvantages of commercial litigation funding in written and oral submissions to the Joint Parliamentary Committee are set out in Peter Cashman & Amelia Simpson, 'Class actions and litigation funding reform: the views of class action practitioners' Research Paper #3 (17 September 2020, revised 1 December 2020).

Traditionally, funders assumed that they may only be paid pursuant to individual contractual arrangements entered into with class members. Thus, many funded class actions have been limited to persons who have consented to the conduct of proceedings on their behalf. This had the advantage of certainty as to the ambit and likely value of the claims of class members. This had obvious advantages for defendants because they are better able to estimate their potential liability and this may enhance the prospect of settlement.[33]

In any event, a transformation from limited 'opt-in' cases to open 'opt-out' class actions followed the acceptance by the Full Federal Court[34] that there was power to make common fund orders. The relatively recent reversal of this, following the decision of the High Court in *Brewster,*[35] has led to a re-kindling of interest in 'opt-in' proceedings and as yet unresolved forensic disputation and appeals concerning whether the courts are empowered to make common fund orders at the conclusion of the case, pursuant to statutory or equitable powers that were not dispositively dealt with by the High Court in *Brewster.*

2.2 *Alleged adverse consequences of commercial funding*

The high threshold of merit adopted by litigation funders means that many more risky, but nonetheless meritorious, cases are unlikely to be funded. In addition, the high commercial return required by funders results in the rejection of smaller, albeit substantial, cases.

Funders are disinclined to fund personal injury or product liability class actions for a variety of reasons, including the common requirement of proof of causation in such cases, particularly those involving injuries and loss allegedly arising out of the use of prescription drugs or therapeutic devices.[36]

In a number of instances, funding commissions are calculated as either a percentage of the recovery or a multiple of the costs outlaid by the funder. In some instances, funding agreements provide that the funder is entitled to receive the *higher* of these amounts. In rare instances, it is the *lower* of the amounts. Commissions calculated on the basis of a multiple of expenditure provide an obvious economic incentive to maximise the financial outlay and this is likely to increase transaction costs and delay and lead to an increased deduction from compensation payments otherwise payable to class members. Equally problematic are funding agreements that provide for an increase in the percentage payable to the funder with the effluxion of time.

It is also the case that some funders who provide the capital for investment utilise other professional personnel to manage their investment. Depending on the nature of the financing and remuneration arrangements with such personnel, additional economic incentives may serve to increase expenditure and protract delay. One such example is a monthly or other periodic project management fee payable to the persons or entity managing the litigation funding arrangements.

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[33] See King & Wood Mallesons, *Class Actions in Australia: The Year in Review 2011*, 9.

[34] *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148; (2016) 245 FCR 191.

[35] *BMW Australia Ltd v Brewster; Westpac Banking Corporation v Lenthall* [2019] HCA 45.

[36] See Vince Morabito and Vicki Waye, 'Financial arrangements with litigation funders and law firms in Australian class actions' in Willem van Boom (ed.) *Litigation, Costs, Funding and Behaviour: Implications for the Law* (Taylor & Francis, 2016) 155, 160-1.

To date in Australia, the financing of class action litigation by third party funders has led to what some commentators (including judges[37]) have contended are other undesirable consequences.

Commercial litigation funding has resulted in restricted 'opt-in' classes where the ambit of beneficiaries is confined to those who have agreed to enter into contractual litigation funding arrangements. Thus, access to justice by all those similarly affected has been curtailed and this undermines one of the key rationales for the class action regime.[38]

Moreover, leaving aside adverse costs issues, if you have individual instructions from all those on whose behalf proceedings are to be brought you do not necessarily need to rely upon the class action procedural mechanism at all. Other creative procedural options are available.

The conversion of the statutory 'opt-out' scheme to 'opt-in' classes has given rise to a considerable amount of satellite litigation and appeals designed to de-rail the proceedings in their entirety.[39]

Closed classes may also lead to requests for particulars of the claims of all of the individual class members and/or limited 'discovery' in respect of documents in the possession of individual claimants.[40]

Limiting classes to those who agree to participate may better enable the claims of class members to be quantified, thus potentially facilitating settlement. However, defendants may be disinclined to settle while the claims of other affected persons, who are not class members, are not statute barred for fear of encouraging further litigation by such persons.

The settlement or resolution of the limited class action does not prevent, and indeed may encourage, follow-on proceedings by those who did not agree to participate in the original 'opt-in' class action(s). This is counter to the judicial efficiency rationale of the class action regime. It is also contrary to the interests of respondents to be subject to a multiplicity of proceedings arising out of the same, similar or related circumstances.

Significant amounts of time, effort and expense are incurred by law firms and/or commercial litigation funders in finding and 'signing up' eligible persons to become group members. This increases the transaction costs of the litigation.

The perceived commercial necessity to sign up individual class members encourages competition amongst law firms and has led to multiple class actions being filed in a number of instances. These may be multiple limited 'opt-in' classes and/or 'opt-out' classes which exclude those already encompassed by 'opt-in' proceedings.

The previous availability of interlocutory common fund orders (and their current potential availability at the conclusion of the proceeding) incentivised funders and law firms to file proceedings in relation to a dispute which is already the subject of litigation by other firms. Multiplicity of proceedings has become a significant problem for the class action regime.

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[37] See, e.g., Callinan and Heydon JJ in *Campbell's Cash and Carry Pty Ltd v Fostif Pty Ltd* (2006) 229 CLR 386, 486-488; Keane P, as he then was, '*Access to Justice and other Shibboleths*', paper presented at the Judicial College of Australia Colloquium, Melbourne, October 2009.

[38] Duffy (n 30) 173.

[39] See *Dorajay Pty Ltd v Aristocrat Leisure Ltd* [2005] FCA 1483, (2005) 145 FCR 394; *Rod Investments (Vic) Pty Ltd v Clark* [2005] VSC 449; *Multiplex Funds Management Ltd v P Dawson Nominees Pty Ltd* [2007] FCAFC 200; (2007) 164 FCR 275.

[40] See, e.g., *Meaden v Bell Potter Securities Limited* [2011] FCA 136 (Edmonds J).

The fact of commercial funding of class action litigation, whether of limited classes or opt-out classes, has led to a proliferation of interlocutory disputation, satellite litigation and appeals seeking to have the proceedings stayed or dismissed by virtue of the existence and/or nature of the litigation funding arrangements in place. One recent manifestation of this problem is the challenge in the Queensland Supreme Court to class action litigation brought in that State, pursuant to Part 13A of the *Civil Proceedings Act 2011* (Qld), on the grounds that the litigation funding arrangements in that case were unenforceable as they were contrary to public policy. This argument was recently rejected by the Queensland Court of Appeal.[41]

Recently, litigation has also given rise to appeals in relation to the powers to make common fund orders at the conclusion of the proceedings[42] and the methodology for resolving competing and overlapping class actions.[43]

In view of the potentially large outlays and risks, commercial litigation funders require those assisted to agree to a relatively substantial proportion of their recovery being paid to the litigation funder in the event of success. Thus, the overall net recovery received by individual class members is correspondingly reduced.

According to the initial empirical research by Professor Morabito, in the eleven Part IVA cases encompassed by his research that had settled by 2011, 30.67% of the settlement amounts were paid to the litigation funders. [44] In Research Paper #5 we present up to date empirical data on funding commissions and legal costs incurred in class actions.

Amounts paid to litigation funders will not necessarily recoup all of the legal costs incurred on behalf of the class during the conduct of the proceedings. In many cases, the legal fees and expenses incurred by the representative plaintiff exceed $10 million. Because lawyers are prohibited from charging fees as a percentage of the amount recovered, the transaction costs incurred in conducting funded class actions include both the legal fees and expenses and the commercial return to the litigation funder. As both lawyers and funders seek to make a profit from their respective contributions, the overall transaction costs are thereby increased and the net return to the class members is correspondingly decreased.

The active involvement of commercial litigation funders in the conduct of proceedings, including settlement discussions and decision-making, may complicate or exacerbate ethical and conflict of interest problems.[45] Also, the involvement of funders in the management and conduct of litigation can cause tension in the relationship with the law firm conducting the litigation.

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[41] *Gladstone Ports Corporation Limited v Murphy Operator Pty Ltd & Ors* [2020] QCA 250 (Sofronoff P, Morrison JA and Davis J).

[42] *Davaria Pty Limited v 7-Eleven Stores Pty Ltd (No 7)* [2020] FCA 1487 and *Brewster v BMW Australia Ltd* [2020] NSWCA 272.

[43] *Wigmans v. AMP Limited & Ors* (High Court of Australia Case No. S67/2020).

[44] Vince Morabito and Vicki Waye, 'Reigning in Litigation Entrepreneurs: A New Zealand Proposal' (2011) *New Zealand Law Review* 323 at 346. As noted by Morabito and Waye, there have been proposals for the capping of the amounts payable to litigation funders. One large commercial law firm acting on behalf of a tobacco company proposed that returns should be capped at 25% of any damages award: Allens Arthur Robinson '*Access to Justice Submission on behalf of Philip Morris Limited*' (2009) referred to at 349, note 114.

[45] See Duffy (n 30).

Some have expressed concern that the introduction of litigation funding, and the perceived unholy alliance between 'entrepreneurial' law firms[46] and commercial funders motivated by profit, has led to undesirable 'trafficking' in litigation whereby cases (albeit meritorious) are orchestrated by lawyers and funders, rather than initiated or driven by clients or class members.[47]

Finally, some have expressed concern at the potential for abusive or unmeritorious class actions being commenced and being improperly used to coerce settlements so as to avoid the prohibitive costs of defending the proceedings. There is little empirical evidence of this occurring in practice although the facts of the *Fostif* litigation gave rise to an understandable expression of judicial concern amongst some members of the High Court.[48]

One obvious concern of respondents who successfully defend proceedings is whether they are able to recover any costs out of the pockets of commercial litigation funders. To date, a number of cases have highlighted both legal and financial constraints on recovery from (some) litigation funders and led to a call for enhanced capital adequacy requirements.

A number of these concerns have (a) driven various proposals for (additional) regulation of the commercial litigation funding 'industry'; (b) led to the current inquiry by the Parliamentary Joint Committee and (c) resulted in further recent regulatory reforms. These and other issues in relation to regulation are referred to in the following section and in other parts of this Research Paper.

2.3 *The regulation of funded class actions*

The terms of the current inquiry by the Parliamentary Joint Committee require the Committee to inquire into and report by 7 December 2020 on:

> Whether the present level of regulation applying to Australia's growing class action industry is impacting fair and equitable outcomes for plaintiffs, with particular reference to the following:
>
> 1. what evidence is available regarding the quantum of fees, costs and commissions earned by litigation funders and the treatment of that income;
> 2. the impact of litigation funding on the damages and other compensation received by class members in class actions funded by litigation funders;
> 3. the potential impact of proposals to allow contingency fees and whether this could lead to less financially viable outcomes for plaintiffs;
> 4. the financial and organisational relationship between litigation funders and lawyers acting for plaintiffs in funded litigation and whether these relationships have the capacity to impact on plaintiff lawyers' duties to their clients;
> 5. the Australian financial services regulatory regime and its application to litigation funding;

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[46] Former High Court Justice Callinan was less than complimentary about the '*increasingly competitive entrepreneurial activities of lawyers undertaking the conduct of class actions or group actions*' in *Mobil Oil Pty Ltd v Victoria* (2002) 211 CLR 1, 73 [172]. This comment was further quoted in *Campbells Cash & Carry Pty Ltd v Fostif Pty Ltd* (2006) 229 ALR 58 [246] in the joint judgment of Callinan and Heydon JJ.

[47] See, e.g., Callinan and Heydon JJ (in dissent) in *Campbell's Cash and Carry Pty Ltd v Fostif Pty Ltd* (2006) 229 CLR 386, 486-488; Keane P, as he then was, '*Access to Justice and other Shibboleths'*, paper presented at the Judicial College of Australia Colloquium, Melbourne, October 2009. For an article which addresses many of the claims concerning collusion between law firms and funders resulting in poor settlement outcomes for class members, see Vicki Waye, 'The initiation and operations phase of the litigation funder - class action law firm relationship: an Australian perspective' (2018) 60(2) *International Journal of Law and Management* 595, 613-4.

[48] See the joint judgment of Callinan and Heydon JJ (in dissent) in *Campbell's Cash and Carry Pty Ltd v Fostif Pty Ltd* (2006) 229 CLR 386, 486-488.

6. the regulation and oversight of the litigation funding industry and litigation funding agreements;
7. the application of common fund orders and similar arrangements in class actions;
8. factors driving the increasing prevalence of class action proceedings in Australia;
9. what evidence is becoming available with respect to the present and potential future impact of class actions on the Australian economy;
10. the effect of unilateral legislative and regulatory changes to class action procedure and litigation funding;
11. the consequences of allowing Australian lawyers to enter into contingency fee agreements or a court to make a costs order based on the percentage of any judgment or settlement;
12. the potential impact of Australia's current class action industry on vulnerable Australian business already suffering the impacts of the COVID-19 pandemic;
13. evidence of any other developments in Australia's rapidly evolving class action industry since the Australian Law Reform Commission's inquiry into class action proceedings and third-party litigation funders; and
14. any matters related to these terms of reference.

To a considerable extent, the findings of the inquiry have been pre-empted by recent reforms. Moreover, in our earlier Research Papers we have provided both quantitative and qualitative evidence in respect of many if not most of these issues.

In considering the need for the further 'regulation' of class actions and funding arrangements, a starting point is (a) the plethora of *presently applicable* laws, procedural rules, ethical obligations and other duties applicable to one or more of the participants in commercially funded class action litigation and (b) *existing* review and regulatory mechanisms. These include the following 22 categories:

- state and territory legislative provisions governing legal costs agreements
- ethical obligations in respect of the conduct of lawyers
- internal complaints management processes adopted by law firms[49]
- oversight and complaints mechanisms of legal profession bodies (Law Societies and Bar Associations) in respect of ethical and other obligations of lawyers
- regulatory oversight of lawyers and complaints procedures through the offices of legal services commissioners or legal services boards
- procedural and other court rules governing the conduct of litigation
- statutory overriding obligations to facilitate the just, quick and economical resolution of civil proceedings
- fiduciary duties[50]
- federal and state consumer protection laws
- practice notes adopted by state and federal courts requiring, inter alia, disclosure of litigation funding agreements
- principles of contract law
- Commonwealth law applicable to the conduct of corporations engaged in trade and commerce
- continuous disclosure and other laws applicable to publicly listed entities

[49] See e.g. Christine Parker and Linda Haller, 'Inside Running: Internal Complaints Management Practice and Regulation in the Legal Profession' (2010) 36(3) *Monash University Law Review* 217.
[50] We discuss this in detail in 'Costs and funding commissions in class actions' Research Paper #5 (26 October 2020).

- Commonwealth law in respect of providers of services
- state and federal statutory protections that protect class members from adverse costs orders
- statutory class actions provisions which require notice and confer the right to opt-out of proceedings
- legislative provisions requiring court approval of settlements and the discontinuance of proceedings
- codes of conduct adopted by commercial litigation funders
- laws and judicial powers applicable to abuse of process
- residual or inherent powers of courts to control the conduct of proceedings and participants
- extensive Victorian statutory provisions applicable to litigants, lawyers and funders
- judicial powers to require security for costs and to award costs against parties and third party litigation funders.

Although (some) litigation funders are subject to the consumer provisions of the Australian *Securities and Investment Commission Act 2001* (Cth),[51] until recently there were no licencing requirements imposed on litigation funders by the *Corporations Act 2002* (Cth).

On 22 May 2020, the Commonwealth Treasurer announced that the Government would introduce regulations that would require third-party litigation funders to obtain an Australian Financial Services License (AFSL) and treat funded class actions as managed investment schemes (MIS). Thereafter the *Corporations Amendment (Litigation Funding) Regulations 2020* (Cth) were passed. The provisions became operative on 22 August 2020, but do not apply to (a) litigation funding schemes entered into prior to that date; (b) funders supporting insolvency actions or (c) litigation involving single plaintiffs.

The Regulations removed the previous exemptions for litigation schemes entered into on or after 22 August 2020. The question of whether pre-existing schemes became subject to the new regulatory obligations when group members enter into litigation funding agreements on or after 22 August 2020 was recently considered by Justice Rares. His Honour concluded that the grant of new interests whereby group members entered into litigation funding agreements on the same terms as those entered into by others before the operative date of the Regulations would not amount to the entry by the funder or group members into a 'new' litigation funding scheme.[52]

Of particular interest is the fact that the litigation funder in that case was a charitable body set up to provide legal and financial assistance to farmers. The Australian Farmers' Fighting Fund (AFFF) advanced the costs and disbursements in conducting the litigation in consideration of agreements entered into with group members entitling the AFFF to 10% of the amount recovered by such group members by way of settlement or judgment. Any income obtained by the AFFF was deployed in providing financial assistance in other cases.[53]

In light of recent regulatory reforms, in August 2020 ASIC introduced a new *ASIC Corporations (Litigation Funding Schemes) Instrument* to assist funders to manage the transition to the new regulatory regime. ASIC provides guidance on its website as to who must hold an AFSL and when a

[51] Providing protection and redress in respect of unfair contract terms and unconscionable, misleading and deceptive conduct.
[52] *Brett Cattle Company Pty Ltd v Minister for Agriculture (No 3) [2020] FCA 1628* [19]. The group members comprise persons allegedly adversely affected by the Commonwealth Government's ban on live cattle exports.
[53] Evidence was given that the AFFF had given financial backing to over 100 court cases that related to issues about decisions of governments, industrial disputes, animal activism, mining rights, and farm finance and debt issues. Ibid [8].

managed investment scheme must be registered.[54] ASIC has certain powers under the *Corporations Act 2001* (Cth) to provide exemptions from, or modify, obligations under Chapters 5C and 7, where appropriate. ASIC announced in August that it had 'formed the view that strict compliance with the member register requirements is not reasonably practical for responsible entities of registered litigation funding schemes that have one or more passive members.'[55] ASIC does not have the power to grant relief from member register obligations and, accordingly, has provided 'a "no-action" position in relation to the obligations under sections 168 and 169 of the Act for responsible entities of registered litigation funding schemes that are open litigation funding schemes'.[56] Key obligations of holders of an AFSL are set out in s 912A of the *Corporations Act 2001* (Cth) and discussed in ASIC *Regulatory Guide 104*.[57]

In the explanatory notes to the reforms, the objective is said to be 'to subject litigation funders to greater regulatory oversight by removing this exemption, in order to ensure that they meet appropriate standards beyond those imposed by the courts on a case-by-case basis.'[58] The previous system of oversight was said to create a situation in which returns for plaintiffs and class members were lower than in unfunded matters, and without regulation, there would be a large influx of funders which, to now, 'have shown insufficient transparency and accountability regarding their business models, competence and finances, alongside increasingly diverse and opaque funding arrangements'.[59] The reforms were also said to address the risk of inconsistent product disclosure statements and problems of alignment between the interests of class members and funders which may lead to settlements before trials where this is not in the interests of the class.[60] The benefits of the change were said to outweigh the risks that the higher costs imposed by the change would lead to increased consumer costs, lessened competition in the funding market and fewer meritorious actions being funded.[61]

The reform has already led to some unintended consequences. For example, the regulatory reforms prompted an urgent amendment the *Legal Profession Uniform General Rules 2015* providing a grace period of a year in which for the purposes of section 258(3) of the *Uniform Law,* a law practice is permitted to provide legal services in relation to a managed investment scheme, given that litigation funding schemes are no longer subject to an exemption.[62]

The removal of the MIS regime exemption for funded class actions will mean that *Corporations Act* anti-hawking provisions will apply and this will restrict the ability of lawyers to bookbuild. More significantly, the regulations may stall or inhibit the ability for funders to commence class actions for some time, cause additional delays and expense.

At the time of writing, there is debate in the Senate as to whether the Regulations should be amended or rescinded. The regulatory changes, coupled with the temporary amendments to continuous disclosure laws, have been described by the Shadow Attorney-General and Shadow

[54] ASIC, <https://asic.gov.au/regulatory-resources/funds-management/litigation-funding/>.
[55] ASIC, 'No-action position for responsible entities of certain registered litigation funding schemes in relation to member registers', media release, 18 August 2020 <https://asic.gov.au/media/5759483/20200818-litigation-funding-no-action-position.pdf>.
[56] Ibid.
[57] ASIC, Regulatory Guide 104: *Licensing: Meeting the general obligations.*
[58] Explanatory Statement, Corporations Amendment (Litigation Funding) Regulations 2020 (23 July 2020) 8.
[59] Ibid 9.
[60] Ibid.
[61] Ibid 10.
[62] *Legal Profession Uniform General Amendment (Litigation Funding Schemes) Rule 2020* [NSW].

Assistant Treasurer as 'a shameless move towards denying justice and fair compensation to ordinary Australians.'[63]

The new regulatory scheme, and regulation of litigation funders generally, was the focus of many of the oral and written submissions to the Parliamentary Joint Committee, which we discuss in Research Papers #1 and 2 and were also raised in discussions with the class actions practitioners whom we interviewed, summarised in Research Paper #3.

The issue of the regulation of litigation funders has also been the subject of considerable commentary in recent years, both in Australia and in other jurisdictions.[64]

According to academics Morabito and Waye,[65] four areas of concern can be identified as a possible basis for some form of regulatory intervention:

- the size of the return to the funder
- the potential for the funder to control the conduct of the proceedings[66]
- the financial capacity of the funder particularly its ability to meet any adverse costs order and
- conflicts between the funder, the class members and the lawyer(s) representing the class.

Each of these areas could be the subject of judicial supervision and control. This could arguably be achieved without the need for any other form of external regulation (as is the case in class actions in the United States and Canada), if litigation funding arrangements are within the ambit of judicial power in the class action context. In certain contexts, they clearly are (for example, where it is alleged that they give rise to an abuse of process and where court approval of settlements is sought).

In this Research Paper we do not seek to deal with all of the 'regulatory' issues in detail.[67] Brief reference will be made to some developments.

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[63] Mark Dreyfus and Stephen Jones MP, Press release: 'ASIC warns Frydenberg attack on class actions could undermine economy' (22 July 2020) 2.

[64] For an analysis involving various economic theories, including game theory and agency theory, see Duffy (n 30). For an analysis involving strategic alliance theory and qualitative data obtained from interviews with law firm and funder employees on the relationship between lawyers and funders, see Vicki Waye, 'The initiation and operations phase of the litigation funder - class action law firm relationship: an Australian perspective' (2018) 60(2) *International Journal of Law and Management* 595.

[65] Morabito and Waye (n 44) 348.

[66] In another publication, Morabito and Waye note: 'putting aside questions about control over settlement, and dealing purely with litigation tactics, arguably ASIC's concerns over funder control are misplaced. If a funder determines that interlocutory proceedings, or an appeal or limiting the causes of action should not be pursued because these strategies would not be worthwhile, surely the exercise of objective commercial judgment would benefit rather than harm class members who would otherwise not be able to effectively monitor whether the class law firm was over-servicing.' Vince Morabito and Vicki Waye, 'Financial arrangements with litigation funders and law firms in Australian class actions' in Willem van Boom (ed.) *Litigation, Costs, Funding and Behaviour: Implications for the Law* (Taylor & Francis, 2016) 155, 185.

[67] For an excellent (although now somewhat dated) review see: IMF (Australia) Ltd, *Policy and Regulatory Issues in Litigation Funding Revisited*, paper presented to Commercial Litigation Funding Conference (Windsor Ontario, July 2013) and the paper by Wayne Attrill, *The Regulation of Conflicts of Interest in Australian Litigation Funding*, paper presented at UNSW seminar, Class Actions: Securities and Investor cases (Sydney, 29 August 2013) <http://www.imf.com.au/docs/default-source/site-documents/the-regulation-of-conflicts-of-interest-in-australian-litigation-funding---wayne-attrill-19-aug-13>.

2.4 *Funded class actions: 'managed investment schemes' or 'financial products'?*

In *Brookfield Multiplex Limited v International Litigation Funding Partners Pte Ltd,*[68] the Full Federal Court held (by majority) that funded class actions are *managed investment schemes* as defined in the *Corporations Act 2001* (Cth). This meant that a wide range of registration, licensing, conduct, disclosure and other requirements could be imposed on litigation funders and their arrangements with their clients.

A further complication arose with the decisions of the NSW Supreme Court,[69] and the Court of Appeal, as to whether a litigation funding agreement constituted a 'financial product' and whether it could be validly rescinded where the funder did not hold an AFSL.[70] The Court of Appeal held, by majority, that the litigation funding agreement was not a 'credit facility', and thus not excluded from the obligations otherwise applicable to financial products. The decision was overturned by the High Court which held that the Funding Deed in that case was a credit facility.[71]

In any event, regulations were implemented[72] that exempted litigation funding schemes from the obligations applicable to managed investment schemes under the Act. In order to clarify that these arrangements are also not 'financial products' as defined in Chapter 7 of the Act, the Regulations provided exemptions from the licensing, conduct and disclosure requirements in that Chapter.

However, in view of concerns about potential conflicts between the interests of litigation funders compared to those of their clients in certain situations, for example when assessing proposed awards or settlements, the then Federal Government resolved that these concerns would be addressed by making the exemptions conditional on appropriate arrangements being put in place to manage conflicts of interest. This is discussed further below.

As noted above, the current Federal Government has now reversed this position and, by regulation, brought funded class actions within the ambit of the managed investment scheme provisions. As discussed below, this is problematic and has met with almost universal disapproval by the experienced class action practitioners, acting for both applicants and respondents, whom we interviewed.[73]

Whether or not litigation funding arrangements are properly able to be characterised as coming within the ambit of the managed investments scheme provisions, it is of interest to examine the *consequences* if they do.

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[68] *Brookfield Multiplex Ltd v International Litigation Funding Partners Pte Ltd* (2009) 180 FCR 111; (2009) 260 ALR 643; [2009] FCAFC 147.

[69] *Chameleon Mining NL v International Litigation Partners Pte Limited* [2010] NSWSC 972 (Hammerschlag J).

[70] *International Litigation Partners Pte Ltd v Chameleon Mining NL* (2011) 276 ALR 138; [2011] NSWCA 50.

[71] *International Litigation Partners Pte Ltd v Chameleon Mining NL* [2012] HCA 45.

[72] *Corporations Amendment Regulations 2012* (No 6) (Cth). In 2010, the Government approved regulations being made carving out funded class actions, as well as similar arrangements, from the definition of managed investment schemes in the *Corporations Act*. The Assistant Treasurer and Minister for Financial Services and Superannuation released for public consultation an exposure draft of related regulations to clarify that funded class actions, as well as similar arrangements, are not managed investment schemes under section 9 of the *Corporations Act 2001*.

[73] Cashman and Simpson (n 32).

As Finkelstein J observed at first instance in *Brookfield*: '[w]hat lies behind this allegation is Multiplex's desire to stop the action in its tracks'.[74]

At issue in *Brookfield* was the arrangement between the funder and the law firm.[75] Moreover, as Finkelstein J observed at first instance: 'the obligations that would come into existence if this were a managed investment scheme, assuming they could be put into effect, *would afford group members little protection of the kind envisaged*'.[76]

The majority in the Full Court referred to the risks previously identified by the Australian Law Reform Commission and the Companies and Securities Advisory Committee against which any regulatory scheme would purportedly guard:

- investment or market risk – the risk that the investment will decline in value, either because the market as a whole declines in value or because the particular investments of the scheme decline in value
- institution risk – the risk that the institution which operates the scheme will collapse
- compliance risk – the risk that the operator of a scheme will not follow the rules set out in the scheme's constitution or the laws governing the scheme, or will act fraudulently or dishonestly.

The majority considered the list 'to be a fair summary of the risks likely to be encountered by investors'.[77] However, how such risks are to be effectively reduced or minimised by subjecting litigation funding arrangements to the managed investment scheme regulatory requirements is far from clear.

The majority proceeded to describe the purpose intended by the litigation funding arrangements in question in that case:

- to facilitate the realisation of claims by group members against Multiplex, using legal services to be provided by the law firm at the expense of the funder;
- the funder also undertook to meet any order for costs made against group members or any order for security for Multiplex's costs with the intention that the funder would be reimbursed from, and derive a profit from, the proceeds of such realisation; and
- the group members would be otherwise protected from any liability for their own costs, any order that they pay Multiplex's costs, or any order that they give security for costs in the relevant proceeding.

There was some debate in that case as to whether the funder or the law firm was the 'responsible entity' for the purposes of Ch 5C. According to the majority:

> Both fulfil functions which might be thought to be part of the operation of the scheme, but neither is qualified to be a responsible entity as required by s 601FA. If either is operating the scheme, it will be in breach of s 601ED(5). There can be little doubt that between them,

[74] *Brookfield Multiplex Ltd v International Litigation Funding Partners Pte Ltd* (2009) 256 ALR 427 at [2] referred to by Jacobson J, on appeal *Brookfield Multiplex Limited v International Litigation Funding Partners Pte Ltd* [2009] FCAFC 147 at [116].
[75] Jacobson J, [37] referred to by the majority in the Full Court: *Brookfield Multiplex Limited v International Litigation Funding Partners Pte Ltd* [2009] FCAFC 147 (Sundberg and Dowsett JJ) [28].
[76] Referred to by the majority in the Full Court: *Brookfield Multiplex Limited v International Litigation Funding Partners Pte Ltd* [2009] FCAFC 147 (Sundberg and Dowsett JJ) [30] (emphasis added).
[77] Ibid [32].

> they are operating the scheme which is unregistered and lacks a responsible entity. The obvious consequence of our view that the scheme must be registered is that a qualified responsible entity must be appointed, unless the Australian Securities and Investments Commission ("ASIC") takes action to excuse the scheme from registration.[78]

Importantly, the responsible entity of a managed investment scheme must be a *public company* that holds an *AFSL* authorising it to operate a managed investment scheme.[79]

In the two class actions that were in issue in *Brookfield*, each was a class limited to persons who had entered into a litigation funding agreement.

Both Finkelstein J, at first instance, and Jacobson J (in dissent in the Full Court) were of the view that the litigation funding arrangements in that case did not come within the ambit of the managed investment scheme provisions. Thus, the four members of the Federal Court who decided this issue were divided 2:2.

It could hardly be said that the motivation of the respondent in the *Brookfield* class action litigation was to ensure compliance with the managed investment scheme requirements for the benefit of the class members. It was, as the above quoted extract from the judgment of Finkelstein J at first instance makes clear: 'to stop the litigation in its tracks' and thus frustrate the claims of the class members entirely.

Moreover, the risks against which the managed investment scheme were designed to safeguard are either of little relevance or consequence in commercially funded class action litigation, or are able to be dealt with by a variety of other existing mechanisms and safeguards.

Clearly, the risk that the litigation funder may not have the resources to continue to fund the litigation or to pay any adverse order for costs is a matter of obvious concern to the representative applicant and class members. It is certainly the case that some class actions are being or have been in the past funded by litigation funding entities with insufficient assets. However, it Is not clear why this 'problem' cannot be addressed by existing mechanisms, including judicial scrutiny of litigation funding arrangements, at the inception and during the course of litigation, and security for costs orders.

It is also not clear why the obligation to hold an AFSL will necessarily either enhance probity or ensure sufficient solvency. Moreover, as one of the ASIC Regulatory Guides makes clear:

> ASIC is not a prudential regulator. Therefore, our financial requirements do not seek to prevent AFS licensees from: (a) becoming insolvent; or (b) failing because of poor business models or cash flow problems.[80]

The existing Practice Note applicable to the conduct of class actions in the Federal Court requires the solicitors acting for funded parties to notify the court if the funder becomes insolvent or is otherwise unable or unwilling to continue to provide funding for the proceeding.[81] However, this does not necessarily always occur.

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[78] Ibid [104].
[79] S 601FB, *Corporations Act 2001* (Cth).
[80] ASIC, Regulatory Guide 166: *Licensing: Financial requirements* (September 2017) [166.5].
[81] Clause 6.3(d).

In any event, subjecting funded class actions to the MIS regulatory requirements will do little, if anything, to address the multitude of conflict of interest and other problems, identified below, that arise in class action litigation.

In addition, following a consultation process carried out by the Federal Treasury in 2015 following the implementation of the *Corporations Amendment Regulation 2012 (No 6)* it was found that:

> Opposition to regulation under any extensive and relatively onerous regime was broad based and included all defendant lawyers, most litigation funders, consumer organisations and some academics.
>
> With respect to the *Multiplex* decision itself, those stakeholders held the view that the MIS regime was not conceived with class actions in mind and therefore does not operate in a meaningful way when it is applied to class actions.[82]

According to the Treasury review, those consulted stated that there was little evidence of significant problems or consumer detriment in litigation funding arrangements. A major consumer organisation expressed concern that imposing an unsuitable regulatory regime would be likely to impede access to justice.

The obligation on operators of litigation funding schemes to hold an AFSL and to register each litigation funding scheme will no doubt give rise to a greater degree of transparency and presumably solvency. This will also require litigation funders, inter alia: to act honestly, efficiently and fairly, to maintain appropriate levels of resources and to be competent to provide financial services. This will be subject to regulatory scrutiny by the Australian Securities and Investment Commission (ASIC), a body that was singularly uninterested in this role when consulted by the Australian Law Reform Commission in the course of its recent inquiry into litigation funding and class actions.[83]

In lieu of a licensing scheme for litigation funders, the ALRC proposed a 'suite of recommendations.[84] ASIC submitted to the ALRC that the security for costs regime provides a better method of dealing with adverse costs orders in favour of respondents and insurance against financial loss than could be provided by a licensing regime:

> …the AFS licensing financial requirements are not designed to act as security to meet a particular liability, nor are they intended to protect against credit risk generally.[85]

Both the ALRC and ASIC were of the view that the court was better placed to regulate litigation funders, through court rules and procedures, oversight and security for costs.[86]

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[82] Treasury, *Post-Implementation Review Litigation Funding Corporations Amendment Regulation 2012 (No 5)*, October 2015.

[83] The ALRC conducted over 60 consultations with stakeholders and received over 75 submissions. The ALRC recommended, inter alia, that ASIC *Regulatory Guide 248* should be amended to require third party litigation funders to report annually to ASIC on their compliance with the requirement to implement adequate practices and procedures to manage conflict of interest (Recommendation 15). It was also recommended that Regulation 5C.11.01 of the *Corporations Regulations 2001* (Cth) be amended to include 'law firm financing' and 'portfolio funding' within the definition of a 'litigation funding scheme' (Recommendation 16).

[84] Australian Law Reform Commission, *Integrity, Fairness and Efficiency-An Inquiry into Class Action Proceedings and Third Party Litigation Funders*, Final Report No 134, December 2018, 18.

[85] Ibid [6.32].

[86] Ibid [6.37].

Although requiring the licensing of commercial litigation funders has attracted considerable support, subjecting litigation funding arrangements to the MIS provisions was opposed or not supported by (a) two of the four Federal Court judges who grappled with the issue in the *Multiplex* case; (b) previous Treasury officials; (c) the previous Federal Government; (d) ASIC; (e) the Australian Law Reform Commission;[87] (f) the Law Council of Australia, commercial funders and numerous others in their recent submissions to the Parliamentary Joint Committee[88] (g) most of the 30 experienced legal practitioners, who act for both applicants and respondents, whom we interviewed recently in the course of our current research and (h) the current Federal Shadow Attorney-General and Shadow Assistant Treasurer.[89]

2.5 *Other regulatory approaches*

We refer below to some of the other regulatory approaches that have been under consideration in recent years.

2.5.1 *Uniform judicial regulation*

As Morabito and Waye have noted,[90] judges acting under the auspices of the Council of Chief Justices of Australia and New Zealand considered a proposal to harmonise rules of court relating to litigation funding in order to expressly empower courts to order the payment of costs and security for costs by litigation funders. The Council did not follow through with this proposal.

However, Practice Notes in the Federal Court[91] and in other jurisdictions require disclosure to the court (and the parties) of funding agreements by which a litigation funder is to pay or contribute to any costs of the proceedings, albeit with the redaction of some matters in the version provided to the respondent.

2.5.2 *Uniform regulation by government*

The Standing Committee of Attorneys-General has given consideration to regulation of litigation funders and published a discussion paper in 2006.[92] However, the issue was subsequently remitted to the Federal Government for further consideration. A previous Federal Government's position is summarised above.

2.5.3 *Regulation through the Australian Financial Complaints Authority (AFCA)*

One regulatory option would be to require commercial litigation funders to become members of the complaints resolution scheme administered by the Australian Financial Complaints Authority (AFCA). This option was supported in submissions to the Joint Committee.[93] However, there was also significant criticism of this form of oversight. AFCA was considered to be unequipped to deal with

[87] Ibid [6.37]-[6.42].

[88] See, e.g., Slater and Gordon, Submission No. 18, June 2020, 6.3-6.7; Shine Lawyers, Submission No. 35, 11 June 2020, 44-45, 47-48; Augusta Ventures, Submission No. 31, 11 June 2020, 16; Litigation Capital Management, Submission No. 23, June 2020, 23-24; Litigation Lending Services Ltd, Submission No. 36, 11 June 2020, 2.5; Law Council of Australia, Submission No. 67, 16 June 2020, 5, 75.

[89] See Ronald Mizen, 'Labor seeks to quash litigation funding rules' (*Australian Financial Review* online, 25 August 2020) <https://www.afr.com/politics/federal/labor-seeks-to-quash-litigation-funding-rules-20200825-p55p35>.

[90] Morabito and Waye (n 44) 354.

[91] See *Class Actions Practice Note* (GPN-CA) 20 December 2019.

[92] *Litigation Funding in Australia*, May 2006.

[93] See, e.g., submission No. 40 pp. 17-18, cited in Cashman and Simpson (n 31).

collective disputes. There were also concerns that its status would be sub-judicial, it would operate on a different timeframe to the court proceedings and could interfere with those proceedings, it could cause additional delay, and give rise to confidentiality issues.[94]

2.5.4 *Licensing*

In its report on *Access to Justice,* the Productivity Commission made a number of recommendations concerning the regulation of commercial litigation funders.

It recommended that:

- the Australian Government should establish a licensing system for third party funding companies designed to ensure that they hold adequate capital relative to their financial obligations and properly inform clients of relevant obligations and systems for managing risks and conflicts of interest
- the ethical conduct of litigation funders should continue to be regulated by the courts
- the license system should require litigation funders to be members of the Financial Ombudsman Scheme
- any remaining concerns about categories of funded actions, such as securities class actions, should be addressed directly through amendments to underlying laws, rather than through any further restrictions on litigation funding.[95]

In recent reports, both the Australian Law Reform Commission and the Victorian Law Reform Commission gave detailed consideration to the regulation of litigation funders, after extensive consultation. Their recommendations are further discussed in Research Paper #1.

2.6 *Regulation in other jurisdictions*

In Canada, it appears that all of the oversight of legal and ethical issues that arise in class action litigation funding arrangements is left with the class action judges.[96]

The manner in which judicial oversight over both fee and funding arrangements operates in Canada is illustrated by a number of recent cases. For example, in *Houle v St Jude Medical Inc*[97] in 2017, the Ontario Superior Court of Justice initially refused to approve a new *hybrid* model of funding agreement on the grounds that it was unfair. The case is interesting because it involved a combination of a percentage fee agreement with the lawyers acting for the plaintiff and an agreement with a commercial litigation funder (Bentham IMF Capital Inc) that agreed to provide an indemnity against any adverse costs order and to fund part of the fees and disbursements. The lawyers acting for the plaintiff and class members initially agreed to conduct the case on a 33% contingency fee. However, following arrangements entered into with the funder, the firm agreed to lower its claim to between ten and thirteen percent, depending on the time required to resolve the litigation. The funder agreed to pay the lawyers 50 percent of their reasonable time, up to a certain amount. The funder sought 20-25 percent of the potential proceeds. Thus, depending on the time

[94] See, e.g., submissions 5, 18 and 23, summarised in ibid.
[95] Australian Government, Productivity Commission, *Access to Justice Arrangements*, Inquiry Report, September 2014, recommendation 18.2.
[96] However, other methods of regulation have been proposed, such as the introduction of statutory rate caps and mandatory disclosure requirements, see Poonam Puri, 'Profitable Justice: Aligning Third-Party Financing of Litigation with the Normative Functions of the Canadian Judicial System' (2014) 55(1*) Canadian Business Law Journal* 34, 47-53.
[97] 2017 ONSC 5129 (Perell J).

taken to resolve the case, the lawyers and the funder jointly claimed between 30 and 38 percent of the amount recovered. As we note in an earlier Research Paper,[98] in Australia, the cumulative total of lawyers' fees and funding commissions often exceed this total percentage amount.

Justice Perell objected to the funders percentage of the proceeds and conditionally approved of an arrangement that would allow the funder a guaranteed ten percent of the proceeds, with further court approval required for any amount over the ten percent. Perell J also objected to the termination rights of the funder in the funding agreement and proposed that any termination should be subject to court approval. He also objected to the overly broad and intrusive provisions of the funding agreement and the degree of control able to be exercised by the funder:

> These clauses interfere with the lawyer and client relationship and with the Houles' autonomy as the genuine plaintiff of the proposed class action. The [lawyers'] Retainer Agreement reveals that much less intrusive provisions could be substituted in a way that was fair to the Class Members and also fair in protecting Bentham's investment in the litigation. I direct that before the Litigation Funding Agreement can be approved the above clauses should be deleted and replaced. Corresponding amendments are also required to clause 10.4, which describes the consequences of termination.[99]
>
> To be candid, some of these clauses in the Litigation Funding Agreement would not necessarily be offensive in other class action cases, where it actually might be preferable transparently to allow Class Counsel alone or in partnership with a third-party funder to control the litigation. In cases where the representative plaintiff has been recruited and he or she has little or no skin in the action because his or her damages are trivial, the behaviour modification goal of class proceedings might be better achieved by accepting the conspicuous involvement of a non-party who has an entrepreneurial motivation to pursue the wrongdoer. To be candid, in some cases, it is pretentious for the court to play an ostrich with its head in the sand to ignore the reality that the entrepreneurial class counsel is more interested in pursuing the wrongdoer than is the genuine plaintiff with a cause of action. The case at bar is, however, not one such case. The Houles are genuine plaintiffs, and the Class Members have good reason to pursue compensation for their injuries.[100]

The Ontario Divisional Court dismissed an appeal from the judgment of Justice Perell.[101] In agreeing with the reasoning of Perell J, Justice Myers (with whom Sachs and Mullins JJ agreed) rejected the argument that a litigation funding is an ordinary commercial bargain, commenting that:

> unlike other commercial arrangements, there are broader interests at play with third party funding agreements that courts must weigh and consider that are fundamental to protecting the administration of justice from harm.[102]

It was further noted that:

> The common law has always had concerns with the idea of strangers becoming involved in others' litigation. The common law seeks to ensure that litigation does not become

[98] Cashman and Simpson (n 27).
[99] 2017 ONSC 5129 [93].
[100] Ibid [94].
[101] *Houle v St Jude Medical Inc* 2018 ONSC 6352 (Can LII).
[102] Ibid [42].

> susceptible to interlopers finding ways to profit at the expense of the vulnerable and thereby harming not just the parties but the institution of civil justice.[103]

The proposed funding terms were said to be quite attractive to class action plaintiffs and especially their lawyers. However, Myers J expressed the concern that such funding terms:

> come at a cost to the representative plaintiffs and to the uncertified class of potential plaintiffs. The cost includes both a monetary component and also an added element of risk to the sacrosanct independence and fidelity of the relationship between the plaintiffs and their counsel.[104]

The proposed terms of the commercial funding agreement were contrasted with the funding provisions of the *Class Proceedings Fund* in Ontario:

> The Fund will in some cases indemnify representative plaintiffs for adverse costs awards in return for 10 percent of the proceeds of the action *plus* reimbursement of any disbursements that it funds. The Fund does not pay anything to counsel for legal fees.[105]

It would appear that the case proceeded without external commercial funding. In the final settlement approval following resolution of the case in 2019, Perell J approved of: a settlement amount of $CAD 4,250,000, plus $CAD 750,000 for costs; payment to class counsel of an amount of $CAD 1,371,675 for fees and disbursements; and an honorarium of $CAD 5,000 to each of the plaintiffs. Any amount left in the fund six months after the distribution of payments to eligible class members was to be paid *cy-près*[106] to the Heart and Stroke Foundation of Canada.[107]

In 2019, the Ontario Supreme Court of Justice approved a hybrid arrangement in which counsel was to receive its billed hours on a current basis with an additional top-up of two to three percent to be determined at the stage of settlement approval or following trial.[108] The recovery by the funder, in combination with the legal fees, was capped at a maximum of 29 percent of the final settlement or award.[109]

More recently in *Drynan v Bausch Health Companies Inc*, Glustein J of the Ontario Superior Court of Justice approved a hybrid funding agreement.[110] In *Drynan*, the approved agreement capped recovery of the funder of 25% of the proceeds and the reimbursement of 80% of the counsel's legal fees (plus an additional top up for the counsel subject to court approval) at an aggregate 33% of the proceeds. This was a recovery consistent with case law on presumptive validity. Glustein J considered that it was not necessary to limit pre-approval to 10% as in *Houle,* because there was no uncertainty as to the final percentage recovery in *Drynan*.[111] The approved termination clause in *Drynan* was subject to court approval and applied to certain events, which reflected the reasonable

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[103] Ibid [3].
[104] Ibid [5].
[105] Ibid [20].
[106] On *cy-près* relief see our earlier Research Paper #6: 'Class action remedies: *cy-près:* "an imperfect solution to an impossible problem"' (19 November 2020).
[107] *Houle v St Jude Medical Inc and St Jude Medical Canada Inc Ontario*, Settlement Approval Order, 1 August 2019, Ontario Superior Court of Justice CV-17-512508-00CP (Perell J).
[108] *JB & M Walker Ltd / 1523428 Ontario Inc. v TDL Group,* 2019 ONSC 999, Ontario Superior Court of Justice CV-17-584058; CV-17-577371-00CP (EM Morgan J) [14], [25].
[109] Ibid.
[110] *Drynan v Bausch Health Companies Inc.,* 2020 ONSC 4379, Ontario Superior Court of Justice CV-19-00632601-00CP (*Drynan*).
[111] Ibid [111].

protection of the funder's interests, but did not infringe the autonomy of the counsel or plaintiff in the conduct of the litigation.[112] Similarly, the 'promise' clauses in *Drynan* did not infringe the independence and autonomy of the plaintiff or counsel, in contrast with the clauses initially proposed in *Houle*.[113]At the hearing at which judicial approval was sought for the funding and fee arrangements, the defendant contended that the termination and 'promise' clauses in the funding agreement did not permit the plaintiff or class counsel to independently manage the litigation and thus should be struck out. The Court adopted the parties' use of the term 'promise' for the contractual representations made by the plaintiff in the funding agreement. The Court found that such 'promise' clauses did not have the effect of giving the funder control of the litigation.

In several Canadian provinces, statutory class action funds may charge a prescribed percentage (10%) of the recovery in funded class action proceedings. As the decisions at first instance and on appeal in *Houle* make clear, this has also set a benchmark against which the reasonableness of commercial litigation funding arrangements may be judicially scrutinised.

Following recent amendments to the Ontario *Class Proceedings Act,*[114] the procedure for judicial approval of third-party funding agreements is set out in statute. The representative plaintiff must apply for court approval as soon as practicable after entering into the agreement.[115] Without court approval, the agreement is of no force or effect.[116] The defendant is expressly allowed to make submissions concerning the approval of the agreement pursuant to s 31.1(8).

The provision sets out matters of which the court must be satisfied before approving an agreement. The court must be satisfied that:[117]

(i) the agreement, including indemnity for costs and amounts payable to the funder under the agreement, is fair and reasonable,
(ii) the agreement will not diminish the rights of the representative plaintiff to instruct the solicitor or control the litigation or otherwise impair the solicitor-client relationship
(iii) the funder is financially able to satisfy an adverse costs award in the proceeding, to the extent of the indemnity provided under the agreement, and
(iv) any prescribed requirements and other relevant requirements are met.

The application of deemed undertaking rules and provision in the agreement for confidentiality obligations also require judicial approval.[118] The legislation provides that the court 'may give any necessary directions respecting a dispute or question that arises in relation to a third-party funding agreement.'[119]

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[112] Ibid [56].
[113] Ibid [59]-[62]. For example, in *Houle*, the plaintiff was obligated to remain a party under the proposed agreement. In *Drynan,* there was an express recognition that the plaintiff was under no such duty or obligation. Moreover, in *Houle,* the plaintiff was required to follow all reasonable legal advice of counsel. In *Drynan,* the plaintiff was merely required to 'listen carefully' to the advice of counsel.
[114] *Class Proceedings Act,* 1992, S.O. 1992, s 33.1.
[115] Ibid s 33.1(2). Notice must be provided to the defendant and the plaintiff must serve or otherwise provide to the defendant a copy of the agreement. Subject to regulations, the plaintiff is able to redact information which 'may reasonably be considered to confer a tactical advantage on the defendant' although the court can order disclosure of redacted information. An unredacted copy must be provided to the court: s 33.1(4), (5), (6), (7).
[116] Ibid s 33.1(3).
[117] Ibid s 33.1(9)(a). In making this determination, the court must consider whether the representative plaintiff had the benefit of independent legal advice: s 33.1(10).
[118] Ibid s 33.1(9)(b).
[119] Ibid s 33.1(13).

The requirement in subsection (9)(a)(ii) would not appear to countenance the litigation management clauses initially proposed in *Houle*. As Perell J noted in that case, some of the clauses 'would not necessarily be offensive in other class action cases, where it actually might be preferable transparently to allow Class Counsel alone or in partnership with a third-party funder to control the litigation.'[120] However, under the new provision, such clauses likely cannot be approved by a court in any action, even where the court might consider the transparent exercise of control by the counsel or funder to be preferable.

As noted above, in the United States it is the lawyers, rather than independent commercial financiers, that seek judicial approval for payment (on a percentage or other basis) out of any class action settlement or following judgment.

In the United Kingdom, after the event insurance has been commonly used to obtain protection against adverse costs orders in individual and 'group' litigation. However, with the limited exception of competition cases,[121] opt-out statutory class actions are not part of the legal landscape[122] and representative action rules continue to be construed narrowly. Moreover, statute precludes the recovery, by way of costs orders, of after the event insurance premiums.[123]

The Civil Justice Council in December 2010 published a consultation paper concerning a 'Self-Regulatory Code for Third Party Funding' following earlier (2007) advice to the Lord Chancellor in the report on 'Improved Access to Justice, Funding Options and Proportionate Costs'.

In his *Costs Enquiry Report* in 2010, Lord Justice Jackson favoured 'self-regulation' of third party funding.

A group of commercial litigation funders initially prepared a draft Code of Conduct. The Civil Justice Council Working Party on Third Party Funding worked on the Code which was adopted by the Council and published in November 2011. The Code was subsequently reviewed by the Association of Litigation Funders (ALF) and a revised Code was published in January 2014. It is a self-regulatory system, whereby members of the ALF are bound by the Code.[124] An Australian association of litigation funders has now been established which has also adopted a Code of Conduct.[125]

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[120] *Houle v St Jude Medical Inc and St Jude Medical Canada Inc Ontario*, Settlement Approval Order, 1 August 2019, Ontario Superior Court of Justice CV-17-512508-00CP (Perell J) [94].

[121] *Consumer Rights Act 2015* Schedule 8 para. 5(7)(c) and (11), amending the *Competition Act 1998* s 47B. See Andrew Higgins and Adrian Zuckerman, 'Class actions come to England - more access to justice and more of a compensation culture, but they are superior to the alternatives' (2016) 35(1) *Civil Justice Quarterly* 1; Jack Williams and Alan Bates, 'A priceless victory for consumers: the Court of Appeal revitalises competition law's collective actions: *Merricks v Mastercard* [2019] EWCA Civ 674' (2019) 38(3) *Civil Justice Quarterly* 327; Alma Mozetic, 'Collective redress: a case for opt-out class actions in England and Wales' (2016) 35(1) *Civil Justice Quarterly* 29.

[122] *Civil Procedure Rules 1998* r 19.11. The law in Scotland does provide for opt-out class actions more generally (see *Civil Litigation (Expenses and Group Proceedings) (Scotland) Act 2018*, ss 20(7)-(8), 21).

[123] Pursuant to s 29 of the *Access to Justice Act 1999*, premiums were recoverable. The law subsequently changed, subject to limited exceptions, as a result of s 46 of the *Legal Aid, Sentencing and Punishment of Offenders Act 2012.*

[124] See <https://associationoflitigationfunders.com/>. Members of the UK body are Augusta Ventures Ltd, Balance Legal Capital LLP, Burford Capital, Calunius Capital LLP, Harbour Litigation Funding Ltd, Redress Solutions PLC, Therium Capital Management Ltd, Vannin Capital PCC and Woodsford Litigation Funding Ltd, most of which are active in the Australian market.

[125] See <www.associationoflitigationfunders.com.au>. The members are Augusta Ventures, Balance Legal Capital, Court House Capital, Grosvenor Litigation Funding, Investor Claim Partner, Ironbark Funding Litigation Lending, Premier Litigation Funding, Southern Cross Litigation Finance and Vannin Capital.

As Mulheron has noted, there are four 'conundrums' that have arisen in relation to the regulation of third-party funding in England and Wales: [126]

- capital adequacy requirements
- the means of avoiding any 'champertous' behaviour by funders
- the grounds upon which a funder may terminate the funding agreement and
- the impact on third party funding of recently introduced percentage fees, or damage-based fee agreements.

Following the Jackson review[127] in the United Kingdom, percentage contingent fees have been introduced in the area of civil litigation generally.[128] In England and Wales, percentage fee agreements in civil litigation are now lawful.[129] In actions for damages for personal injuries legal fees may be up to 25% of the amount recovered. The cap is 35% in employment matters and 50% in other matters, including commercial matters.

The first three of the abovementioned conundrums identified by Mulheron continue to be of relevance in Australia. The fourth now looms large given the recent introduction of percentage fee arrangements in the Supreme Court of Victoria. To these may be added a fifth, somewhat more intractable conundrum: how to deal with conflicts of interest.

3. Dealing with conflicts of interest

Complex issues arise out of class action litigation, particularly in commercially funded cases, due to the actual or potential conflicts of interest which may and often do arise.[130] These are not susceptible to simple solutions and are not readily amenable to either supervision or control by external bodies such as ASIC.

In the case of commercially funded class actions, as noted above, ASIC previously proposed that each funder and each lawyer, if they wished to be exempt from otherwise applicable regulatory provisions, should: (a) be responsible for determining their own arrangements to manage interests that may conflict with their duties; and (b) be able to demonstrate that they have adequate arrangements to manage conflicts of interest, including documenting, implementing, monitoring and reviewing their arrangements. As noted by ASIC, conflicts of interest in commercially funded class actions may be actual or potential and present or future.[131]

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[126] Mulheron (n 28).

[127] Lord Justice Jackson, *Review of Civil Litigation Costs, Final Report*, December 2009. Available on line from the Stationery Office: <www.tsoshop.co.uk> and <http://www.judiciary.gov.uk/publications/review-of-civil-litigation-costs-final-report/>. The implementation and impact of the reforms are discussed in the paper by Lord Justice Jackson presented to the Civil Justice Council conference on 21 March 2014, <http://www.judiciary.gov.uk/publications/review-of-civil-litigation-costs/>.

[128] Although, somewhat perversely, the soon to be currently proposed introduction of an opt-out class action regime for competition cases is to be accompanied by a prohibition on lawyers in such cases charging a percentage of the amount recovered.

[129] s 45 of the *Legal Aid, Sentencing and Punishment of Offenders Act 2012* which amended s 58AA of the *Courts and Legal Services Act 1990.* The *Damages-Based Agreements Regulations 2013* were introduced in Parliament on 22 January 2013 and took effect from 1 April 2013. For an explanation and critique of the provisions see Rachael Mulheron, 'The Damages-based Agreements Regulations 2013: Some conundrums in the "Brave New World" of funding' (2013) 32(2) *Civil Justice Quarterly* 241.

[130] Various dimensions of this are analysed in Vicki Waye 'Conflicts of interests between claimholders, lawyers and litigation entrepreneurs' (2007) 19(1) *Bond Law Review* 225.

[131] Australian Securities and Investments Commission, *Litigation Schemes and Proof of Debt Schemes: Managing Conflicts of Interest*, Regulatory Guide 248 (2013) [248.11].

New regulations which came into force in July 2013 had the effect of encompassing commercially funded class actions within the ambit of 'financial services' for the purposes of Ch 7 in the *Corporations Act 2001* (Cth) and regulations made thereunder.[132] Under these arrangements, a person or entity providing financial services for litigation (and proof of debt schemes) was exempt from requirements that would otherwise apply under Ch 7 of the *Corporations Act 2001* (Cth) *provided* that they maintain adequate practices for managing any conflicts of interest that may arise. A regulatory guide was promulgated by ASIC.[133]

Various other proposals have been made to address conflicts of interests for lawyers acting in class action cases, including those funded by commercial funders.[134]

Concern about the problem of conflicts of interest in class actions is reflected in recently adopted practice notes. For example, the Federal Court Practice Note applicable to the conduct of class actions[135] states that the litigation funding agreement and any costs agreement should include provisions for managing conflicts of interest (including of "duty and interest" and "duty and duty") between any of the applicant(s), the class members, the applicant's legal representatives and any litigation funder.[136] Moreover, the applicant's legal representatives have a continuing obligation to recognise and manage properly any conflicts of interest throughout the proceeding.[137]

In the Canadian context, conflict of interest and other ethical problems that arise in the conduct of class actions have been examined by Kalajdzic based, in part, on interviews with seven Canadian judges with extensive class action experience.[138] As she notes, such problems arise out of the distinctive features of class action proceedings. They include the 'entrepreneurial litigation' problem, the 'adversarial void' problem and the 'absent client' problem. These problems are illustrated by some of the Australian cases referred to below.

3.1 *Problems with self-regulation*

It is clearly sensible, in principle, to require lawyers and funders to have in place 'arrangements' for the management of conflicts of interest and arrangements for documenting, implementing, monitoring and reviewing their arrangements.

However, the implementation of such arrangements is unlikely to deal adequately with the problems that frequently arise in practice or achieve the objectives previously identified by ASIC.

There are a number of problems with 'self-regulation' as a solution to conflicts of interest in commercially-funded class action litigation.

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[132] *Corporations Amendment Regulation 2012 (No 6)*, r 7.6.01AB, as amended by the *Corporations Amendment Regulation 2012 (No 6) Amendment Regulation 2012 (No 1*). See generally ASIC Regulatory Guide 248 – *Litigation schemes and proof of debt schemes: Managing conflicts of interest,* (2013).

[133] ASIC, Regulatory Guide 248.

[134] See, e.g., Michael Legg, *Litigation Funding in Australia: Identifying and Addressing Conflicts of Interest for Lawyers*, Report, US Chamber Institute for Legal Reform, February 2012. See also Simone Degeling and Michael Legg, 'Fiduciary Obligations of Lawyers in Australian Class Actions: Conflicts Between Duties' (2014) 37(3) *UNSW Law Journal* 914.

[135] Class Actions Practice Note (GPN-CA), December 2019.

[136] Ibid clause 5.9.

[137] Ibid clause 5.10.

[138] Kalajdzic (n 3). Kalajdzic proposes various amendments to the Ontario *Rules of Professional Conduct.* See also Paul Perell, 'Class Proceedings and Lawyers' Conflicts of Interest' (2009) 35 *Adv Quarterly* 202.

First, there is the difficulty of determining the 'adequacy' of the arrangements put in place by lawyers and funders to 'manage' conflicts of interest.

Secondly, there is the difficulty of ascertaining whether such arrangements are working in practice. By whom and by what means is compliance to be supervised and enforced? It is unrealistic to expect that conflicts will always be resolved by funders and lawyers in a manner that protects the interests of class members.

Thirdly, the pervasive nature of the actual and potential conflicts that arise in the context of class action litigation is such that it is difficult, if not impossible, to formalise a description of their nature or prescribe, in advance, arrangements for managing them. The variety and diversity of actual and/or potential conflicts of interest in the conduct of class action litigation are such that self-imposed and self-policed 'arrangements' to 'manage' such conflicts are unlikely to come to grips with many of the more intractable problems.

These problems are not confined to commercially-funded class actions although such litigation gives rise to additional complications. Several examples may illustrate some dimensions of the problems.

3.2 *Types of conflict*

In class action or group litigation there may be conflicts of interest, inter alia: (a) within the class, i.e. intra-class conflicts; (b) between the class members and the lawyers conducting the case; (c) between the class members and the funder; (d) between the funder and the lawyers conducting the case between the representative party and the class members; (f) between funded class members and those who have not entered into litigation funding agreements;[139] (g) between different law firms and representative parties involved in competing or overlapping class actions.

It is important to bear in mind the difference between *real* conflicts of interest and both conflicts of opinion and *spurious* conflicts. Real conflicts loom large when an increase in a benefit to one participant may reduce the benefit to another participant. Miller suggests that spurious conflicts are those where (a) some class members may be entitled to more or less than others due to differences in legal entitlements; (b) some class members have claims requiring different levels of proof; (c) some class members are claiming different types of relief.[140] However, such so-called 'spurious' conflicts may give rise to difficult ethical issues, and instances of actual conflict, particularly during the formulation of the terms of a proposed settlement, when lawyers acting for the class and/or funders seek to make allocation decisions themselves (or in concert with the lawyers for the respondent) as to the entitlements of different sections of the class in the absence of some independent evaluation mechanism. As discussed below, the requirement for court approval of any settlement in a class action does not always safeguard the interest of absentee class members.

3.2.1 *Intra-class conflicts*

There are a multitude of situations where conflicts of interest may arise including between members of the class. This may include:

[139] The issue of conflicts of interest in class actions has generated a considerable amount of scholarly analysis in the United States. See, e.g., Samuel Issacharoff, 'Class Action Conflicts, (1997) 30 *UC Davis Law Review* 805; Geoffrey Miller, *Conflicts of Interest in Class Action Litigation: An Inquiry into the Appropriate Standard*, New York University Center for Law and Business, Working Paper CLB 03-16, 581.
[140] Miller ibid.

- where some class members may have an ongoing business or other relationship with the defendant whereas others do not (e.g. in franchisee disputes or in cartel cases where some victims of the cartel are ongoing customers of those engaged in the cartel)
- in landlord/tenant or body corporate disputes where some of the parties and class members are ongoing occupants
- in disputes with financial institutions as to the legality of fees and charges,
- public interest cases where the desire for broader strategic outcomes sought by an 'ideological' representative party may transcend the narrower (self) interests of some class members
- personal injury and product liability cases where some class members may have suffered different injuries of varying degrees of severity, different levels of financial loss, or may suffer additional latent injuries in the future
- shareholder litigation where class members may have purchased shares at different points in time or where some have sold and others have retained their shares
- employment cases where class members comprise present and former employees
- actions against insurers where some class members are continuing policy holders who may pay increased premiums in the future as a consequence of any settlement or judgment in the class action
- international class actions where class members are from different jurisdictions.[141]

There are a number of cases in Australia where conflicts of interest between class members, or potential class members, have received judicial attention.[142]

3.2.2 *Conflicts between members of the class and lawyers acting for the class*

As Miller notes, the payment of fees to lawyers conducting the class action often gives rise to a 'structural' conflict with class members.[143] However, the position in Australia is somewhat more complicated than that in North America, given the prohibition on percentage fees for lawyers (recently removed in Victoria) and the costs follow the event rule.

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[141] See, e.g., the silicone breast implant class action litigation in the United States where the class comprised women from numerous countries. The United States lawyers for the class (who also represented substantial numbers of United States women under individual fee and retainer agreements) negotiated a $US 4.25 billion dollar 'global' settlement that provided that no more than 3% of the settlement fund would go to non-United States class members. This was approved by the United States District Court notwithstanding the vigorous objection of lawyers representing 'foreign' class members, including from Canada and Australia: *Heidi Lindsey v Dow Corning Corp*, Opinion (Approval of Settlement) United States District Court, Northern District of Alabama, Southern Division, 1 September 1994. Appeals from this settlement approval were stayed when Dow Corning filed for bankruptcy under Chapter 11 of the United States *Bankruptcy Code*. The ethical conduct of lawyers involved in transnational class action litigation is examined in Catherine Rogers, 'When Bad Guys are Wearing White Hats' (2013) 1 *Stanford Journal of Complex Litigation* 487.

[142] For example: *King v AG Australia Holdings* (where additional persons sought to join the class after a settlement had been announced); *Williams v FAI Home Security Pty Ltd (No 4)* (2000) 180 ALR 459 (proposed narrowing of the class to exclude some class members); *Crawford v Bank of Western Australia Ltd* [2005] FCA 949 (where some class members had different claims against some respondents); *Darwalla Milling Co Pty Ltd v F Hoffmann-La Roche (No 2)* (2006) 236 ALR 322 (disparities in the strength of claims of different class members); *Wotton v State of Queensland* (2009) 109 ALD 534 (impact of discontinuance on different class members). These cases are discussed in Damian Grave, Ken Adams and Jason Betts, *Class Actions in Australia* (Thompson Reuters, 2nd ed, 2012) 631-635. A number of other cases are discussed in this section of the chapter.

[143] Miller (n 139).

Where the defendant agrees to pay the fees and expenses incurred in conducting the case on top of any settlement amount payable to the class,[144] in theory there is no manifest or inherent structural conflict. However, in reality there is often a murky process of negotiation in relation to the quantum of compensation payable to the class and the amount of legal fees and expenses payable by the defendant on top of, or out of, that amount.

A defendant understandably seeks to minimise both amounts. The lawyers acting for the class seek to maximise both amounts. In the process of negotiation the lawyers may be seeking recovery of some or all of their fees and expenses incurred and the funder will be seeking to maximise its entitlement to a percentage of the amount payable to the class and also seeking to maximise the recovery of any costs and expenses incurred in financing the litigation. The process of negotiation will often give rise to a considerable degree of horse trading.

The process of negotiation (or mediation) is not only not transparent to the class members or the court, but may be subject to confidentiality constraints which explicitly protect the process from disclosure. Those seeking to negotiate to maximise their own pecuniary interests, such as lawyers and funders, and also to advance the interests of the class members, are in a difficult position. Such difficulties may be exacerbated when only a subset of the class have entered into litigation funding and representation agreements.

Excessive legal fees proposed to be paid to class counsel in class action settlements have attracted considerable attention in the United States. One organisation, the Center for Class Action Fairness, has successfully challenged lawyers' fees in 39 cases, reducing such fees by around $US271 million.[145] Excessive legal fees (said to amount to almost 70 per cent of the real settlement amount) attracted scathing judicial criticism by the 7th Circuit Court of Appeals in the proposed settlement of the glucosamine class action.[146] Of interest is Judge Posner's observation:

> 'It might make sense for the district judge in a large class action suit like this to appoint an independent auditor, on the authority of Fed. R. Evid. 706, to estimate the reasonableness of class counsel's billing rate.'[147]

One issue that arose in that case, and others, concerns the extent to which payments to persons or entities who are not class members, including by way of *cy-près* distributions and 'administrative costs', can be taken into account in calculating fees payable to class counsel. We discuss the issue of *cy-près* remedies in detail in Research Paper #6.

Pecuniary self-interest on the part of the lawyer(s) conducting class action litigation and funders has loomed large in several cases in Victoria. One notorious example of this issue was the commencement of a number of 'securities fraud' class actions by a company which had acquired a

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[144] Such as in the recent Volkswagen clean diesel class action litigation: *Cantor v Audi Australia Pty Limited (No 6)* [2020] FCA 658.

[145] The Center for Class Action Fairness initially merged with the Competitive Enterprise Institute but is now part of the Hamilton Lincoln Law Institute and is based in Washington DC. It has opposed numerous allegedly abusive *cy-près* settlements that benefit third parties rather than class members. See the Statement by Theodore H Frank, founder of the Center for Class Action Fairness, to the House Judiciary Committee, Sub-Committee on the Constitution and Civil Justice Examination of Litigation Abuse, March 13, 2013: https://cei.org/sites/default/files/Testimony%20-%20Cy%20Pres.pdf.

[146] *Pearson v NBTY Inc*, 772 F.3d 778, 19 November 2004. The proposed *cy-près* distribution was also overturned on appeal. This is discussed in our earlier Research Paper: *Class action remedies: cy-près; an imperfect solution to an impossible problem*, Research Paper #6, 19 November 2020.

[147] Ibid 781-2.

small number of shares in various entities.[148] To complicate the conflict problem, the company commencing the proceedings and acting as lead plaintiff was established by a class actions lawyer, Mark Elliott, who additionally acted as a solicitor in the proceedings and who was also a director and shareholder of the company. The individual loss suffered by the lead plaintiff company was relatively modest, but the fees likely to be earned by the solicitor in conducting the class actions were likely to be substantial. The defendant to one of these actions sought to prevent the proceedings from continuing on various grounds. At first instance, the trial judge declined to accept that this amounted to an abuse of process, but was satisfied that the solicitor should be restrained from acting for the company while it was the lead plaintiff in the litigation.[149] Ferguson J also took the view that the proceedings ought not to be permitted to proceed as a class action whilst the company and the solicitor acted 'in tandem' as plaintiff and solicitor. [150]

On appeal, the majority of the Victorian Court of Appeal held that the proceedings amounted to an abuse of process. It accepted that the predominant purpose of bringing the proceedings was not to vindicate the right to compensation which the company asserted, but to generate legal work and fee income for the solicitor. This was held to constitute an abuse of process and a permanent stay was ordered.[151]

The problematic model employed in these actions was the subject of adverse judicial comment in a number of the cases in which Mr Elliott was involved. For example, Sifris J in the *Myer* proceedings stated:[152]

> Acting as sole plaintiff, MCI would clearly not have commenced this proceeding. Acting as a representative plaintiff it has only commenced this proceeding so that it (or its associates) may be rewarded in the manner identified. Absent such reward it would not have provided 'the platform'. It is this hope and expectation of reward that is the predominant purpose. There is a direct relationship between the platform and the reward. No reward, no platform. This is the business model. Although this is what most funders do, the critical difference is that in the case of such funders the reward follows the legitimate vindication of rights which is the predominant purpose of the litigation. In this case, the vindication of rights is incidental to or purely a pre-condition to the reward.

The ongoing *Banksia* class action litigation[153] in Victoria has highlighted the problematic conduct of both lawyers and the funder in that case. *Banksia* is discussed in detail in various parts of our earlier Discussion Papers. At the hearing of the settlement approval application in the *Banksia* class action,

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[148] See *Melbourne City Investments Pty Ltd v Myer Holdings Limited* [2016] VSC 655 [11]-[17].
[149] *Melbourne City Investments Pty Ltd v Treasury Wine Estates limited (No 3)* [2014] VSC 340.
[150] Ibid.
[151] *Treasury Wine Estates Ltd v Melbourne City Investments Pty Ltd* [2014] VSCA 351 (Maxwell P and Nettle JA; Kyrou JA in dissent).
[152] *Melbourne City Investments Pty Ltd v Myer Holdings Limited* [2016] VSC 655 [147]. An application to the High Court seeking special leave to appeal was refused. While de-railing the claims of the plaintiff company and preventing the solicitor from generating fees from the class action, a permanent stay also can have the effect of staying the claims made on behalf of all the other class members
[153] See *Bolitho v Banksia Securities Limited (No 5)* [2019] VSC 554(Dixon J) (settlement approval application). The ongoing litigation in respect of the fees sought by the funder and the lawyers is referred to in various other Research Papers by the authors. The proceedings have involved seven firms of instructing solicitors, five senior counsel and 6 junior counsel (including the contradictor. There have been nine parties or participants: Mark Elliott (deceased); Alex Elliott; AFPL, the special purpose receivers, John Lindholm and Peter McCluskey of KPMG; the contradictor Peter Jopling QC and Jennifer Collins; barristers Norman O'Bryan QC and Michael Symons (who are no longer defending the proceedings against them); Portfolio Law and Anthony Zita; and the costs consultant Peter Trimbos (deceased).

the contradictor appointed by the court contended that there had been multiple findings by the Supreme Court that companies associated with the solicitor Mark Elliott had abused the processes of the court to generate income to Mr Elliott and/or associated companies.[154] However, the oversight exercised by the courts in cases involving this problematic model demonstrates that the court currently possesses, and is willing to exercise, adequate powers to control the conduct of funders, lawyers and others in class action proceedings.

A conflict between the interests of lawyers and class members may also arise where the law firm agrees to indemnify the representative party against any adverse costs order. This has become relatively routine in class actions in Canada[155] but does not appear to be a common practice in Australia, although it occurs. The problem does not arise in the United States because of the absence of a 'loser pays' rule. In Australia, together with the law firm's interest in obtaining payment in cases conducted on a 'no win no fee' basis, the existence of a costs indemnity rule serves as a powerful incentive to settlement and risk avoidance. Where such an indemnity is given and the representative party is unsuccessful and ordered to pay costs, the law firm is in an invidious position. There will inevitably be a strong incentive to accept any form of settlement (or discontinuance) of the claims of the remaining class members, if this will mean that the law firm is able to avoid an obligation to pay the costs of the successful defendant. Of course, in commercially funded cases the funder will usually contractually assume liability to meet any order for costs against the funded party. This serves as an incentive to avoid risk and pursue settlement but it is part of the risk accepted in consideration of obtaining a substantial commission in successful cases. However, in many cases, whether commercially funded or not, after the event (ATE) adverse costs insurance may indemnify litigants, funders and lawyers in respect of adverse costs orders.

A further potential conflict arises out of the briefing of counsel to conduct the class action litigation. At present, funders routinely choose the counsel that *they* wish to conduct the litigation, often without any regard to the views of the solicitors on the record and almost invariably without any consultation with the representative applicant conducting the case, let alone the class members. Moreover, during the conduct of the litigation, funders not infrequently change, remove or add counsel at their whim. This is usually at the ultimate expense of the class members. On occasions, additional counsel may be briefed to advise the funder, separately from the counsel retained to conduct the litigation. The funder may treat these separate legal costs as costs arising in the litigation, which it may seek to recover from the proceeds of the litigation. This adds to costs, complication and potential conflict. The representative applicant is rarely, if ever, consulted, let alone asked to provide instructions, and the class members are not informed.

Pecuniary self-interest does not appear to be an issue in cases conducted by public interest lawyers. However, Miller contends that the 'psychic' reward sought by public interest lawyers, from promoting broader public interests, may come into conflict with the individual interest of class members.[156]

3.2.3 *Conflicts between funders and class members*

[154] *Treasury Wine Estates Ltd v Melbourne City Investments Pty Ltd* (2014) 45 VR 585 [11]-[14*]; Melbourne City Investments Pty Ltd v Myer Holdings Ltd* [2016] VSC 655 [129]; *Melbourne City Investments Pty Ltd v Leighton Holdings Ltd* [2015] VSCA 235 [45]; *Melbourne City Investments Pty Ltd v Myer Holdings Ltd* (2017) 53 VR 709 [40], [48], [56], [58]-[75] referred to by Dixon J, Ibid, at [64].

[155] See the discussion in Kalajdzic (n 3). As noted in one Canadian case: 'it is almost unheard of…for there to be no agreement, or understanding, between plaintiffs and class counsel in respect of the payment of costs if the action is unsuccessful': Cullity J in *Drady v Canada (AG)* (2008) 164 ACWES (3d) 32 (Ont Sup Ct), quoted by Kalajdzic at note 68.

[156] Miller (139).

To the extent that funders are entitled to a percentage share of the amounts recovered by funded (or other) class members, their interests are aligned in seeking to maximise the amount recovered. However, in a relatively uncompetitive litigation funding market (at least until recently), class members have had little, if any, bargaining power in determining the percentage payable to the funder. Lawyers acting for the class members, who are to be paid by the funder to conduct the litigation, are understandably reticent to drive a hard bargain as to the percentage payable to the funder. Consequently, and perhaps not surprisingly, the percentage amounts payable to commercial funders in Australian class action litigation appear to be high by international standards and large commercial funders are making substantial profits.

This problem is exacerbated where the class is instigated by the funder and where potential litigants and class members enter into litigation funding arrangements with the funder, or an associated entity, prior to becoming clients of any particular law firm. However, in recent years the Australian litigation funding market has become much more competitive. This has served to drive down funding commissions, although the proliferation of competing class actions has added to transaction costs and delays.

Admittedly, funders are usually outlaying significant funds for the conduct of the litigation. They may have had to provide substantial security for costs and they run the risk of having to pay adverse costs in the event of an unfavourable outcome. Thus, from their perspective, commercial considerations will often favour acceptance of a low but reasonable offer of settlement. By way of contrast, class members who have not had to outlay anything and who are statutorily protected from adverse costs may be rationally inclined to roll the dice and litigate the case to a conclusion. In practice, they will have little, if any, real choice.

A further problem arises where only some of the class members have entered into a litigation funding agreement. In theory at least, if the same settlement amount is payable to both funded and non-funded class members, those who have not entered into a funding agreement (whereby they agree to give say 30% to the funder) will receive a higher net amount. However, to date, the adoption of the so-called funding equalisation formulae in a number of class action settlements has resulted in both funded and non-funded class members receiving the same net amount under settlements approved by the court.[157] Such allocation decisions are made by those with a manifest conflict without any involvement or consent by those class members who have not entered into a litigation funding contract.

Until recently, in numerous cases, courts have agreed to make orders for the payment of a percentage of the amount recovered to the litigation funder from both class members who have entered into contractual funding agreements and those who have not.[158]

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[157] See, e.g., *Dorajay Pty Ltd v Aristocrat Leisure Ltd* [2009] FCA 19; *P Dawson Nominees Pty Ltd v Brookfield Multiplex Limited (No 4)* [2010] FCA 1029 (Finkelstein J). As noted by Finkelstein J: 'The effect of applying the "funding equalisation factor" is to redistribute an amount equivalent to the commissions that would have been payable by the non-funded group members between all group members'[28]. Whether this is in fact the 'effect' in any given case will depend on how the settlement is structured. A funding equalisation formula was also adopted in *Inabu Pty Ltd v Leighton Holdings Limited* [2014] FCA 622; *Inabu Pty Ltd v Leighton Holdings Limited (No 2)* [2014] FCA 911 (Jacobson J). In a number of cases *all* group members have entered into litigation funding agreements with a commercial funder: see e.g., *Hudson Ventures Pty Ltd v Colliers International Consultancy and Valuation Pty Limited* [2014] FCA 982.

[158] See e.g., *Pathway Investments Pty Ltd v National Australia Bank Ltd (No 3)* [2012] VSC 625 (*Pathway*); *Farey v National Australia Bank Ltd* [2014] FCA 1242.

On one view, the ability of a funder to obtain payment from a larger pool of class members (without having to incur the transaction costs of signing up such class members) should have led to a reduction in the percentage amount payable by members of the expanded group. In this respect, it is of interest to note that in *Pathway*, the percentage amount payable to the funder in fact decreased according to the total number of shares held by individual class members. As noted by Pagone J:[159]

> The original group members had each entered into agreements with the litigation funder agreeing to pay to the litigation funder a certain percentage of any distribution by reference to the number of the bank shares which they held: 40 per cent if less than 1 million shares; 35 per cent if between 1 million shares and 10 million shares; and 30 per cent if more than 10 million shares.

In August 2012, Pagone J made orders for payments of comparable amounts by group members (who had not entered into litigation funding agreements) who joined the class and registered their claims by a specified date. No reasons appear to have been given for the making of such orders at the time, but the matter was adverted to in the subsequent judgment approving the settlement. Although the percentage amount payable to the funder decreased according to the number of shares held by individual investors, there does not appear to have been any decrease in the commission payable by class members when the class was expanded to encompass shareholders who had not entered into litigation financing agreements.

In practice, neither funded nor unfunded class members have any real leverage or negotiating power in determining the amount payable to the funder. In theory, they could object at the time at which the court is being asked to make the necessary orders. In practice, to date at least, they have not done so. As noted by Pagone J in *Pathway*:

> The amounts payable from the distribution to the original group members appear to have been agreed to between sophisticated parties with substantial means and neither they, nor the registered group members, have raised objection.[160]

However, in one case ASIC objected to the more favourable treatment of class members who had funded the litigation, all of whom were clients of the law firm conducting the case. Under the terms of a proposed settlement they were to receive substantially more than the class members who had not funded the litigation.

Although the Federal Court initially approved of the settlement,[161] this was overturned on appeal.[162] Under the proposed settlement, about 317 group members would have received approximately 42% of the quantum of their claimed and lost equity contributions and be reimbursed their legal costs. These group members were represented by the firm acting for the representative applicant in the proceeding. They had contributed varying amounts to funding the class action. The balance of the group, about 733 group members, would have recovered 17.6% of their claims to lost equity. These group members were not represented by the law firm in question. The difference in the amounts payable to the group members who had funded the litigation and the other group members was because of the proposed payment to the former of a 'funders' premium' of $28.875 million, or 35%

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[159] *Pathway Investments Pty Ltd v National Australia Bank Ltd (No 3)* [2012] VSC 625 [20].
[160] Ibid.
[161] *Richards v Macquarie Bank Limited (No 4)* [2013] FCA 438.
[162] *Australian Securities and Investment Commission v Richards* [2013] FCAFC 89 (Jacobson, Middleton and Gordon JJ).

of the total settlement. This proportion was said to have been chosen by reference to the percentage amounts usually paid to commercial litigation funders in class actions.

The Full Court was of the view that the differential treatment of the two categories of class members was not fair or reasonable for two main reasons. First, because of the inequality of opportunity afforded to the group members who had not signed retainers to share in the funder's premium on the terms offered to clients of the law firm. This inequality was said to have been heightened by the *ex post facto* offer of highly attractive terms to a small group of the law firm's clients after the settlement was announced. The second aspect of the unfairness was due to the calculation of the premium by reference to the success fees said to be normally obtained by commercial funders of class action litigation.

Although representing the class as a whole, the law firm facilitated a proposed settlement that gave preferential treatment to those class members who were its individual clients, albeit on the basis that they had funded the litigation. The court initially approved the settlement on these terms and it would have been implemented, but for the intervention and appeal by ASIC.

A revised settlement was subsequently approved by the Court, notwithstanding further objections by some class members.[163] The revised settlement did not include a substantial 'funder's premium' for those class members who had financed the litigation.

The eventual treatment of class members who had financed the litigation in *Richards* is to be contrasted with the settlement approved by the Victorian Supreme Court in the *Great Southern* class action litigation. In that case, class members who had paid substantial legal fees ($20 million) to the firm conducting the case were entitled to recover such fees out of the settlement sum. This was said to 'level the playing field' as it put class members who had funded the litigation in the same position as class members who had not provided funding but who had obtained the benefit of the settlement.[164]

In another investor class action, the Federal Court refused to approve a proposed settlement in which all class members would have the same percentage amount deducted from amounts otherwise payable to them to be paid to the commercial funder of the litigation.[165] In that case, 92 per cent of the class members had entered into a litigation funding agreement with a commercial funder and a fee and retainer agreement with the firm conducting the litigation. Gordon J refused to agree to the proposed deduction of a commission payable to the funder from the amounts proposed to be paid to the eight per cent of class members who had not entered into litigation funding agreements. She took the view that an amount equivalent to the proposed commission should be deducted but then re-allocated to the total settlement sum, which would then be allocated on a pro rata basis across all class members.

The proposed settlement in that case also involved a deduction, from the total settlement sum of $75 million, of all legal fees and expenses claimed by the solicitors acting for the class, along with other amounts,[166] before the allocation of the remaining sum to eligible class members. Although Gordon J had no difficulty, in principle, with the legal fees and expenses being deducted from the total settlement sum (notwithstanding that only 92 per cent of the class members had entered into a fee and retainer agreement with the solicitors conducting the case) she expressed various

[163] *Richards v Macquarie Bank Limited (No 5)* [2013] FCA 1442.
[164] *Clarke (as trustee of the Clarke Family Trust) v Great Southern Finance Pty Ltd* [2014] VSC 516 (Croft J) [16].
[165] *Modtech Engineering Pty Limited v GPT Management Holdings Limited* [2013] FCA 626.
[166] The amount payable to the commercial funder and also an amount in respect of the time and expenses incurred by the representative Applicant in conducting the litigation.

concerns about the quantum of the fees claimed and the inadequate information provided to the court to justify the payment of such legal fees and expenses. Various matters were referred to a Registrar for enquiry and the preparation of a report to the Court.[167] Subsequently, some of the claimed fees and expenses were reduced or not allowed.[168] In a further judgment, consideration was given to, inter alia, the claimed expenses arising out of the Registrar's review and settlement administration expenses which had been incurred or would be incurred in the future.[169] As Gordon J noted, in the initial judgment raising concerns about the fees claimed, in a class action settlement approval application:

> The solicitor is acting for itself – it seeks an order that its costs be approved by the Court and paid to it. There is no contradictor. The group members who are to share the liability for the fees and disbursements are unable to oppose the application.[170]

She went on to suggest that in view of the increase in the number of class actions it may be time for there to be a requirement that any legal costs agreement between group members and a firm of solicitors should be approved by the Court before it is binding on the group members. That suggestion appears to have substantial merit.

Although the close 'commercial' relationship between lawyers conducting class actions and commercial funders financing them may give rise to ethical issues and conflict problems, additional complications may arise where the law firm conducting the case is directly or indirectly connected with the entity financing it.[171] A number of commercial funders financing class action litigation in Australia (and elsewhere) have close connections with law firms. Usually, such funders do not finance cases conducted by firms with which they are associated. On one occasion, it was proposed that a litigation funder, Claims Funding Australia Pty Ltd,[172] would co-fund a class action conducted by the firm that had established the funder. The proposed arrangement was transparent and the firm sought the imprimatur of the Judge presiding over the case.[173] However, various Legal Services Commissioners apparently filed objections with the Court and the proposed arrangement was discontinued after the Commonwealth Attorney-General intimated that he would take steps if the proposed arrangement proceeded. That, in itself, may highlight another dimension of conflict. In the case in question, damages were being claimed *against the Commonwealth* for financial losses suffered following the outbreak of equine influenza in large parts of New South Wales and Queensland in 2007, following alleged failures on the part of the Commonwealth Department of Agriculture, Fisheries and Forestry.[174]

3.2.4 *Conflict between the representative party and class members*

[167] Along with the claim for an amount payable to the applicant for time and expenses.
[168] See *Modtech Engineering Pty Limited v GPT Management Holdings Limited (No 2)* [2013] FCA 1163. In giving approval to certain of the fees and expenses claimed, Gordon J rejected the proposition that some idea of the reasonableness of the fees claimed could be obtained by looking at what percentage they comprised compared with the total settlement in the present case and in other analogous proceedings [141].
[169] *Modtech Engineering Pty Limited v GPT Management Holdings Limited (No 3)* [2014] FCA 680.
[170] *Modtech Engineering Pty Limited v GPT Management Holdings Limited* [2013] FCA 626 [27].
[171] This issue is addressed in US Chamber Institute for Legal Reform, Australian Securities and Investments Commission, Consultation Paper 185: *Litigation schemes and proof of debt schemes: Managing conflicts of interest* (undated), 14.
[172] The funder was established by persons associated with law firm Maurice Blackburn (and funded by the firm).
[173] As noted by Attrill, the application was made by CFA as trustee of the Claims Funding Australia Trust in *Clasul Pty Limited & Ors v Commonwealth of Australia* (NSD 630/2013) in the Federal Court in Sydney: Attrill (n 67) note 68.
[174] See *Clasul Pty Ltd v Commonwealth of Australia* [2014] FCA 133.

Although a conflict between the representative party and class members may arise out of idiosyncrasies in the individual claim of the representative party in Australia, the greatest potential or actual conflict arises out of the liability of the representative party for adverse costs. In a funded case, where the funder assumes liability for adverse costs and has the financial ability to meet any such liability, the focal point of the conflict transfers from the representative party to the funder.

Apart from the issue of adverse costs, the difficulty in practice is that the representative party does not have any meaningful control over either the conduct of the litigation or the terms of settlement. Funding contracts which often provide for the advice of counsel in the event of a disagreement about the terms of a proposed settlement may provide some comfort. However, such advice is usually only sought from the counsel conducting the case. The counsel have usually already agreed to the proposed terms of settlement and may have actively participated in any negotiation or mediation process.

Moreover, having been paid by the funder, counsel may be understandably disinclined to rock the boat where the funder wants to take the money and run and where the defendant has already agreed to the proposed terms of settlement. This is not to suggest that counsel providing advice as to the reasonableness of any proposed settlement do not take their professional responsibilities seriously. However, as in any complex litigation, there will usually be a multitude of risks and legal and evidentiary factors which may be favourable or unfavourable to either side, and commercial prudence often dictates that the proposed settlement will be considered reasonable.

Furthermore, the mere fact that there may be conflicts of opinion as to whether a settlement is favourable may not preclude the parties agreeing to the terms as reasonable, as long as it does not structurally disadvantage some class members compared with others.

A further area of divergence between the interest of the representative party and some members of the class may arise in complex product liability or personal injury cases where the representative applicant may have suffered one type of injury (e.g. in the case of the Vioxx class action[175] where the representative applicant Mr Peterson suffered a heart attack) whereas other class members may have suffered different injuries (such as strokes in the Vioxx case). The gravity of the problem may be greater where (as in the Vioxx class action) the issue of the causal relationship between the consumption of Vioxx and subsequent heart attacks and strokes was litigated at the trial of Mr Peterson's case (even though he had not personally experienced a stroke). At first instance, Mr Peterson succeeded on his individual claim[176] in connection with his heart attack but the trial judge was not persuaded that Vioxx caused other injuries such as strokes, with obvious adverse cost consequences for the representative applicant. Mr Peterson had no personal interest in the judicial determination of whether Vioxx causes strokes but assumed the burden of proving this at the trial of his case and failed.

A conflict may also arise, not only between the representative applicant and other class members, but between different class members who have material differences in the merit of their respective claims. This is highlighted by the judicial rejection of the proposed settlement in the abovementioned Vioxx litigation.

After the Applicant's success at trial was overturned on appeal, the parties entered into a settlement agreement and sought court approval. Under the terms of the proposed settlement, living group

[175] *Peterson v Merck Sharp & Dohme (Aust) Pty Ltd (No 6)* [2013] FCA 447.

[176] But only on two of the causes of action pursued. In addition, he was not successful against one of the respondents against whom these two causes of action were not pleaded.

members who satisfied certain criteria would be entitled to payments of $2,000, subject to an overall cap of $497,500. In the event that the total payments to living group members would exceed this amount, each approved eligible living group member would receive one equal share of $497,500.

Deceased group members (and approved, eligible group members in the *Reeves* proceeding) would receive $1,500 subject to an overall cap of $45,000. In the event that the total of all payments to deceased group members in both proceedings exceeded this amount, each approved, eligible, living group member would receive one equal share of $45,000.

Under the terms of the proposed settlement Mr Peterson was relieved of his liability to pay the respondent's costs of the trial and appeals and was eligible to receive payment of $2,000. The applicant's solicitors had agreed to implement the proposed settlement, without any charge to the group members.

In refusing to approve the proposed settlement, Jessup J made the following observations:

> Under the proposed settlement, for group members whose circumstances are similar to those of the applicant, the payment of the monetary sum proposed would constitute a windfall. For the applicant himself, who lost his case and faces a very substantial liability in costs to the respondents, the proposed settlement would have very obvious advantages. On the other hand, for a group member who might, consistently with the reasons of the Full Court, anticipate a favourable judgment, the settlement would represent an obvious injustice. In relation to those in the latter category, the applicant has taken upon himself the burden of conducting a representative proceeding, and has had a sufficient measure of success to make it both unfair and unreasonable of him now, in effect, to walk away from the claims of those group members on the strength only of being able to settle the claims of the less deserving group members. In doing so without discrimination, the applicant has, in my view, reached a settlement which should not be approved under s 33V.[177]

Jessup J expressed concern at two other aspects of the proposed settlement. One was the proposal whereby the applicant's solicitors would advance the claims of class members seeking payment in circumstances whereby any increase in eligible claimants which exceeded the proposed cap on payments would result in a diminution of the amount paid to each qualifying claimant. Jessup J was not satisfied that the applicant's solicitors could carry out the function contemplated without inevitably being confronted by a conflict of interest.[178] Also, the absence of the advice of counsel with respect to the question of whether the settlement was in the interests of group members as a whole was said to be a matter of concern.[179]

Jessup J stated that he had no difficulty with either the threshold criteria to be applied in determining which class members were eligible for payment or the fact that the pool of potentially eligible claimants was to be limited to the 1660 class members who had registered their individual claims within the deadline previously approved by the Court.

Following the rejection of the proposed settlement, a further settlement agreement was formulated between the parties and proposed to the Court for approval. On this occasion the previous 'ceiling' of $497,500 had become the settlement sum. But Jessup J noted:[180]

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[177] *Peterson v Merck Sharp & Dohme (Aust) Pty Ltd (No 6)* [2013] FCA 447 [20].
[178] Ibid [22].
[179] Ibid [23].
[180] *Peterson v Merck Sharp & Dohme (Aust) Pty Ltd (No 7)* [2015] FCA 123 [6]-[7], [9].

> The striking feature of the settlement is the size of the overall settlement sum itself. The small number of group members whose entitlement is not to be discounted by reference to any personal circumstances – i.e. those who will receive a payout at the maximum level – will receive only $4,629.36 each. It is, in my view, inconceivable that, independently advised, a person in such a situation would regard that sum as adequate compensation for the loss and damage associated with a heart attack to the occurrence of which Vioxx made a material contribution. By definition, the claim of such a person would not be retarded by the problems of causation which beset the applicant in the *Peterson* proceeding in the Full Court.
>
> How this outcome can be reconciled with the need to do justice to those whose claims will become *res judicata* upon the making of final orders in these proceedings is a subject which has troubled me greatly in my consideration of the applications which are now before the court…
>
> At the hearing of the s 33V applications, I was informed that the total settlement sum was a "negotiated figure". Counsel for the applicants was unable to provide any other justification for the figure, or to relate it to the circumstances of those whose claims remain outstanding. But it does not take much imagination to perceive the character of the chips that were on the table during the negotiations referred to. On the judgment of the Full Court, the applicant in the *Peterson* proceeding was exposed to a costs liability which would, I infer, dwarf the settlement sum. Absent some other expedient, there is little doubt but that the applicant would have been ruined by the enforcement of the respondents' entitlements in this regard. The temptation for him to compromise the claims of the other group members as a means of extracting himself from this liability would, I infer, have been irresistible. When looked at in this way, the settlement which the court is now being asked to approve has, to say the least, a certain whiff of expediency about it.

Notwithstanding such concerns, Jessup J was persuaded that three considerations favoured the acceptance of the settlement. First, the number of members of the group with claims had become finite and was now known and finalised. There were few objections and they had been responded to by the solicitors. Second, no other applicant sought to continue the conduct of the proceedings, and Jessup J note that he did not 'see why the applicant, having run a major case in the interests of group members, but having failed on his own claim, should continue to be exposed to those obligations and risks in the interests of others who are content to remain below the parapet.'[181] Third, in the absence of approval of the settlement, it was likely that the proceedings would be dismissed. In this event, 'the group members would be denied even the nominal monetary acknowledgement that the present settlement proposal involves.'[182]

The outcome was a very unsatisfactory settlement, providing minimal benefits to the class members and maximum benefit to the representative applicant who was relieved of his obligation to pay the many millions of dollars in costs awarded to the United States and Australian corporate respondents who had succeeded in part at trial and in full on appeal.

However, it is our understanding that the solicitors acting for the applicant at trial had given him an indemnity in respect of adverse costs or had reached an understanding to this effect. Thus, if this was the case, the terms of the settlement relieved the solicitors of their obligation to indemnify the applicant in respect of the costs ordered against him. Whether such indemnity arrangement, if it

[181] Ibid [11].
[182] Ibid [12].

existed, was known to the solicitors acting for the respondents in the course of negotiating the settlement is not known to the present authors. Any such indemnity does not appear to have been communicated to the Court, to the class (or to counsel conducting the proceedings).[183]

Another area of conflict between the representative applicant and group members arises where the applicant seeks to recover, out of funds otherwise payable to group members as a whole, a personal payment in respect of the time and expense incurred in conducting the class action.[184] To date, judges have generally accepted that such a payment may be fair and reasonable,[185] even if there have, on occasions, been issues as to the quantum or reasonableness of the amount claimed.[186] Where such sum is proposed to be paid in addition to, rather than out of, the total amount payable to the class members there may be no apparent conflict.[187]

Although a conflict may arise where the proposed payment to the applicant is to come out of funds otherwise payable to class members, in practical terms such payments have been relatively modest and have not substantially diminished the pool of settlement funds. However, it seems clear that notice should be given to class members of any proposed payment so as to provide them with an opportunity to object.[188] In practice, few class members would contend that any such payment is not fair and reasonable, particularly where it is intended to compensate for the time and expense incurred by representative parties in pursuing a remedy for the benefit of the class as a whole.

3.3 *Determining the ambit of the class*

At the time of commencement of many class actions, a decision will often have to be made as to whether the class should be limited (an 'opt-in' class) or open (an 'opt-out' class).[189] Where an opt-out class is chosen there will still usually be difficult decisions to be made as to the ambit of the class.

Many class actions to date have been limited to class members who have agreed to litigation funding and representation arrangements. This is because funders have only been prepared to fund the conduct of claims on behalf of persons who have agreed to pay a percentage of the amount recovered to the funder. Unlike the position in Canada and the United States, until the decision of the Full Federal Court in *Money Max,*[190] it had been assumed that Australian courts were not empowered to order the payment of a percentage fee to a litigation funder out of any monies

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[183] It should be disclosed that the first author was junior counsel (with Julian Burnside QC and Bernard Quinn) acting for the applicant for part of the trial proceedings.

[184] This issue is considered in detail by Vince Morabito, 'An Empirical and Comparative Study of Reimbursement Payments to Australia's Class Representatives and Active Class Members' (2014) 33(2) *Civil Justice Quarterly* 175.

[185] See, e.g., *Lee v Bank of Queensland Limited* [2014] FCA 1376; *Inabu Pty Ltd v Leighton Holdings Limited (No 2)* [2014] FCA 911; *Pathway Investments Pty Ltd v National Australia Bank (No 3)* [2012] VSC 625; *Darwalla Milling Company Pty Ltd v F Hoffmann-La Roche Ltd* (No 2) [2006] FCA 1388; (2007) 236 ALR 322.

[186] See *Modtech Engineering Pty Limited v GPT Management Holdings Limited* [2013] FCA 626 referred to above.

[187] As in *Lee v Bank of Queensland Limited* [2014] FCA 1376. However, conflict could still occur if, during the course of negotiations, the gross sum payable to the class was reduced by the amount payable to the applicant for his or her time and expenses.

[188] See, e.g., *Boase v Sullivan Commercial Pty Ltd t/a McGees Property (No 3)* [2013] FCA 15 [11].

[189] Examples of open and closed class definitions are provided in Grave, Adams and Betts (n 142) Appendix 8. See also the precedents section by Michael Legg and Lachlan Armstrong on 'Representative Proceedings' in Kevin Lindgren and Catherine Branson, *Federal Civil Litigation Precedents*, Nexis Lexis, loose leaf.

[190] *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148; 245 FCR 191; 338 ALR 188.

payable (either by way of judgment or settlement) to members of the class who had not entered into litigation funding agreements. The position has, of course, now been determined by the High Court in *Brewster*[191], at least insofar as interlocutory orders are concerned. Whether such a power exists to make an order at the conclusion of the case remains a live issue.[192]

Decisions concerning the ambit of the class are usually made by the lawyers proposing to conduct the action and/or the funder of the proposed litigation. Commercial considerations loom large. Persons with small losses or claims that are more difficult to establish may be excluded from the ambit of the class.

It is difficult to conceive of how either self-imposed arrangements for the management of conflicts of interest or managed investment scheme regulatory obligations will deal with the conflict between the members of the potential litigation 'class' who have entered into litigation funding arrangements and the total class of persons who may have claims.

3.4 *Determining the amount payable to the litigation funder pursuant to contractual arrangements*

As noted above, at present the percentage fee payable to many commercial funders in class actions in Australia is relatively high. As financial disclosures by publicly listed funders and evidence before the Joint Committee make clear, they are making substantial profits from the financing of such cases.

Until relatively recently there was insufficient competition in the marketplace. As a result of the absence of real competition, some law firms wishing to conduct funded class actions were understandably reluctant to seek to negotiate a lower fee payable to the funder. The representative party and class members have little, if any, bargaining power.

There is some uncertainty as to whether the court has power to vary contractual arrangements entered into between funders and class members although the court can, no doubt, at least in theory, refuse to approve a settlement where it considers that the proposed payments to the funder are too high. In practice this is unlikely to occur.

Arrangements for the management of conflicts of interest or subjecting funded class actions to the managed investment scheme requirements would not appear to be appropriate or effective to deal with this problem.

3.5 *Determining the amount payable to the litigation funder pursuant to a common fund order*

Obvious conflicts also arise where lawyers for the applicant and funder determine the amount to be sought by way of a common fund order in circumstances where this extends to class members who have not given consent and may remain ignorant notwithstanding notice of the application. Neither self-imposed arrangements for the management of conflicts of interest or managed investment scheme requirements are capable of adequately dealing with this problem.

3.6 *Determining how funding commissions should be apportioned amongst class members pursuant to funding equalisation orders*

[191] *BMW Australia Ltd v Brewster* [2019] HCA 45; 94 ALJR 51; 374 ALR 627.
[192] *Davaria Pty Limited v 7-Eleven Stores Pty Ltd (No 7)* [2020] FCA 1487 and *Brewster v BMW Australia Ltd* [2020] NSWCA 272.

Similarly, where funders and lawyers seek to reduce the compensation payable to non-funded class members by way of funding equalisation orders, the consequential conflicts of interest cannot be managed, let alone satisfactorily be resolved, under the previous ASIC Reg 248 conflicts of interest regime or under the recently introduced managed investment scheme provisions.

3.7 *Determining the fee and retainer arrangements with lawyers*

The representative party and the class members have little if any influence over the fee and retainer arrangements into which they enter for the conduct of class action litigation. Funders have virtually unilateral control over such arrangements. Again, it is difficult to conceive of how this could be changed by the newly introduced regulatory obligations in commercially funded cases.

3.8 *Competing and overlapping class actions*

There will usually be conflicting and divergent interests where there are multiple class actions arising out of the same event(s) and where the defined classes are the same or overlapping.

As noted in the Case Management Handbook,[193] there are various sorts of competing class actions, including:

- open classes with the same definition of 'group member' who are making the same claims against the same respondent(s)
- open classes with similar but distinct claims, such as where the same group is defined but in which the claims are reliant on some shared causes of action and some not common
- where each action defines the group differently but who have similar causes of action against the same respondent;[194] and where the actions sue one common respondent for the same claims but one action also claims against other respondents
- a closed class followed by an open class
- a closed class followed by another closed class where the group membership for each is exclusive of the other but where the claims are against at least one common respondent and are similar.

Where such cases are pending in the same court the court will usually be required to determine how to best manage the multiplicity of proceedings. This may involve orders to stay one or more cases or orders for the consolidation or concurrent conduct of the cases before one judge.[195]

In some instances, the lawyers acting in the competing classes may agree to collaborate and seek jointly to conduct the litigation.

More difficult managerial problems arise where the cases are filed in different jurisdictions.

As noted in the Case Management Handbook, '[t]here is no legislative guidance and very little judicial direction for practitioners who must confront a competing class action or those who are instructed to commence one.'[196] More recent jurisprudence has provided some guidance.

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[193] Law Council of Australia (n 23) chapter 13.

[194] Note 296 in the original states: 'Such as the different classes of persons who claimed losses in *Johnson Tiles Pty Ltd v Esso Australia Ltd* [1999] FCA 56 or shareholders who acquired an interest in shares in the same company but in time periods that overlap but are not the same.'

[195] See, e.g., the discussion by Finkelstein J in *Kirby v Centro Properties Limited* [2008] FCA 1505 [10], and Merkel J in *Johnson Tiles Pty Ltd v Esso Australia Ltd* [1999] FCA 56 [64].

[196] Law Council of Australia (n 23) [13.121]. Footnote reference is made to Michael Legg, 'Entrepreneurs and Figureheads – Addressing Multiple Class Actions and Conflicts of Interest' (2009) 32(3) *UNSW Law Journal* 90,

Such problems have led to a considerable body of jurisprudence in both Canada and the United States. Also, North American courts have evolved a variety of procedural mechanisms for dealing with a multiplicity of proceedings, including 'carriage' motions[197] and mandatory transfer of different proceedings to one judge for all pre-trial procedural steps.[198]

Further judicial guidance will likely be available when the High Court hands down its decision in the *Wigmans*[199] matter that was argued on 11 November 2020.

However, in the interim, the conflicts arising out of competing class actions cannot be expected to be resolved through either self-regulation by either lawyers or litigation funders, or by the imposition of the regulatory obligations applicable to managed investment schemes.

3.9 *Determining when to settle and for how much*

At present, class members have virtually no say or influence over when a case is settled and the terms of any proposed settlement other than by formal objection at the 'fairness' hearing. This rarely occurs in practice, although it would appear to be increasing.

It is not uncommon for funders to incorporate in their funding agreement a provision whereby the advice of the most senior counsel may be sought if there is some actual or potential disagreement as to when to settle or for how much.[200] This is clearly an 'arrangement' to 'manage' actual or potential conflicts of interest.

As noted above, almost invariably the advice is to be provided by counsel engaged in the conduct of the litigation. This has the advantage that they are familiar with the legal, factual and evidentiary material and well-placed to express an informed view. The downside is that they may not be truly 'independent'.

It is difficult to facilitate an informed opinion by an 'independent' person who is not involved in the conduct of the litigation because of the time and expense required to become familiar with often complex and voluminous documentation and evidence.

Under the legislative class action schemes the docket or trial judge is required to approve of any settlement and has an important role in protecting the interests of the absentee class members. In many funded cases there are no 'absentee' class members, given that class members will have entered into contractual agreements with the funder and the law firm conducting the case.

In relation to the role of the court in approving settlements, Murphy J has observed:

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911 and Vince Morabito, 'Clashing Classes Down Under – Evaluating Australia's Competing Class Actions through Empirical and Comparative Perspectives' (2012) 27 *Connecticut Journal of International Law* 245.

[197] Carriage motions involve different law firms competing for judicial approval as class counsel to conduct a class action proceeding.

[198] For example, the multi district litigation (MDL) provisions of the United States *Federal Rules of Civil Procedure,* 28 USC, s 1407 (2006). For a critique of MDL proceedings and 'dubious' class actions, see Linda Mullenix, 'Dubious Doctrines: The Quasi Class Action' (2012) 80(2) *University of Cincinnati Law Review* 389.

[199] *Wigmans v. AMP Limited & Ors* (High Court of Australia Case No. S67/2020).

[200] In Appendix 1 to a 2013 conference paper, Attrill sets out the criteria for counsel to apply in approving of a proposed settlement, with reference to ASIC regulations: (n 67) 14.

> It should be kept in mind that the Court assumes its onerous burden at a stage of the proceeding when the interests of the applicant and the respondent have merged in the settlement and neither side seeks to critique the settlement from the perspective of class members. Both sides have become 'friends of the deal'.[201]

Moreover, where the parties are in agreement that a settlement is desirable and have reached agreement on its terms, the judge is in an invidious position. He or she will not be as familiar as the parties with the underlying strengths and weaknesses of the positions of both sides, although it is not uncommon for affidavit evidence and confidential counsels' opinions to be provided to assist the court. There is clearly a 'public interest' in the settlement rather than the litigation of disputes. Furthermore, the judge (or usually another judge) faces the unpalatable prospect of continuing with the conduct of the litigation if a proposed settlement is not approved.

It is difficult to counter the funder's view that the litigation should settle on terms acceptable to the funder. Usually the funder will have the option of withdrawing from the further funding of the case and this provides considerable leverage. Moreover, the commercial interests of the funder, in both recouping its expenditure and in receiving a profit from a funding commission, usually far exceeds the economic interests of the individual representative applicant and class members.

In cases where the law firm has not been paid in full for conducting the class action litigation, and thus has a commercial interest in receiving the unpaid balance of fees or expenses, the prospect of receiving such payment provides an irresistible pressure to settle.

It is not uncommon in commercially funded class actions for law firms to be subject to caps on fees payable by the funder or to a requirement to receive payment in full only in the event of the case succeeding. Moreover, enhanced success fees maybe recoverable in the event of a settlement.

Because of statutory protections, class members are not liable for adverse costs and thus this element of risk aversion does not arise for them.

The funder will usually have assumed liability for any adverse costs (and may be ordered to pay them in any event, absent contractual undertakings). The funder may also have provided substantial security for costs. Accordingly, commercial risk aversion and an understandable desire to take 'a bird in the hand' will often induce funders to settle for substantially less than what the claim would be worth if litigated successfully.

Class members who have entered into litigation funding contracts have little say over settlements and little, if any, real capacity to oppose or seek to vary any settlement agreed to by the funder and the lawyers conducting the case.

On one view, in an opt-in class action, where all class members are clients of the law firm conducting the litigation, the 'normal' ethical requirement of obtaining the consent of clients to the terms of any proposed settlement should be applicable. In practice, this maybe impracticable, either because of the number of class members or divergent views about the proposed terms of the settlement within the class.

Thus, in practice, litigation funding agreements seek to circumvent any requirement for individual consent by contractually obliging funded class members to be bound by any settlement deemed reasonable on the advice of counsel.

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[201] *Kelly v Willmott Forests Ltd (in liq) (No 4)* (2016) 335 ALR 439 [63], cited with approval by Incerti J in *Michela Joy Burke v Ash Sounds Pty Ltd trading as The Falls Music and Arts Festival (No 4)* [2020] VSC 581 [34].

Additional commercial leverage may be applied, overtly or more subtly, given that the funder usually will have an unconditional contractual right to withdraw from the future funding of the litigation.

The problem is exacerbated where the funder effectively exercises 'control' over the settlement negotiations. At the time of updating this Research Paper, in his judgment approving of the settlement in the *Spotless* class action (*Alison Court v Spotless Group Holdings Ltd*), Murphy J expressed concern at the funders involvement in the settlement negotiations without the presence of the applicant's lawyers. In his view, 'such a practice is to be deprecated'. He proceeded to suggest that the Federal Court *Class Actions Practice Note* should be amended to provide guidelines as to the appropriate lines of demarcation between the applicant's lawyers and the funder in settlement negotiations.

Class members who become aware of the proposed terms of settlement, by notice or otherwise, and who are dissatisfied with the proposed terms may exercise their right to opt-out of the class action and either pursue separate claims or do nothing. Passivity will result in them being bound by the settlement. By way of contrast, affirmative consent by clients is required for any settlement in ordinary litigation.

In many instances, the right to opt-out is more theoretical than real. The claim may not be worth enough to litigate it individually. The funder is unlikely to continue funding separate individual claims. The risk of adverse costs may present an insuperable deterrent. Thus, in practice, accepting or acquiescing in a 'bird in the hand' may be the only real option.

Additional conflicts may arise, including: (a) between lawyers acting for the class and the representative party; (b) between different lawyers acting for the class; (c) between different representative parties.

As Miller notes, conflicts between different lawyers or law firms acting for the class 'are likely to reflect factors having nothing to do with the litigation - prior dealings, personal animosities and jealousies, or raw struggles for wealth or power'.[202] Such problems may be exacerbated where there are competing or overlapping class actions or different class actions for different sections of those with claims against the same defendant(s).

Yet again, it is difficult to conceive of how any self-imposed arrangements for the management of conflicts of interest or the managed investment scheme provisions will deal with the abovementioned problems.

3.10 *Determining who should administer any approved settlement*.

In seeking settlement approval in class actions in Australia, a somewhat unique process has been adopted whereby the solicitors who have conducted the proceedings on behalf of the applicant and class members often seek to have themselves appointed as the administrators of the settlement. If so appointed, they become the arbiters of the individual claims of class members, many of whom may have been and continue to be clients of the firm.

Where this has been proposed as a condition of settlement approval a manifest conflict of interest problem arises. This problem has attracted judicial consternation. As Lee J has noted:

[202] Miller (n 139) 55.

> at the very least it seems to me a court must have the ability to take whatever steps are necessary or appropriate in relation to settlement distribution to minimise costs. Like the common fund condition precedent referred to in *Cao (No 2)*[203] at [34], attempts to dictate a particular form of order to the court by, in effect, providing the court with no option but to refuse the settlement unless solicitors for the applicant are appointed the claims administrator, are inconsistent with assisting the court to discharge its protective and supervisory function in relation to group members properly. Moreover, and again without being critical of the highly respected solicitors and firm involved in the present application, it is, at best, a "bad look" for a representative applicant to give instructions that a settlement (presumably struck because it is perceived to benefit group members) is *only to go ahead* and provide benefits to group members, if the applicant's solicitors obtain a contract for the provision of future services (presumably at a profit paid out of monies that would otherwise go to group members). In some cases it might amount to more than a mere "bad look", although this is not such a case.[204]

Where appointment as claims administrator is not a condition, per se, of settlement approval but a matter for determination by the judge considering the approval application, it has become relatively routine for the firm conducting the litigation to be appointed as the settlement administrator, usually without inviting tenders for this work from other persons or entities.

Although the firm conducting the litigation has obvious class action experience, expertise and familiarity with the claims, the usual commercial motivation of the firm is the substantial continuing fees that can be generated. Depending on how such fees are calculated, how the work is carried out and who is to pay the costs, further conflict problems may arise. This is particularly the case where fees are to be deducted in whole or in part from the settlement monies (and interest earned thereon) otherwise payable to the class members. The commercial interest of the firm in maximising income for this work comes into conflict with the interests of class members in minimising these transaction costs and expediting payments.

4. Judicial supervision

The interests of 'absentee' class members are protected, at least to some extent, by judicial oversight of the litigation and the requirement of judicial approval of any settlement. However, judicial oversight is a relatively inadequate surrogate for informed client involvement in the conduct of the litigation and class member consent to the terms of any settlement.

In Australia, unlike in the United States and Canada, judicial imprimatur is not required for the commencement of a class action given the absence of any certification requirement. Moreover, the certification criteria in both United States and Canadian jurisdictions incorporate an explicit requirement that the court be satisfied that both class counsel and the representative party will adequately represent the interests of the class as a whole.[205]

In the absence of any such requirement at the commencement of a class action in Australia, the onus is on class members (or possibly third parties or the court) to take proactive steps to remove a representative party or lawyers acting for the class if it can be affirmatively demonstrated that they are not acting in the interests of the class. In practice this is unlikely to happen. Moreover, the class action will not proceed in the absence of an acceptable substitute.

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[203] *Caason Investments Pty Limited v Cao (No 2)* [2018] FCA 527.
[204] *McKenzie v Cash Converters International Ltd (No 4)* [2019] FCA 166 [15], quoted with approval by Dixon J in *Bolitho v Banksia Securities Limited (No 5)* [2019] VSC 554 at [80].
[205] See e.g. Rule 24(a)(3) United States *Federal Rules of Civil Procedure.*

At the settlement stage, as noted above, there will be strong pressure on the judge to approve the proposed terms. Objectors are relatively rare in Australia (by way of contrast with the United States where lawyers acting for objectors frequently oppose proposed settlements). Information asymmetry exists as between the judge and the parties, with the latter having much more information and real insight into the factors behind the agreed terms of settlement.

Questionable conduct on the part of parties or lawyers may not be readily apparent to the court. Confidentiality constraints may exempt from disclosure certain conduct. In some instances, the court will be provided with confidential affidavit evidence supporting the settlement without such evidence being available to the other party, let alone the class members.

Unlike in the United States, where depositions may be taken of class counsel and class representatives in advance of the settlement hearing (if not blocked by order of the court), in Australia there is no ready procedural mechanism[206] for the questioning or cross examining those who have the conduct of the litigation. Although non-confidential affidavits sought to be relied upon in support of the settlement may facilitate cross examination of the deponents by class members objecting to the settlement, this appears to be very rare in Australia.

In some cases, commercial entities who were class members with substantial claims, and particularly those with an ongoing business relationship with the defendant, may have opted out of the class action and settled their individual claims on more favourable terms without any form of judicial scrutiny and without remaining class members being informed.

5. General observations

There is a compelling case for a greater degree of transparency, competition and supervision with respect to class actions generally and commercially funded class actions in particular. However, neither the previous self-administered obligations to manage conflicts of interest nor the current managed investment scheme requirements are up to the task.

Although not a panacea, we propose the establishment of a public fund and the adoption of more specific and focused *statutory* obligations, and extensive sanctions for non-compliance, applicable to litigants, lawyers and funders. The obligations proposed could be in the form of those incorporated in the *Civil Procedure Act 2010* (Vic). These proposals are discussed in our earlier Research Papers.

As is now the case in Victoria, law firms in class action litigation in other jurisdictions should also be permitted to enter into percentage fee arrangements in class action proceedings, subject to certain safeguards[207] and subject to approval by the judge overseeing the class action in question. This would encourage greater competition with commercial funders, avoid the need for a third party commercial funder in many instances, reduce overall transaction costs and reduce the potential for conflicts of interest by reducing the number of commercial parties involved in many cases. It would also circumvent the forum shopping likely to follow from the recent introduction of percentage contingency fees in Victoria.

The fact that law firms are prepared to commercially finance class action litigation is evident from the fact that a number of commercial funding entities, both within Australia and in the international

[206] However, amendments in 2012 to s 46 of the *Federal Court of Australia Act 1976* (Cth) enable a judge to make orders for a pretrial oral examination either within or beyond Australia.
[207] See e.g. the safeguards suggested in the Victorian Law Reform Commission, *Civil Justice Review*, Report 14, 2008, chapter 11 [7.83].

market, have been established and funded by private law firms. Moreover, many class actions are conducted on a 'no win no fee' basis.

Following the decision of the Full Federal Court in *Money Max*[208] and prior to the decision of the High Court in *Brewster,*[209] funders were able to obtain, with court approval, a percentage of the amount recovered for the benefit of the whole class (by either settlement or judgment) in 'opt-out' class actions without having to sign up class members. On one view, this should have led to a decrease in the percentage amount payable by the class as a whole, including those who may have previously entered into litigation funding agreements. This does not necessarily mean that the funder's proceeds were correspondingly reduced. Depending on the numbers, 20% from a large pool is likely to be larger than 30% from a smaller pool.

However, the extent to which previously available common fund orders served to increase the class of beneficiaries and reduce the per capita transaction costs is not clear. There was clearly a period, during which common fund orders were flavour of the month, when the increasing competition among funders and law firms led to a decrease in funding commissions sought. Moreover, in some instances, such as in the current *Wigmans*[210] matter, a policy decision was made by some law firms to proceed on a 'no win no fee' basis without a funder. These decisions were made in order to maximise the commercial return to the firm, reduce the transaction costs payable by the class (in the form of a funding commission) and to obtain a competitive edge over competing class actions seeking a judicial green light.

Some legal uncertainty remains as to the power of the court to make orders at the conclusion of the case whereby those who have not entered into litigation funding agreements are required to pay a percentage of any recovery to the commercial funder. In any event, courts should be clearly specifically empowered to consider the 'reasonableness' of commercial litigation funding and fee arrangements entered into with the applicant (and class members), including at the inception of the litigation (but subject to review at the time of final settlement or judgment). This may require the unpalatable task of judges evaluating commercial considerations but, assuming that it is within their judicial power to do so, it is not clear who else could be better suited to the task. Recent Canadian jurisprudence, referred to above, illustrates how courts can effectively control both fees and funding arrangements. The need for such judicial scrutiny would be reduced, or eliminated, if funding was provided through a public fund, motivated by access to justice considerations rather than commercial profit.

Although in many instances it is desirable to have greater competition between funders and law firms seeking to be involved in the conduct of class actions, the fact that this has in recent years led to a proliferation of competing and overlapping class actions is regrettable. It has led to unacceptable increases in costs and delays. Whether the current consideration of this problem by the High Court in the *Wigmans* case will lead to a satisfactory judicial solution remains to be seen.

In light of the proliferation of competing class actions, instituted by different law firms, often either with or without the backing of commercial funders, the concerns expressed by various members of the Supreme Court in Victoria in respect of a number of cases orchestrated by Melbourne lawyer Mark Elliott loom large. There has been serious judicial criticism of the 'business model' of Mr Elliott, whereby shares were acquired and class actions were commenced for a 'predominant purpose' of making money rather than vindicating the rights of class members. Concerns have also been

[208] *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148; (2016) 245 FCR 191.
[209] *BMW Australia Ltd v Brewster; Westpac Banking Corporation v Lenthall* [2019] HCA 45; (2019) 94 ALJR 51; 374 ALR 627.
[210] *Wigmans v AMP Limited & Ors* (High Court of Australia Case No. S67/2020).

expressed about the impact of this commercial strategy on the proper administration of justice, including the appearance of justice.

Where a viable class action has been commenced it is difficult to contend that the 'predominant' motivation of the lawyers and/or funders commencing competing overlapping class actions is the vindication of the rights of the class members (already encompassed and sought to be vindicated in the other class action(s)).

As Justice Sifris noted in one of the many controversial class actions connected to Mark Elliott: '[l]ike the generation of legal fees, the generation of income [through a commercial funder] is not a legitimate predominant purpose'.[211] In considering the 'business model' of Mr Elliott, Sifris J compared the position of litigation funders: 'the critical difference is that in the case of such funders the reward follows the legitimate vindication of rights which is the predominant purpose of the litigation. In this case, the vindication of rights is incidental to or purely a pre-condition to the reward'.[212] On appeal, all members of the Victorian Court of Appeal agreed that this amounted to an abuse of process. As Justice Whelan noted, whether this was illegal or immoral was irrelevant and the court could appropriately intervene if this was found to be an abuse of process, which it did. He proceeded to add:

> I do not consider that the courts should countenance the institution or maintenance of a claim that a party has actively sought out and deliberately manufactured or engineered so as to profit from the process.[213]

In the case of competing class actions, where there is already a class action on foot seeking to 'vindicate the rights' of class members, the commencement of a duplicative class action thereafter on behalf of those same class members could hardly be contended to be other than for the predominant purpose of generating legal fees and, in the case of funded cases, profits for the commercial funder(s), if the court can be persuaded to allow their matter to proceed.

The conundrum is that simply permitting the first case commenced to go forward has other obvious undesirable consequences, including encouraging a rush to the court. Moreover, the first class action may have been itself commenced expeditiously (and in some cases prematurely) for the 'predominant' purpose of advancing the commercial interests of the lawyers and/or funder and for achieving a strategic forensic advantage in the expectation or knowledge that other class actions will be brought by 'competitors'. It will often be known or anticipated that several law firms or funders are contemplating class action proceedings as they often publicly call for expressions of interest, or registration, by potential class members.

It will be of interest to see how the High Court grapples with these thorny issues.

6. A problem in search of a solution

[211] *Melbourne City Investments Pty Ltd v Myer Holdings Limited (No 2)* [2016] VSC 655 [130]. The Victorian Court of Appeal dismissed the appeal from the judgment of Sifris J: *Melbourne City Investments Pty Ltd v Myer Holdings Limited* [2017] VSCA 187 (Osborn, Whelan and Ferguson JJA). See also *Treasury Wines Estates Limited v Melbourne City Investments Pty Ltd* (2014) 45 VR 585; *Melbourne City Investments Pty Ltd v Leighton Holdings Limited* [2015] VSCA 235; *Melbourne City Investments Pty Ltd v Treasury Wines Estates Limited* [2016] FCA 787.

[212] Ibid [147].

[213] *Melbourne City Investments Pty Ltd v Myer Holdings Limited* [2017] VSCA 187 [74].

For the reasons outlined above, and discussed in our earlier Research Papers, neither self-regulation in the manner originally proposed by ASIC and subsequently adopted, nor the current managed investment scheme regulatory regime, are likely to be effective in dealing with the pervasive problem of conflicts of interest that often arise in commercially-funded class action litigation.

Although IMF (Australia) Ltd[214] (as it was then known) was of the view that litigation funding agreements should be accepted as 'financial products' and that funders should be required to hold a financial services license (as IMF originally did), IMF maintained that there should not be any statutory or other requirements as to the content of litigation funding agreements including matters such as caps on commission and other commercial considerations. In its previously expressed view: 'The existing law regulates unfair contracts and the free market will determine commission rates and other commercial aspects of funding transactions'.[215]

The more recent 'policy' position of Omni Bridgeway Limited (as it is now known) is set out and discussed in our earlier Research Paper.[216] As we stated there:

> The fact that commercial funders are risk averse is hardly surprising but their unwillingness to take on cases other than high value low risk claims, particularly in the area of investor claims, is troubling. The unavailability of commercial funding for product liability claims in respect of personal injury claims is a problem and the explanation offered to the current Parliamentary Joint Committee by the representative of litigation funder Omni Bridgeway is problematic.
>
> The fact that the largest commercial litigation funder in Australia has expressed a preference for limited 'opt-in' classes and is opposed to common fund orders and percentage fees for lawyers is perhaps not surprising from its business development perspective. It is, however, questionable from a policy and access to justice perspective.
>
> The obvious problem with *opt-in* classes is evident from the experience with the recent VW clean diesel case. The Australian 'opt-out' classes comprised all 100,000 consumers and others who acquired the diesel cars.[1] In the UK a similar number of around 95,000 affected car owners are currently seeking compensation in the High Court group action. However, the UK procedure requires claimants to *opt in* to pursue a claim. The 95,000 who have done so represent only about 8% of the total of 1.2 million affected vehicles.[217]

It is true, as IMF suggested some time ago, that the existing law provides remedies for unfair or unconscionable conduct, as well as unfair contracts. However, it is not clear that such law is readily applicable, or able to be effectively invoked, in respect of the manner in which conflicts of interest arise in conducting and concluding commercially-funded class actions in Australia.

Moreover, although it was contended that 'the free market will determine commission rates and other commercial aspects of funding transactions', those most directly affected by funding arrangements and commissions (i.e. the class members) are neither fully informed of, nor in a

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[214] On 28 November 2013, IMF (Australia) Ltd changed its name to Bentham IMF Limited. In November 2019, IMF Bentham and Omni Bridgeway merged and adopted the name Omni Bridgeway. Following a shareholder meeting in February 2020 the unified global name of Omni Bridgeway Limited was adopted. The company now has offices in Australia, the United States, Canada, Singapore, Hong Kong and London.
[215] IMF's MIS Submission, 8 March 2010 [118].
[216] Cashman and Simpson (n 27).
[217] Ibid 36.

position to negotiate the terms of the funding arrangements either at the inception or during the course of the litigation.

There are formidable asymmetries of information and power in class action cases. Class members usually have little or no relevant information and possess little if any power to influence the conduct or outcome of the litigation.

Self-regulation and self-enforcement of arrangements for dealing with conflict, implemented and supervised by those who are in a position of conflict, is not likely to be an effective solution to the problem. Oversight by ASIC and subjecting funded litigation to the managed investment scheme requirements is unlikely to protect the interests of class members adequately.

There is considerable force in the view that existing (abovementioned) regulatory arrangements in respect of lawyers and funders with a financial services license should not be further complicated by an additional layer of external regulatory oversight.

Apart from external regulatory supervision, it also needs to be borne in mind that, at present, various divergent interests are managed by parties and lawyers who are already subject to a variety of contractual and ethical duties, together with fiduciary duties, statutory obligations and duties to the court which we refer to above.

Judicial scrutiny of the conduct and settlement of class action litigation is likely to be effective if it is proactive and informed. However, in practice, for the reasons referred to above, this may not always identify, let alone resolve, some of the conflict problems. The recent legislative reforms in Ontario, referred to above, which expressly confer powers on courts in that Province to review and approve proposed funding and fee arrangements *at the inception of the class action litigation*, serve as a useful model for Australian reform.

In Victoria, litigants, lawyers, funders and insurers involved in the conduct of class actions in the Supreme Court are now subject to statutory standards of conduct incorporated in the *Civil Procedure Act 2010* (Vic) following the adoption of certain of the recommendations of the Victorian Law Reform Commission.[218] This also incorporates sanctions for non-compliance. We advocate the adoption of these provisions in other jurisdictions. Analogous but less far-reaching provisions also exist in NSW.[219] We also advocate the introduction of a statutory class action fund, as previously proposed by numerous law reform bodies.

One other possible solution is for litigation funding agreements to be subject to the regulatory scrutiny of the existing legal services regulator. This was, in fact, advocated by the previous NSW Legal Services Commissioner Steve Mark.[220] However, in the absence of agreement on national regulation of the legal profession, this has the present disadvantage of involving different bodies in some jurisdictions. Moreover, it is not clear how excessive costs and funding commissions can be 'regulated' under this regime.

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[218] Victorian Law Reform Commission, *Civil Justice Review*, Report 14, 2008. See in particular chapter 3: 'Improving the standards of conduct of participants in civil litigation'.

[219]The *Civil Procedure Act 2005* (NSW) defines persons with a relevant interest in court proceedings and imposes obligations on them. Section 56 defines a person with a relevant interest as a person who (a) provides financial assistance or other assistance to any party to the proceedings and (b) exercises any direct or indirect control, or influence, over the conduct of a party in respect of the proceedings. This may include insurers and persons who fund litigation.

[220] The Office of the Legal Services Commissioner, *The Regulation of Third Party Litigation Funding in Australia- A Discussion Paper*, March 2012.

Compliance with laws applicable to the technical formalities of costs agreements entered into between the solicitors and the (nominal) representative party provides little protection for class members who may become burdened with some of all of the costs incurred. Whilst hourly billing rates remain unregulated it is difficult to conceive of how the managed investments scheme regulatory obligations or oversight by ASIC will add value to the existing mechanisms for judicial scrutiny, review and approval of costs and funding commissions in class actions.

Proposals for reform made by the Productivity Commission, referred to above, are commendable in principle but, if implemented, may still not deal effectively with many of the problems that arise in practice.

At the time of writing one further alternative advocated in the present political debate in the Senate is a requirement that at least 70% of the recovered compensation go to class members.

In her analysis of the problem of conflict of interest in class actions in Canada, Kalajdzic identifies a number of additional problems not dealt with above.[221] Many such problems are pervasive in class action litigation in all jurisdictions, including Australia. As she suggests, the entrepreneurial and representative nature of class action litigation signifies that conflicts arising out of it, fall outside the ambit of normal professional conduct rules and their inclusion would require a 'normative shift':

> The named plaintiff is no ordinary client. The lawyer's clients include persons not named in … the proceedings. The judicial role takes on aspects of inquisitorial legal systems. And the lawyer is zealous advocate, venture capitalist, and private attorney general in equal measure.[222]

After reviewing various proposals for controlling class action 'abuse' in the North American context, including enhanced judicial scrutiny, court appointed private monitors, independently represented plaintiff committees, the use of Special Masters and third party experts to review proposed settlements, she outlines various options for specifying clearer guidelines for ethical conduct, including reform of professional conduct rules.

In Australia, various problems have been identified and several solutions suggested by other authors.[223] In May 2014, the Commonwealth Attorney-General announced that he was proposing to appoint an advisory panel to examine conflicts of interest and 'moral hazards' between lawyers conducting class actions and the companies financing them.[224] The Institute of Company Directors has also previously expressed concern at class actions against Australian companies funded by commercial litigation funders with 'little or no regulation'.[225] By way of contrast, plaintiff law firms

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[221] Kalajdzic (n 3).

[222] Ibid 24. On the analogy between venture capital and litigation funding agreements see Maya Steinitz, 'The Litigation Finance Contract' (2012) 54 *William & Mary Law Review* 455.

[223] See, e.g., Legg (n 134); Degeling and Legg (n 134); Michael Legg, 'Class action settlements in Australia - The need for greater scrutiny' (2014) 38(2) *Melbourne University Law Review* 590. The author proposes four reforms in relation to approval of settlements: court appointed experts to assess legal fees; an independent guardian to represent class members' interests; less use of suppression orders and specifying details of settlements in publicly available judgments.

[224] Chris Merritt, 'Crackdown on opportunistic class actions', *The Australian* (online), 23 May 2014 <https://www.theaustralian.com.au/business/legal-affairs/crackdown-on-opportunistic-class-actions/news-story/27ca479f28c137fc3139365c4d18a07d>.

[225] Australian Institute of Company Directors, *Submission to the Productivity Commission Inquiry into Access to Justice Arrangements*. Similar concerns were expressed in a submission by the United States Chamber of Commerce Institute for Legal Reform.

and commercial funders usually contend that, by and large, existing regulatory arrangements are adequate and that the history of litigation funding in Australia provides no evidence of widespread or significant abuse.[226]

More recent contentions, by way of written and oral submissions to the current Parliamentary Joint Committee, are summarised and discussed in our earlier Research Papers. It is clear that there have been, and continue to be, some types of manifest 'abuse'. However, many of the (identified) problems have been effectively dealt with by judicial supervision and control of Australian class action proceedings, as a number of the cases referred to above and in our earlier Research Papers illustrate.

In other jurisdictions, such as in Europe[227] and in Japan,[228] legislators have sought to circumvent some of the problems identified in this Research Paper by conferring a right to bring class action proceedings on consumer or public interest bodies rather than private litigants.

In the Australian context, the conferral of the right to bring (restricted)[229] class actions on regulatory bodies such as ASIC and the ACCC may overcome some of the problems of conflict but has been relatively ineffectual in practice. Moreover, the limitation of such remedies to those who consent to the bringing of proceedings on their behalf undermines the utility of such actions.

In view of the pervasive and complex nature of the identified problems there is no simple panacea. The position of most protagonists in this debate is aptly summarised by Lord Justice Jackson (albeit in another context):

> Every stakeholder group seems to perceive the public interest as residing in a state of affairs which coincides with its own commercial interest.[230]

Although numerous problems of conflict of interest remain in search of a solution, the implementation of the reforms advocated above and in our earlier Research Papers would, in our

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[226] See, e.g., the submission by Maurice Blackburn to the Productivity Commission Inquiry into *Access to Justice Arrangements*, 8 November 2013.

[227] See Astrid Stadler, Emmanuel Jeuland and Vincent Smith (eds), *Collective and Mass Litigation in Europe: Model Rules for Effective Dispute Resolution* (Edward Elgar, 2020).

[228] Japan's class action law confers on specified qualified consumer organisations the right to bring a class action on behalf of consumers in respect of five types of claims. The model adopts a bifurcated approach. At the first stage, common issues are determined in respect of the class as a whole. If the matter proceeds, at the second stage, those with claims in effect have to opt-in to establish their entitlement to relief. The *Act on Special Provisions of Civil Court Procedures for Collective Recovery of Property Damages of Consumers*, Act No 96 of 2013, was passed in December 2013 and came into force in 2016. See generally Michael Madderra, 'The New Class Actions in Japan' (2014) 23(3) *Pacific Rim Law & Policy Journal* 795. However, as noted by Akihiro Hironaka and Yui Takahata, the system has been rarely used since it was introduced: 'The new Japanese system for collective redress was very prudently--perhaps too prudently--legislated. The opt-in system cannot create sufficient incentive for consumer entities to file and pursue litigation against business operators. Compared with its operating costs, the kinds of damages that can be addressed through this system are too small. The scope of the claims is too narrow and standing for the first stage is too restricted': 'Is the Opt-in System Doomed to Fail? An Experience with the New Japanese Legislation on Collective Redress' (2020) 14 *Dispute Resolution International* 27, 40.

[229] Regulatory bodies are only able to bring proceedings for damages on behalf of identified class members who have consented in writing to claims being made on their behalf: see e.g., s 242(2) of the *Australian Consumer Law 2010* (Cth).

[230] Lord Justice Jackson (n 127) 1.

view, enhance the potential of class actions to better serve the interests of litigants, class members and the public interest.