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Australian Law Reform Commission

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Sydney NSW 2001

Email: class-actions@alrc.gov.au

ASA SUBMISSION: INQUIRY INTO CLASS ACTION PROCEEDINGS AND THIRD-PARTY LITIGATION FUNDERS

Dear Sir/Madam

The Australian Shareholders' Association (ASA) represents its members to promote and safeguard their interests in the Australian equity capital markets. The ASA is an independent not-for-profit organisation funded by and operating in the interests of its members, primarily individual and retail investors, self-managed superannuation fund (SMSF) trustees and investors generally seeking ASA's representation and support. ASA also represents those investors and shareholders who are not members, but follow the ASA through various means, as our relevance extends to the broader investor community.

ASA has participated in discussion with the Australian Law Reform Commission as noted on page 135 of the consultation paper, *Inquiry into Class Action Proceedings and Third-Party Litigation Funders*. The ASA has not commented on all sections of the consultation paper. We have responded to selected sections as outlined below, in respect of shareholder class actions.

3. Regulation of Litigation Funders

Australian Financial Services Licence

Should there be further regulation of litigation funders other than that they have sufficient capital and knowledge? For example, should a litigation funder should be required to hold an AFSL?

Notwithstanding IMF Bentham's holding of an AFSL, we query why litigation funders should hold an AFSL, given they are running a court case, not providing financial advice. There is a view that some check in the system is required to ensure that litigation is not funded by a party with a significant conflict of interest, for example, a competitor entity, and again we query whether holding an AFSL would prevent such a conflict arising. There may be some merit in a regulatory

guide such as ASIC's RG146 (Licensing: Training of financial product advisers) or other consumer protections to protect participants from inflammatory language and being misled/misinformed in a class action. We note the primary responsibility of the legal practitioners to ensure that the litigation is run competently and in a manner befitting the practitioner's role as an officer of the court.

The role of security for costs

Should security be requested?

We recognise that litigation funders are almost invariably required to lodge substantial sums by way of security, but they are commercial entities and this is part of their business model. If security payments for individuals are high, it destroys the very concept of a class action, which is to allow those who may not have significant personal wealth to seek legal redress. A security payment from the law firm or funder would weed out frivolous claims. Individuals should not have to contribute. It is obvious that no class action will proceed unless the lawyers/funders can be satisfied that there is a strong likelihood of success and a return on their investment.

5. Commission Rates and Legal Fees

Lift the ban on contingency fee arrangements, with limitations

As outlined in the ASA submission to the Victorian Law Reform Commission consultation paper, *Access to Justice—Litigation Funding and Group Proceedings,* dated 6 October 2017, the ASA's in-principle support for contingency billing is subject to the maintenance of Australia's loser pays costs rule and constraints on percentage recoveries.

Our support for the removal of the prohibition on contingency billing is subject to:

- constraints on percentage recoveries — the contingency fee should be capped at 25 per cent (combined solicitor and litigation funding fee)
- the maintenance of Australia's loser pays costs rule, and
- it being used on its own with no additional fees (for example, lawyers should not be able to charge a percentage of damages in addition to their hourly rate).

We are therefore in agreement with the Productivity Commission's recommendation in its report Access to Justice Arrangements that the prohibition on contingency, or damages-based billing, be removed, subject to certain consumer protections such as comprehensive disclosure requirements and percentages being capped. Also, as recommended by the Productivity Commission, contingency or damages-based fees should be used on their own with no additional fees (for example, lawyers should not be able to charge a percentage of damages in addition to their hourly rate). The ASA is of the view that the removal of the ban on contingency billing would:

- allow smaller scale class actions of merit to be tested in the legal system, which would increase access to justice

- improve the accountability of directors, executives and professional advisers to shareholders
- result in greater returns to group members, as the overall costs to the consumer are likely to be substantially less than the combined costs of a third-party funder and lawyer
- encourage more plaintiffs to mount a more financially marginal but otherwise worthy case.

The ASA's in-principle support for contingency billing is subject to the maintenance of Australia's loser pays costs rule and constraints on percentage recoveries. This is how contingency billing was introduced in the UK and Canada, providing the example of how such constraints prevent an explosion of 'frivolous' claims. Notwithstanding this, ASA is strongly of the view that plaintiffs should not pay costs. Class actions provide an affordable service to ensure that access to justice is not contingent on personal wealth. Should plaintiffs know that they may have to pay large sums, the concept of providing access to justice for shareholders who would not otherwise be able to access legal assistance to secure redress for corporate misconduct is undermined. ASA believes that plaintiffs and law firms need to agree on costs if the class action is lost before they agree to the class action. This could take the form of the losing legal firm being responsible for costs, with their client responsible to them for reimbursement thereof to the extent agreed.

Constraints on percentage recoveries provides certainty to group members about what will be distributed to them and aligns the interests of the lawyers and clients. For example, if the contingency fee was set at 25 per cent, group members would have certainty that 75 per cent of proceeds would be distributed to them. We note, for example, that the law firm Maurice Blackburn has established that "In a sample of 10 funded cases run by Maurice Blackburn, close to an additional $90 million would have been returned to group members if those cases were run on a flat, all-inclusive 25 per cent contingency fee basis".[1]

The Law Institute of Victoria, in its paper Percentage-Based Contingency Fees: Position Paper[2], states that it views contingency billing as improving access to justice, noting that "Removing the prohibition on law practices charging contingency fees would facilitate access to justice by providing another method by which legal costs can be agreed upon, thus enabling some claims to be brought which would otherwise not be brought due to lack of funding".

The Law Institute of Victoria has long advocated for the introduction of contingency fees, noting that it will increase access to justice by people who do not qualify for legal aid and cannot afford to pay legal fees upfront. Its reasons for supporting the lifting of the ban on contingency billing are that it enables meritorious matters that are not able to be funded by the client alone to be funded; aligns costs to outcomes rather than hours spent working on the matter; clarifies legal costs for the client; and provides an incentive to law firms to resolve matters efficiently. Moreover, the Law Institute notes that contingency billing is already being used by litigation funders.

[1] Maurice Blackburn, Response to Productivity Commission Access to Justice Arrangements Issues Paper
[2] Law Institute of Victoria, Percentage-Based Contingency Fees: Position Paper, Released 17 February 2016

Concern has been expressed that contingency fees create conflicts of interest between the lawyer's fiduciary duty to the client and their financial interest in the outcome of a case. However, the ASA agrees with the Productivity Commission that it "is unconvinced that any perverse incentives inherent in damages-based billing are more pronounced than those embodied in conditional billing." Lawyers already have a financial interest in the outcome of the case under conditional billing. Conditional billing is charged on an hourly rate, which can provide an incentive to over-service. Contingency billing removes this incentive and creates an incentive to achieve the largest pay-out in the shortest possible time. Hourly rates become irrelevant as a contingency fee (or damages-based fee) sees the lawyer receive an agreed percentage of the amount recovered by the client.

Conclusion

The ASA is of the view that removing the existing prohibition on law firms charging contingency fees (except in areas where contingency fees would be inappropriate, including personal injury, criminal and family law matters) would assist to mitigate the issues presented by the practice of litigation funding.

Our support for the removal of the prohibition on contingency billing is subject to:

- constraints on percentage recoveries — the contingency fee should be capped at 25 per cent
- the maintenance of Australia's loser pays costs rule, and
- it being used on its own with no additional fees (for example, lawyers should not be able to charge a percentage of damages in addition to their hourly rate).

Please do not hesitate to contact us should you wish to discuss our submission.

(Attachment: ASA policy position Class Actions)

Yours sincerely

Judith Fox
Chief Executive Officer