# SEEING PAST THE US BOGEY – LESSONS FROM AUSTRALIA ON THE FUNDING OF CLASS ACTIONS

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*The bogey of US style actions has dominated public thinking and policy formulation regarding the design of collective redress mechanisms in the United Kingdom. As a result, the UK Government has chosen a sector by sector approach rather than a generic class action regime. The spectre of US style litigation has also been influential in the drafting of the costs provisions for the country's first sector-specific opt out class action regime governing class actions filed before the Competition Appeal Tribunal. The purpose of this article is to make a contribution to the debate as to the most satisfactory means of addressing the costs and funding of class actions (whether brought pursuant to a generic class action regime or regimes in specific sectors or industries only) by providing an evaluation of this dimension of Australia's federal class action regime which has been in operation for over 24 years.*

Key words: Class action reform, costs and funding, Australia, commercial litigation funders, conditional costs agreements, competition class actions.

## I. INTRODUCTION

It is hardly surprising that when surveyed about collective redress United Kingdom consumers would eschew US style class actions when they are told that under the US class action model (1) lawyers receive half of the money awarded; (2) that lawsuits in the US cost small businesses billions of dollars a year; and (3) that the initiation of frivolous lawsuits means that seriously injured people wait longer for compensation.[1] Equally unsurprising is the fact that consumers are generally not told that the traditional English representative action often fails to provide effective collective redress,[2] and that as a result, miscreants may avoid responsibility for the harm they inflict. Nor are they told about other opt out collective redress regimes that operate quite differently from the US class action model, that result in substantial compensation awards to consumers, and that successfully deter wrongdoing. Rather, the bogey of US style actions has dominated public thinking[3] and therefore policy formulation.[4]

As a result of the enactment of the *Consumer Rights Act 2015* an opt out class action regime was introduced for the first time in the United Kingdom. But the regime only permits class actions with respect to competition cases brought before the Competition Appeal Tribunal ("CAT regime"). Accordingly, a crucial question which will inevitably attract the attention of scholars, policy makers and anyone with an interest in access to justice is whether it is desirable to enact legislation that will

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[1] Institute for Legal Reform, *Comparing Litigation Costs: Canada, Europe, Japan and the United States*, (Washington DC: US Chamber Institute for Legal Reform, 2013) available at www.instituteforlegalreform.com/uploads/sites/1/US_and_UK_Infographic.pdf

[2] See, for instance, *Emerald Supplies & Anor v British Airways Plc* [2011] Ch 345 - representative part of a claim based on breach of the prohibition against cartels was struck out because it could not be shown that members of the class shared the same interest in the claim.

[3] See, for instance, the following from the Financial Times: J Croft & L Fortado, "US-style class action lawsuits poised to come into force in UK", *Financial Times*, 28 September 2015.

[4] See, for instance, United Kingdom, Department for Business Innovation and Skills, *Private Actions in Competition Law: A Consultation on Options for Reform – Government Response* (2013), para 5.33 highlighting government concerns regarding the need to avoid a plethora of unmeritorious class actions and the excesses of the US class action regime.

permit and regulate class actions with respect to all types of substantive claims and, if so, what features this regime should possess. Even if a generic opt out regime continues to be rejected and the legislature only considers collective redress mechanisms on a sector by sector basis, the balance struck between access to justice, the deterrence of opportunism, and the minimisation of transaction costs embedded in the design of each of the regimes will remain crucial to their success.

With respect to regime design, the Ontario Law Reform Commission explained, in 1982, that:

> The question of costs is the single most important issue that this Commission has considered in designing an expanded class action procedure … the matter of costs will not merely affect the efficacy of class actions, but in fact will determine whether this procedure will be utilised at all.[5]

The significance of this dimension of class action regimes is already apparent from the extensive attention that the costs provisions incorporated within the CAT regime have received to date.[6] What is also clear is that "looking outwards to established class action jurisdictions for guidance [is something that] … English law- and policy-makers must surely do".[7]

We do not intend to explore the connection between the problems associated with US class actions, contingency fees, and the lack of a substantive deterrent against meritless claims in the form of a cost shifting regime. These issues have been articulated in depth elsewhere.[8] The aim of the article is to ensure that future debates in the United Kingdom with respect to the cost dimension of class action regimes will have also have the benefit of an accurate understanding of the experience in Australia, a country whose judiciary, legal system and legal profession are very similar to their United Kingdom counterparts. Although there are some differences between the United Kingdom's CAT regime and Australia which we will outline, Australian collective redress is also subject to a cost shifting regime and, consistent with the CAT regime, contingency fees or damages based fees are not permitted.[9]

The country's first and most important class action regime was introduced in the Federal Court of Australia in March 1992 through the enactment of Part IVA of the *Federal Court of Australia 1976* (Cth) ("Part IVA").[10] This is a sufficiently long period to allow a meaningful assessment to be made as to the effectiveness of the measures, regimes and rules that have sought to address funding and costs issues in Part IVA proceedings.

Part II of the article seeks to anticipate the cost-related barriers that will be faced by aspiring class representatives in the United Kingdom by exploring the difficulties that Australian lead plaintiffs have faced over the last 24 years in federal class actions. In Parts III, IV and V all the strategies that have been implemented to fund Part IVA proceedings will be explored together with a review of the significant impact that these funding models have had on the types of substantive claims that have been pursued and the devices that have been used to determine who should be entitled to share the fruits of successful class actions.

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[5] Ontario Law Reform Commission, *Report on Class Actions* (Report no 48; 1982), 647.

[6] See, for instance, A Higgins & A 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 *Civil Justice Quarterly* 1; R Mulheron, "Third party funding and class actions reform" (2015) 131 *Law Quarterly Review* 291; and A Higgins, "Driving with the handbrake on: competition class actions under the *Consumer Rights Act 2015*" (2016) 79 *Modern Law Review* 442.

[7] R Mulheron, "Opting In, Opting Out, and Closing the Class: Some Dilemmas for England's Class Action Lawmakers" (2010) 50 *Canadian Business Law Journal* 376, 379.

[8] Eg John C Coffee Jr, *Entrepreneurial Litigation: Its Rise, Fall and Future* (Cambridge, MA: Harvard University Press, 2015).

[9] *Competition Act 1998*, s 47C(8).

[10] The only three other Australian class action regimes, in Victoria, New South Wales and Queensland, are modelled on the Part IVA regime. See, respectively, *Supreme Court Act 1986* (Vic), Part 4A; *Civil Procedure Act 2005* (NSW), Part 10; and *Civil Procedure Act 2011* (Qld), Part 13A.

In undertaking our evaluation, reliance will be placed on the data that has been collected by the first-named author as part of a comprehensive empirical study of, among others, Australia's federal class action regime. This empirical study has entailed the review of court files, judgments, media reports, relevant web sites and documents and information provided by plaintiff lawyers and litigation funders with respect to every Part IVA proceeding filed in the first 24 years of operation of the federal class action regime ("review period").[11]

A number of important findings, of direct relevance to law makers in the United Kingdom, will emerge from our analysis. The first finding is that the fear, on the part of the government responsible for the creation of the Part IVA regime, that this regime would generate in Australia the same problems that are perceived to have been caused by class actions in the US led to the almost complete absence in Part IVA of important measures. These are measures designed to assist potential class representatives in procuring the significant resources required to secure collective redress.

It will also be shown that this significant omission would have resulted, in the absence of two crucial developments, in access to the federal class action regime being dependent on the availability of various *ad hoc* funding strategies, many of which have proved to be inadequate. The two developments in question are the subsequent enactment by Australia's state legislatures of statutes that permitted and regulated the use by solicitors of conditional costs agreements and the emergence, over the last 15 years or so, of commercial litigation funders as the leading players in Australia's class action landscape. Two other important findings will emerge from this article. The first is that the two funding strategies mentioned above have only partially filled the void left by the drafters of Part IVA. The second is that the business models adopted by many commercial litigation funders and plaintiff solicitors have resulted in significant proportions of victims of illegal conduct not being able to receive the compensation flowing from the successful outcome of class action litigation and several categories of substantive claims being largely ignored in Part IVA litigation.

## II. OVERCOMING THE FINANCIAL BARRIERS

### A. Appointment and standing of class representatives in Part IVA proceedings

Before exploring the financial dimensions of Australia's federal class action regime, it is useful to briefly explain the rules and provisions governing the appointment and standing of class representatives in Part IVA litigation. Unlike most class action regimes around the world, Part IVA does not employ a certification device. Thus, aspiring class representatives are not required to seek approval from the Court before being able to file or proceed with a class action proceeding. It is left to the respondents (as defendants are called in the Federal Court of Australia) to seek judicial intervention whenever they feel that the proceeding in question has failed to satisfy the three prerequisites for filing a Part IVA proceeding (set out below).[12]

In addition, trial judges have, at their disposal, extensive powers to order that proceedings do not continue as Part IVA proceedings despite a finding that these proceedings adhered to each of the three commencement prerequisites.[13] These powers may be exercised by trial judges on their own initiative or following an application by respondents. One of the practical effects of the lack of a certification device is that the ability to commence and conduct a Part IVA proceeding, on behalf of other claimants, is not dependent on the relevant lead plaintiffs persuading the court that they will adequately represent the interests of the represented class. Part IVA does, however, empower trial

[11] During this period a total of 370 federal class actions were filed: V Morabito, *Facts and Figures on Twenty-Four Years of Class Actions in Australia* (An Empirical Study of Australia's Class Action Regimes; Fourth Report; August 2016), 6 (available at http://ssrn.com/abstract=2815777).

[12] See, generally, V Morabito & J Caruana, "Can Class Action Regimes Operate Satisfactorily without a Certification Device? Empirical Insights from the Federal Court of Australia" (2013) 61 *American Journal of Comparative Law* 579.

[13] Part IVA, ss 33L, 33M & 33N.

judges to substitute a class member as class representative where it finds that the existing class representative is not able adequately to represent the interests of the class members. But this power may only be exercised following an application by a class member.[14]

Part IVA's s 33C(1) contains the three commencement prerequisites adverted to above. It provides that where (a) seven or more persons have claims against the same person; (b) the claims in question are in respect of, or arise out of, the same, similar or related circumstances; and (c) the claims of the persons give rise to a substantial common issue of law or fact, a Part IVA proceeding may be filed "by one or more of those persons as representing some or all of them". Section 33D explicitly confirms what is implicit in s 33C(1), namely, that the only persons that have standing to bring Part proceedings are the persons referred to in s 33C(1)(a): members of groups of at least seven persons that each have claims against the same person. This would appear to require that lead plaintiffs in Part IVA proceedings have been harmed by the conduct that is sought to be challenged in the class action.

But in 1999 the Full Federal Court of Australia agreed with several judgments of single judges of the Federal Court to the effect that all that is required by ss 33C and 33D is that lead plaintiffs have standing to sue the intended respondent(s).[15] Where that standing is conferred by legislation, these sections are satisfied notwithstanding the fact that the aspiring lead plaintiffs in question have not themselves been harmed by the impugned conduct. These judicial rulings have enabled the Australian Competition & Consumer Commission ("ACCC") to file six Part IVA proceedings, on behalf of aggrieved consumers, despite the fact that no loss was suffered by the ACCC. We will return to these class actions in Part IIIB below.

### B. Problems faced by aspiring class representatives

Despite reforms, which have been implemented in both the United Kingdom and Australia to make civil litigation more cost-effective, costs associated with maintaining legal proceedings, particularly complex commercial proceedings, continue to reach "dizzying heights".[16] In both jurisdictions, the most significant costs are the fees for the services provided by solicitors and barristers. Also substantial are disbursements such as the fees charged by experts,[17] witnesses' expenses, the cost of the transcripts of court hearings, filing fees[18] and other fees charged by the court.[19] To these costs, common to all legal proceedings, must be added costs that are either unique to, or particularly onerous in, class actions. They are explored below.

There are two dimensions to the liability for costs faced in class actions. The first relates to the costs incurred in running the case. The second concerns liability for the adversary's costs following an unsuccessful outcome. In the absence of retainer agreements entered into between individual class members and the solicitors hired by the class representatives, no solicitor-client relationship exists

[14] Part IVA, s 33T.

[15] *Finance Sector Union of Australia v Commonwealth Bank of Australia* (1999) 166 ALR 141. See also *Australian Competition and Consumer Commission v Chats House Investment Pty Ltd* (1996) 142 ALR 177; *Australian Competition and Consumer Commission v Golden Sphere International* (1998) 83 FCR 424; and V Morabito, "Ideological Plaintiffs and Class Actions - An Australian Perspective" (2001) 34 *University of British Columbia Law Review* 459.

[16] C Binham, "Reforms deliver fresh set of challenges for UK legal system" *Financial Times*, 24 July 2014.

[17] See Australian Productivity Commission Inquiry Report, *Access to Justice Arrangements* (Vol 1; 2014), para 11.6 noting that in Australia "expert evidence has been identified as one of the principal sources of expense, complexity and delay in civil proceedings". See also *Jarra Creek Central Packing Shed Pty Ltd v Amcor Limited* [2011] FCA 671, para 140 (per Jacobson J).

[18] See CC Whitehall, "Soaring court fees 'will discourage ordinary people from seeking justice'", *The Independent*, 27 January 2016.

[19] See Australian Productivity Commission Inquiry Report, above n 17, chap 16, fig 16.2; and New South Wales Law Reform Commission, *Security for Costs and Associated Costs Orders* (Consultation Paper 13; May 2011), paras 1.17-1.22.

between class members and the lawyers in question.[20] As a result, liability for the legal costs associated with advancing the class action is borne solely by the lead plaintiffs.

Similar to the position in the United Kingdom,[21] nor are class members exposed to the risk of adverse costs.[22] Accordingly, class members are able to effectively free ride on lead plaintiffs shouldering the financial responsibility for initiating and advancing class proceedings. While the cost shifting rule can compensate, to some extent, successful lead plaintiffs for the costs they bear when conducting a class action, the rule also substantially increases costs liability in the event that the claim is unsuccessful. Unsuccessful litigants will, in most cases, be ordered to pay a proportion of the costs incurred by their adversaries; usually "one-half to two-thirds of the costs actually incurred".[23] By contrast with the small sums lead plaintiffs are likely to recover on their own behalf, these costs are liable to be huge. In *Madgwick v Kelly*,[24] for example, which involved an application for security for costs, the Full Federal Court of Australia estimated that potential adverse costs faced by the lead plaintiffs amounted to between $7.4 million to $9.2 million. On the other hand, most class members were attempting to recover for losses of between $42,000 and $50,000.[25] Similar disparities are likely to be encountered in the United Kingdom. In the first collective proceeding launched since the new CAT regime came into force, the National Pensioners Convention initiated a collective claim for breach of vertical competition rules involving a class size of around 34,000 members each claiming a refund of £200, which is estimated to cost over £1 million to fund.[26]

The Federal Court of Australia has ordered that lead plaintiffs be compensated for the time and expenses incurred in taking on that role. These types of awards are known as incentive payments in the US and reimbursement payments in Australia. But this type of compensation has only been sought in a limited percentage of Part IVA proceedings and payments have generally been very low compared to the overall cost of the proceedings thus failing to constitute an adequate means of off-setting litigation risk.[27] The fact that individual lead plaintiffs gain little for bearing such disproportionate litigation risk on behalf of the class is a significant disincentive to act in that role unless it is possible to find someone willing to share the costs or bear some or all of the risk.[28]

One of the reasons class actions are so complex and costly in Australia is that the parties, particularly respondents, instigate large numbers of interlocutory applications that are frequently appealed.[29] Justice Beach of the Federal Court of Australia has recently drawn attention to the fact that "many class actions have considerable forensic technical complexity in dealing with common issues such as breach and causation".[30] Complying with requirements designed to protect the interests of class

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[20] *Muswellbrook Shire Council v The Royal Bank of Scotland NV* [2013] FCA 616, para 24 (per Bennett J).
[21] *Competition Appeal Tribunal Rules 2015* (UK), R 98.
[22] *Federal Court of Australia Act 1976* (Cth), s 43(1A).
[23] D Grave, K Adams & J Betts, *Class Actions in Australia* (2nd ed; Lawbook Co; Sydney; 2012), 730. See also Australian Law Reform Commission, *Grouped Proceedings in the Federal Court* (Report No 46; 1988), para 254 ("ALRC 1988 Report"); New South Wales Law Reform Commission, *Security for Costs and Associated Costs Orders* (Report 137; 2012), para 1.5; and Access to Justice Advisory Committee, *Access to Justice – An Action Plan* (1994), para 5.60, n77.
[24] (2013) 212 FCR 1, para 10 (per Allsop CJ & Middleton J).
[25] Ibid para 124 (per Jessup J).
[26] Shearman & Sterling LLP, "Launch of First UK Opt-Out Class Action", 11 March 2016 available at http://www.shearman.com/en/newsinsights/publications/2016/03/launch-of-first-uk-opt-out-class-action [accessed 1 April 2016].
[27] V Morabito, "An Empirical and Comparative Study of Reimbursement Payments to Australia's Class Representatives and Active Class Members" (2014) 33 *Civil Justice Quarterly* 175.
[28] *Woodlands v Permanent Trustee Co Ltd* (1995) 58 FCR 139, 145 (per Wilcox J).
[29] Hon M Wilcox QC, "Investor Class Actions" (Paper presented at the launch of the book *Investor Class Actions* at the Federal Court; Sydney; 3 August 2009), 8.
[30] Justice Beach, "The Use of Assessors in Class Actions" [2015] Issue 129 (July/August) *Precedent* 15, 22.

members has also contributed to the high costs incurred in running Part IVA proceedings.[31] A primary example of these safeguards is provided by the requirement that class members be advised of various important matters such as the commencement of the Part IVA proceeding, the right of class members to opt out of the litigation, and where the class action has been settled, their rights under the relevant settlement agreement.[32] The CAT also envisages that "opt-out collective proceedings (will) require intensive case management by the Tribunal, so as to ensure that the interests of the class are adequately protected".[33] But compliance with the requirements of Part IVA's notice regime can be rather costly, both where the Court directs that notices be published in several newspapers or other publications[34] (an event which has occurred on a fairly regular basis)[35] and where the notice is sent personally to each class member by mail.[36]

### C. Strategies adopted by the Australian Law Reform Commission and the drafters of Part IVA

Part IVA was largely based on the recommendations contained in a report on grouped proceedings completed by the Australian Law Reform Commission ("ALRC") in 1988.[37] Two strategies were recommended by the ALRC to help lead plaintiffs overcome the problems highlighted above. The first measure recommended by the ALRC was to create a special fund that would "provide support for the applicants' proceedings and to meet the costs of the respondent if the action is unsuccessful".[38] The ALRC also recommended that the legislative grouped proceeding regime authorise and regulate the employment of conditional costs agreements "which provide for calculation on the basis of a lump sum increase on party-party costs recovered or a fraction of multiple increase of scale costs".[39] These agreements would need to be approved by the Court and approval could only be provided where the Court formed the view that they were fair and reasonable to all concerned.[40]

Both recommendations were rejected by the drafters of Part IVA. No explanation for the omission regarding the public fund was provided. The non-implementation of the conditional fee recommendation was explained by Senator Tate, the then Minister for Justice and Consumer Affairs, during the Second Reading of the Federal Court of Australia Amendment Bill 1991 (the Bill that contained Part IVA) as follows:

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[31] One such safeguard is that the settlement or discontinuance of a Part IVA proceeding must be approved by the Court (s 33V). In a Part IVA proceeding settled in 2013 the costs that were incurred by the lead plaintiff in securing judicial approval of the settlement that it executed with the respondents exceeded half a million dollars: see *Richards v Macquarie Bank Limited* (Order by Logan J; 13 December 2013), Order 6(b). These costs are not likely to be recouped if the settlement is not judicially approved.

[32] Part IVA, s 33X.

[33] Competition Appeal Tribunal, *Guide to Proceedings* (2015), para 6.7.

[34] See V Waye & V Morabito, "Collective Forms of Consumer Redress: Financial Ombudsman Service Case Study" (2012) 12 *Journal of Corporate Law Studies* 1, 28; and *Johnson Tiles Pty Ltd v Esso Australia Pty Ltd* [2001] VSC 284, para 29 (per Gillard J).

[35] V Morabito, "Opt In or Opt Out? A Class Dilemma for New Zealand" (2011) 24 *New Zealand Universities Law Review* 421, 444. For a recent instance of advertising being "likely to be significantly more expensive than sending the Notice by ordinary prepaid mail and initiating follow-up contact", see *Muswellbrook Shire Council v The Royal Bank of Scotland NV* [2013] FCA 616, para 49 (per Bennett J). See also *Earglow Pty Ltd v Newcrest Mining Limited* [2016] FCA 1433, para 48 (per Murphy J) ("when class members' postal addresses are readily and inexpensively ascertainable that will usually be the most 'efficient and effective' method of providing notice to them").

[36] See, for instance, *Hodges v Waters (No 7)* [2015] FCA 264, para 103 (per Perram J) ("the second fee relates to the cost of the various mail outs to class members which have taken place and the call centre set up to deal with them. This amounted to approximately $350,000").

[37] ALRC Report 1988, above n 23.

[38] Ibid para 308.

[39] Ibid para 297.

[40] Ibid para 293.

> I do not believe this particular proposal will lead Australia to go down the United States road – as it is sometimes referred to – and become an overly litigious society … I do not think we are going down that road by means of this proposal because we have set our face firmly against some features of the American legal system, such as contingency fees, which appear, from my observations over there recently, to drive the American legal system rather than the merits of the issues themselves.[41]

Senator Tate's comments vividly highlight the error commonly made by the drafters of class action regimes when they are required to demonstrate, as is invariably the case, that their regimes will not generate the unsatisfactory consequences that are associated with US class action regimes. This error entails not providing the intended beneficiaries of the regimes with the financial tools or economic incentives required to overcome the financial barriers canvassed above and to effectively avail themselves of collective redress.

The drafters of Part IVA included only one measure designed to assist lead plaintiffs. Section 33ZJ authorises the Court to make an order that an amount equal to the whole, or a part, of the difference between the costs incurred in a Part IVA proceeding and the costs recoverable from the respondent be paid out of the damages awarded. This provision appears to be based on the mechanism that the ALRC proposed for ensuring that, in the event of a successful class action that produced a monetary fund (whether from the award of damages or settlement), what was owed to the class representative's solicitors would be deducted from this fund before it was distributed to class members.

But a number of crucial differences exist between s 33ZJ and the ALRC's proposal that have drastically reduced the utility of the former. The ALRC's mechanism was to operate before the conclusion of the proceeding. However, s 33ZJ only comes into play at the conclusion of the proceeding. Accordingly, it does not address the financial disincentives that are faced by aspiring lead plaintiffs at the outset of litigation.[42] Another significant restriction upon the scope of s 33ZJ is that, unlike the measure recommended by the ALRC, it is only activated by a particular type of successful outcome for the class: the award of damages (an outcome that has been extremely rare).[43] This term (and thus s 33ZJ) does not cover settled proceedings;[44] and settlement has been, by far, the most frequent outcome of Part IVA proceedings.[45] Subsequently, these shortcomings led the Federal Court to devise a number of pro-class law firm and pro-commercial funder mechanisms designed to maintain class actions as effective vehicles for collective redress. These mechanisms are elaborated upon in Parts IV and V.

## III. *AD HOC* FUNDING MODELS EMPLOYED IN PART IVA PROCEEDINGS

In 2009 Justice Wilcox of the Federal Court of Australia, who was one of the authors of the ALRC's 1988 report, revealed that when he learnt that the drafters of Part IVA decided not to set up the grouped proceeding fund recommended by the ALRC, he "thought there would be no group proceedings".[46] Obviously, this has not occurred. Nevertheless, there has been limited employment of the Part IVA regime with an average of 15.4 Part IVA proceedings being filed every 12 months from March 1992 to March 2016.[47]

The two most prevalent strategies that have been employed to fund Part IVA proceedings have entailed plaintiff solicitors acting on a no win - no fee basis, pursuant to which they generally receive

[41] Australia, *Commonwealth Parliamentary Debates*, Senate, 13 November 1991, 3025.
[42] See V Morabito, "Federal Class Actions, Contingency Fees, and the Rules Governing Litigation Costs" (1995) 21 *Monash University Law Review* 231, 237; Grave *et al*, above n 23, 751-753; and *Woodlands v Permanent Trustee Co Ltd* (1995) 58 FCR 139, 145 (per Wilcox J).
[43] Morabito, Fourth Report, above n 11, 13.
[44] See Grave *et al*, above n 23, 751.
[45] Morabito, Fourth Report, above n 11, 13.
[46] Wilcox, above n 29, 6.
[47] Morabito, Fourth Report, above n 11, 6.

nothing if the case is lost and more than the standard remuneration if monetary compensation is secured in the proceedings[48] and, over the last fifteen years or so, funding and indemnities for costs supplied by commercial litigation funders. They are canvassed in Parts IV and V, respectively. We now explore a variety of other funding strategies that have been employed in federal class actions.

### A. Self-represented class representatives

An appropriate starting point is to consider those Part IVA proceedings which were filed despite the apparent lack of any funding. We are referring here to class actions where the class representatives had no solicitor acting for them "on the record" for all or most of the proceedings. This state of affairs was witnessed in 12 Part IVA proceedings.[49] Not surprisingly, the vast majority of these Part IVA cases had an unsuccessful outcome for the relevant groups of claimants.[50]

It seems even more unlikely that self-represented class representatives will secure CAT authorisation in the United Kingdom. Only persons authorised by the CAT are entitled to act as class representatives,[51] and authorisation will only be granted if just and reasonable.[52] Matters to be taken into account include the ability of the proposed representative to fairly and adequately represent the class as well as their ability to pay the defendant's recoverable costs.[53] Given the unsuccessful nature of Australian self-represented class representatives, such constraints appear justified.

### B. Public Regulators

The overall framework of *Consumer Rights Act 2015*, Schedule 8 suggests that, apart from the approval of voluntary redress schemes by the Competition & Markets Authority,[54] collective opt-in and opt-out proceedings are intended to supplement regulatory action, rather than act as mechanisms directly employed by regulators.[55] By contrast, public regulators have been significant users of Australia's federal class action regime.

The ACCC has assumed the role of lead plaintiff in six Part IVA proceedings while, in ten Part IVA proceedings, the Australian Securities & Investments Commission ("ASIC") has acted as the legal representative of the lead plaintiffs and provided them with an indemnity for any adverse costs orders. A majority of these proceedings have been successful (especially those run by ASIC)[56] and no financial contributions were sought from class members with respect to the costs and disbursements incurred in running the proceedings on their behalf. Furthermore, in the nine ASIC class actions that generated settlement proceeds, subject to the exception mentioned in the next paragraph, no portion of these settlement proceeds was applied to reimburse ASIC for its legal costs and disbursements. As a result, eligible class members received greater compensation.[57]

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[48] See also Australian Law Reform Commission, *Managing Justice – A Review of the Federal Civil Justice System* (Report no 89; 2000), para 7.90.

[49] V Morabito, "Replacing Inadequate Class Representatives in Federal Class Actions – *Quo Vadis*?" (2015) 38 *University of New South Wales Law Journal* 146, 165.

[50] A rare example of a self-represented class representative securing a positive outcome, through a settlement, in a Part IVA proceeding is furnished by *Boase v Sullivan Commercial Pty Ltd Ltd trading as McGees Property (No 3)* [2013] FCA 15.

[51] *Competition Act Act*, s 47B(7)(a).

[52] *Competition Act Act*, s 47B(8)(b).

[53] *Competition Appeal Tribunal Rules 2015*, R 78(2).

[54] *Competition Act 1998*, s 49C.

[55] For example, Schedule 8 is entitled "Private Actions in Competition Law". See further Department for Business Innovation and Skills, above n 4.

[56] Ninety per cent of the Part IVA proceedings run and funded by ASIC generated settlement proceeds for the relevant class members.

[57] See *Rikys v Bongiorno Financial Advisers (Aust) Pty Ltd* [2009] FCA 1603, para 16 (per Finkelstein J); *Markov v Dukes* [2010] FCA 1419, para 8 (per Finkelstein J); and *Stoyef v Masu Financial Management Pty Ltd (No 2)* [2008] FCA 1849, para 19 (per Lindgren J).

In at least two of these cases, pursuant to the judicially-approved settlement agreement, ASIC was only entitled to what was left in the settlement fund, if anything, after the settlement distribution process was completed.[58] It is fascinating to note that this dimension of the settlements in question executed by ASIC is in essence the scenario dictated by s 47C(6) of the *Consumer Rights Act 2015*, which provides victorious representative plaintiffs with a right to recoup some of their fees and disbursements from unclaimed damages. However, s 47C(6) has been criticised by Higgins and Zuckerman who have argued, among other things, that it has created uncertainty for prospective funders as well as a conflict of interest between funders and class members.[59] These problems will be further elaborated upon below.

### C. Trade unions

In over 30 Part IVA proceedings filed during the review period trade unions covered the costs of the proceedings and accepted responsibility for the costs of the opponents in unsuccessful cases.[60] Approximately 74 per cent of these union-funded cases were successful and recoupment from class members of some of the costs and disbursements incurred in securing a favourable outcome (that they were not able to recover from their adversaries) was not demanded from class members in approximately half of these cases.[61] Less desirable, for those non-union employees who were involved in the disputes that led to these class actions, was that approximately two-thirds of these Part IVA proceedings were brought for the benefit of union employees only.[62]

### D. Class Representatives and class members

Class representatives, other than ACCC, funded the litigation entirely on their own (without any support from any of the class members or third parties) in at least 10 Part IVA proceedings filed during the review period.[63] Conversely, financial contributions provided by class members constituted the principal funding strategy in at least 22 Part IVA proceedings. These contributions came from all, some or only a minority of the class members.[64]

In approximately a third of these Part IVA proceedings, the financial support offered by class members encompassed an indemnity for any costs orders that may be made against the class

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[58] *Casey v State Trustees Limited* [2010] FCA 163, para 11 (per Gordon J); and *Goodman, in the matter of Glenhurst Corporation Pty Ltd (In Liq)* [2010] FCA 667, para 8 (per Gordon J). This provision simply recognised the fact that, frequently, not all class members entitled to receive a share of a settlement fund take the steps required to exercise their entitlement: see, for instance, Morabito, above n 35, 438-439; *Jarra Creek Central Packing Shed Pty Ltd v Amcor Limited* [2011] FCA 671, para 63 (per Jacobson J); and Mulheron, above n 7, 431-432.

[59] See Higgins & Zuckerman, above n 6, 13.

[60] The relevant unions were also plaintiffs in approximately half of the class actions they funded whilst one or more of the aggrieved workers assumed the role of class representatives. This meant that whilst the unions were parties to the same proceedings, they only pursued their individual claims and did not formally represent the groups of aggrieved workers.

[61] See, for instance, *Constructions, Forestry, Mining and Energy Union v Contract Blinds Pty Ltd* [2009] FCA 572.

[62] For a comprehensive empirical analysis of union-supported Part IVA proceedings filed on or before 3 March 2009, see J Caruana and V Morabito, "Australian Unions – The Unknown Class Action Protagonists" (2011) 30 *Civil Justice Quarterly* 382.

[63] See, for instance, *AF & ME Pty Ltd v Aveling* (Order by Jenkinson J; 24 May 1994), Annexure. With respect to Victorian class actions, see *Melbourne City Investments Pty Ltd v Myer Holdings Ltd* [2016] VSC 239, para 37 (per Derham AsJ).

[64] This strategy was witnessed in the first-ever class action filed pursuant to Part IVA, *Metcalfe v NZI Securities (Australia) Ltd*, as most of the funding for this proceeding was provided by two class members: Affidavit of Christopher Lee (sworn on 28 August 1995), paras 7-9. See also *Kelly v Willmott Forests Ltd (in liq) (No 4)* [2016] FCA 323.

representatives.[65] Financial support from class members was mostly seen in Part IVA proceedings filed by migrants, refugees, employees, franchisees, real estate purchasers and/or owners and investors in tax-minimisation schemes. In at least eight Part IVA proceedings, companies and various kinds of associations and committees were formed, prior to the filing of the class action litigation, primarily to secure contributions to the costs of running the proceedings from as many class members as possible.[66]

### E. Legal aid

Notwithstanding concerns expressed by the ALRC, with respect to the suitability of legal aid as a funding model for grouped proceedings,[67] legal aid has enabled the filing of at least seven Part IVA proceedings. Whilst five of these cases were filed on behalf of migrants,[68] the biggest and best-known Part IVA litigation supported by legal aid were two proceedings filed with respect to a home loan scheme, known as the HomeFund scheme, announced by the NSW Government in 1986 pursuant to which the NSW Government would "organise the provision of low start housing loans of $50 million to benefit upwards of 1,000 borrowers".[69] However, analogous with circumstances in the United Kingdom, severe cuts to legal aid since the 1990s have substantially diminished this source of funding.[70]

### F. Public bodies, NPOs and pro bono legal services

Several publicly-funded entities and not-for-profit organisations have run Part IVA proceedings; usually in conjunction with lawyers representing the class representatives on a pro bono basis.[71] These two funding models (either together or on their own) have mostly been witnessed in class actions filed on behalf of refugees, migrants, intellectually disabled persons and indigenous persons.[72]

### G. Associations, external donors and insurance companies

Various unincorporated associations provided the required funding in several migration class actions.[73] Other associations undertook the task of collecting donations from members of the public of the same nationality as the relevant class members.[74] Financial support, of varying significance, was also provided in at least 10 non-migration class actions by entities that had varying degrees of interest in the substantive claims being pursued in the litigation.[75]

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[65] For instance, an indemnity was provided by most class members in *Wong v Silkfield Pty Ltd*. See also *Walsh v WorleyParsons* [2015] VSC 135, para 38 (per Almond J).

[66] See, for instance, *Legal Services Commissioner v Scott* [2009] LPT 7, para 6 (per Fryberg J); and *Milfull v Terranora Lakes Country Club Ltd* [2006] FCA 801.

[67] ALRC Report 1988, above n 23, para 309. See also Justice J Basten, "Procedural Reform: The New Part 10" (Paper delivered to Justices of the Supreme Court of NSW; 19 July 2011), 11.

[68] See, for instance, *Tsang Chi Ming v Uvanna Pty Ltd* (1996) 140 ALR 273.

[69] Cited in *Woodlands v Permanent Trustee Co Ltd* (1996) 68 FCR 213, 218 (per Wilcox, Burchett and Olney JJ).

[70] B Murphy & C Cameron, "Access to Justice and the Evolution of Class Action Litigation in Australia" (2006) 30 *Melbourne University Law Review* 399, 438.

[71] These entities have included the AED Legal Centre, the Public Interest Advocacy Centre, the Aboriginal Legal Service, the Aboriginal Legal Rights Movement, the Human Rights Law Resource Centre Ltd and Aged-Care Rights Service Inc.

[72] See V Morabito & J Ekstein, "Class Actions Filed for the Benefit of Vulnerable Persons - An Australian Study" (2016) 35 *Civil Justice Quarterly* 61, 65, 68-70 & 88.

[73] In some cases these associations were created solely for the purpose of supporting and co-ordinating the litigation: see V Morabito, "An Empirical Analysis of Appeals by Class Members in Australia's Federal Class Actions" (2013) 42 *Common Law World Review* 240, 257.

[74] See, for instance, R Tang, "Chinese Students Take Class Action", *Sydney Morning Herald*, 20 November 1993, 6. See also *Bitel v Ruddock* [2001] NSWSC 43.

[75] See Waye & Morabito, JCLS, above n 34, 25 and https://www.afff.com.au/t/cases.

Where the conduct that is challenged in the proceedings has caused significant losses with respect to which insurance claims have been made the insurers may also decide to be involved in these proceedings. This scenario was witnessed, for instance, in the *Buckee v Commonwealth of Australia* Part IVA proceeding where the insurers of the lead plaintiffs brought the class action pursuant to their right of subrogation under the relevant policy.[76]

### H. Outcomes

In Part IVA litigation not supported by ASIC, ACCC or trade unions, no favourable outcome was secured for class members in most of the cases where one or more of the funding strategies set out above were employed, subject to one exception. The exception relates to non-migration class actions supported mainly by class members; although attention should be drawn to the fact that in approximately half of these cases some of the alleged victims were excluded, from either the class action or from receiving a share of the settlement proceeds that the litigation produced, because of their unwillingness or inability to make a financial contribution.[77] These are illustrations of closed classes and closing the class devices, respectively, which are explored below. It is also important to note that the vast majority of the class actions filed on behalf of extremely vulnerable individuals (Indigenous people, refugees and migrants) which relied on some of the funding approaches outlined above, were unsuccessful.[78]

## IV. LAWYER-FUNDED CLASS ACTIONS

### A. Signing up enough class members

Since the enactment of Part IVA, the legislatures of several Australian States have enacted statutes that allow lawyers to enter into conditional costs agreements with their clients, pursuant to which uplift fees may be charged in the event of a successful outcome. However, the scope of permissible conditional fee agreements in Australia is far more restrictive than that operating in the United Kingdom where up to a 100 per cent uplift fee can be claimed.[79] In Victoria and New South Wales, for instance, a conditional costs agreement may provide for the payment of an uplift fee not exceeding 25 per cent of the legal costs (excluding disbursements) otherwise payable.[80]

Damages based fees are prohibited in Australia.[81] Nonetheless, the prohibition only applies to lawyers; thus, allowing commercial litigation funders to charge these fees. This preferential treatment enjoyed by litigation funders has prompted a number of interesting initiatives by plaintiff law firms. The most ambitious of these initiatives was implemented in a shareholder Part IVA proceeding filed in 2012 on behalf of shareholders of the respondent that had entered into a litigation funding agreement with McNichol Pty Ltd:

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[76] See *Buckee v Commonwealth of Australia* [2014] FCA 242, para 9 (per Barker J) ("the proceeding may be seen effectively as a dispute between insurers of those whose property was damaged and [one of the respondents'] insurers"). See also, with respect to NSW and Victorian class actions, *Matthews v SPI Electricity Pty Ltd & Ors (No 9)* [2013] VSC 671, paras 20-30 (per Derham AsJ); V Morabito, "Clashing Classes Down Under - Evaluating Australia's Competing Class Actions through Empirical and Comparative Perspectives" (2012) 27 *Connecticut Journal of International Law* 245, 271 n106; and *Johnston v Endeavour Energy* [2015] NSWSC 1117.

[77] See, for instance, *Legal Services Commissioner v Scott* [2009] LPT 7, para 8 (per Fryberg J).

[78] Morabito & Ekstein, above n 72, 88.

[79] *Conditional Fee Agreements Order 2013*, Art 3. Although note that Art 5 imposes a cap of 25 per cent in respect of certain personal injury matters.

[80] *Legal Profession Uniform Law*, s 182(1) & (2).

[81] However, in 2014 the Australian Productivity Commission recommended the adoption of damages based fees capped on a sliding scale for retail clients in class actions: Australian Productivity Commission, above n 17, 625-629. The Australian Government has yet to respond to the recommendations.

> [A]s Mr Jones candidly explains in his affidavit, this litigation is being funded… by a company under the control of Mr Jones who is also the principal of the firm representing the applicants who are now, only really by name, the applicants in the proceeding having assigned their causes of action to Mr Jones's company McNichol [the litigation funder].[82]

Australia's most successful plaintiff law firm, Maurice Blackburn, has stated that if it were allowed to charge damages based fees in class actions, it would do so inclusive of all fees and disbursements for a 25% contingency fee.[83] However, there would be few Australian law firms that would be in a position to not only finance long and hard fought class proceedings on a contingency basis but also to bear the potential risk of adverse costs.[84] Even in the United Kingdom where damages based agreements are available for use outside of the opt-out competition proceedings[85] without any concomitant exposure to adverse cost risk, the take up of these kinds of agreements has been sparing,[86] suggesting that concern regarding contingency fees may be overblown.

To be effective in Australian law, the conditional fee agreement must be signed by the client and incorporate a statement that the client has been informed of their right to seek independent legal advice prior to execution.[87] Executing conditional fee agreements with only the class representatives provides very limited benefits for the solicitors in question given that their individual claims are, more often than not, rather modest.[88] As outlined previously, even where the monetary value of their claims is substantial, the claims will almost invariably be dwarfed by the overall costs and disbursements incurred in running the proceeding. To recover a substantial portion of the value of their professional services class action law firms will therefore need to execute conditional fee agreements with as many claimants as possible and, in particular, those with the largest claims. Without a critical mass of conditional fee agreements in place, there is a substantial risk that the class action law firm will be out of pocket by some millions of dollars.[89]

But the recruitment of a sufficient number of class members faces a number of practical problems. The most fundamental obstacle is the fact that - under an opt out regime such as the one used in Part IVA - a claimant who falls within the ambit of the represented group is a class member whether or not a conditional fee agreement is executed or whether the member agrees to make a contribution to the costs of the proceeding.[90] Unless, of course, plaintiff lawyers are permitted to define the represented

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[82] *Valda Pty Ltd v Mcarthur Coal Ltd* (Transcripts of proceeding; 20 June 2012), p 11 (PE Anastassiou SC). The reference to "applicants" is to the class members as the Originating Application listed each class member and referred to them as "Second Applicant", "Third Applicant" and so on.

[83] L Bullock, "Contingency Plan", *Lawyers Weekly*, 22 March 2016 quoting Andrew Watson from Maurice Blackburn. Two senior Maurice Blackburn solicitors have recently revealed that an internal analysis of funded shareholder class actions conducted by Maurice Blackburn found that a 25 per cent contingency fee would have seen an extra $90 million returned to class members compared with what they actually received after the litigation funders received their remuneration: B Slade and J Ekstein, "Class Actions and Social Justice: Achievements and Barriers" in D Grave and H Mould (eds), *25 Years of Class Actions in Australia* (Ross Parsons Centre of Commercial, Corporate and Taxation Law ; 2017), ch 15.

[84] Australian Productivity Commission, above n 17, 636 - 637 recommending that courts should have a discretion to make adverse costs orders against law firms acting pursuant to DBAs in the same way that courts have a discretion to make an adverse costs order against funders.

[85] *Competition Act 1998*, s 47(8).

[86] Civil Justice Council, Damages Based Agreements (DBAs), Publication of CJC Recommendations 2 September 2015 available at https://www.judiciary.gov.uk/announcements/damages-based-agreements-dbas-publication-of-cjc-recommendations/ [accessed 3 April 2016] noting that the review examining ways to improve DBA regulation was prompted by the sparing use of DBAs as a funding mechanism.

[87] *Legal Profession Uniform Law*, s 181.

[88] See, for instance, V Morabito, "An Australian Perspective on Class Action Settlements" (2006) 69 *Modern Law Review* 347, 379.

[89] *Johnson Tiles Pty Ltd v Esso Australia Pty Ltd* (1999) 166 ALR 731, 740 (per Merkel J).

[90] As a result, class members have little incentive to become clients of the solicitors running the case. See, for example, *Kelly v Willmott Forests Ltd (in liq) (No 4)* [2016] FCA 323, para 32 (per Murphy J) noting that in one

group, in the pleadings, as including only those claimants who have executed retainer agreements with them. We now turn our attention to this strategy.

### B. Closed classes and closing the class mechanisms

#### (i) Closed classes

Prompted by class action law firms, who strongly advocated in favour of a funding scheme that would make class actions financially viable, in 2007 the Full Federal Court acceded to specifications in the pleadings that inclusion in the group of claimants was dependent on becoming clients of the class representative's solicitors.[91] A class defined in this manner subsequently became known as a "closed class".[92] This judicial approach was facilitated by Part IVA's s 33C, which (as explained in Part IIA above) provides that where there has been compliance with Part IVA's three commencement criteria, a proceeding may be brought on behalf of "all or some" of the claimants.

The rise of investor class actions, explored below, escalated the adoption of the closed class mechanism and presaged the involvement of commercial litigation funders, whose activities had previously been confined to non-class insolvency matters. The Second Reading Speech for the Bill that contained Part IVA revealed that shareholders and other investors, together with consumers, were intended to be the primary beneficiaries of this procedural device.[93] But when Maurice Blackburn filed a Part IVA proceeding on behalf of the shareholders of GIO Australia Holdings Ltd in August 1999, there had been only one other shareholder class action filed pursuant to Part IVA which was subsequently dismissed (in March 2000) for want of prosecution.[94] The GIO proceeding was brought on behalf of all relevant GIO shareholders, estimated to be over 67,000, and was conducted on a no win - no fee basis.[95] It was settled four years later for $97 million plus legal costs of over $15 million.[96]

At the time, it was Australia's biggest class action settlement and it is still one of the country's largest ever class action settlements. The size of this settlement showed Maurice Blackburn, other plaintiff solicitors and commercial litigation funders that shareholder class actions and investor class actions generally had the potential to provide significant compensation for aggrieved investors and, of course, their lawyers and/or funders. The practical effect which the discovery has had on the types of substantive claims advanced in Part IVA litigation may be seen by comparing data with respect to the first 12 years of the operation of Part IVA with data concerning the second 12 years. In the first 12 years actions filed on behalf of shareholders and other investors represented 11 per cent of all Part IVA proceedings filed during that period. In the second 12 years of the life of Part IVA, this percentage increased to 52.4 per cent.[97] In Part V other features of investor class actions that have made them particularly appealing to commercial litigation funders will be mentioned.

Commentators such as Higgins[98] and Mulheron[99] have suggested that the use of closed or tied classes is incompatible with the United Kingdom's CAT regime where the CAT must determine whether the

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of the proceedings under consideration there were 446 client class members and 3,319 non-client class members.

[91] *Multiplex Funds Management Limited v P Dawson Nominees Pty Limited* (2007) 164 FCR 275.

[92] *Kelly v Willmott Forests Ltd (in Liquidation)* [2012] FCA 1446, para 64 (per Murphy J).

[93] Australia, *Commonwealth Parliamentary Debates*, House of Representatives, 14 November 1991, 3174-3175 (Michael Duffy, Commonwealth Attorney-General).

[94] *National Mutual Life Association of Australasia Ltd v Reynolds* [2000] FCA 267.

[95] *King v AG Australia Holdings Ltd (formerly GIO Australia Holdings Ltd)* [2002] FCA 872, para 10 (per Moore J).

[96] *King v AG Australia Holdings Ltd (formerly GIO Australia Holdings Ltd)* [2003] FCA 980.

[97] Morabito, Fourth Report, above n 11, 11-12.

[98] Higgins, above n 6, 460

[99] Mulheron, above n 6, 305-307.

proceedings are to be opt-in or opt-out.[100] Thus, if the class was defined as those persons who suffered loss because of a breach of competition law as well as those who signed a conditional fee agreement with a law firm, then the CAT proceeding should be undertaken as an opt-in proceeding. The fact that damages based agreements are available in opt-in collective proceedings[101] is consistent with that interpretation.

On a more normative basis, Higgins and Mulheron argue that closed classes should be avoided because: they impose high transaction costs associated with class member recruitment; they undermine the deterrent benefits of a broad based opt-out regime by unduly narrowing the class; and they fail to resolve the free rider problem.[102] If their views are correct, then it is likely United Kingdom law firms will find it difficult to recruit claimholders to conditional cost agreements which, in the absence of a common fund approach or damages based agreements, may discourage many United Kingdom law firms from being willing to act on their behalf in opt-out proceedings. Class actions can cost millions[103] and can take many years to resolve.[104] Lead plaintiffs cannot bear these costs and most law firms are unwilling to bear these costs without a high risk premium or without assistance from third party funders.

### (ii) Closing the class

What the GIO class action also revealed to plaintiff solicitors was that investor class actions were likely to be among the most expensive types of grouped proceedings; a fact that became more obvious with each subsequent investor class action.[105] Another lesson learnt from the GIO class action was subsequently described as follows by Bernard Murphy, the then Chairman of Maurice Blackburn:

> the absence of [the closed class device in the GIO class action] had the direct consequence that very substantial time and resources of the parties and the Court had to be expended in determining first which shareholders were in the class, and then which of those were interested in participating in the settlement.[106]

The costs referred to above were incurred in sending several forms and questionnaires to class members who were not clients of Maurice Blackburn.[107] The most important of these documents was called Form C. This document advised unrepresented class members (who had not opted out of the litigation) that they needed to fill out and return the form by a certain date in order to remain as class members and, as a result, to be eligible to share the fruits of a successful outcome of the class

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[100] *Competition Act 1998*, s 47B(7)(c); *Competition Appeal Tribunal Rules 2015*, R 8(1)(f).
[101] *Competition Act 1998*, s 47C(8).
[102] This latter point argued by Mulheron only refers to "closed classes" which are defined at the outset of the proceedings according to retainer and or funding agreements. It does not apply to "closing the class" orders which operate res judicata against those who fail to identify themselves as part of the class and which are discussed further below.
[103] See, for instance, *Jarra Creek Central Packing Shed Pty Ltd v Amcor Limited* [2011] FCA 671, para 9 (per Jacobson J) and *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Ltd* [2016] FCAFC 148, para 180 (per Murphy, Gleeson and Beach JJ) ("despite the intent of the legislature, the costs and risks associated with class action proceedings have placed such litigation beyond the resources of ordinary and even most wealthy Australians").
[104] See Morabito, Fourth Report, above n 11, 9-10 for various data regarding the duration of settled Part IVA proceedings.
[105] See, for instance, *Vernon v Village Life Ltd* [2009] FCA 576, para 51 (per Jacobson J); *P Dawson Nominees Pty Ltd v Brookfield Multiplex Ltd (No 4)* [2010] FCA 1029, para 1 (per Finkelstein J); *Clime Capital Limited v Credit Corp Group Ltd (No 3)* [2012] FCA 218, para 15 (per Nicholas J); and *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Ltd* [2016] FCAFC 148, para 180 (per Murphy, Gleeson and Beach JJ).
[106] Affidavit of Bernard Michael Murphy (sworn on 31 March 2005 in *Dorajay Pty Ltd v Aristocrat Leisure Limited*), p 14.
[107] See V Morabito, "Revisiting Australia's First Shareholder Class Action" in Justice KE Lindgren (ed), *Investor Class Actions* (Ross Parsons Centre of Commercial, Corporate and Taxation Law; 2009) 34, 52-54.

action.[108] This process was authorised by Justice Moore despite acknowledging that it "created, in practical effect, an opt in process notwithstanding the scheme of Part IVA and the terms of the notice inviting individuals to opt out".[109]

The Form C mechanism implemented in the GIO class action provides an example of what are commonly referred to as "closing the class" mechanisms which are now frequently employed in Part IVA proceedings where funders or conditional fee agreements are involved.[110] The principal rationales for the device were recently explained as follows by the Full Federal Court of Australia:

> Such orders have the benefit of providing the respondent with greater finality on any settlement. … They also tend to facilitate settlement by allowing both sides to have a better understanding of the total quantum of class members' claims.[111]

In most cases, the consequence for those class members who fail to adhere to the conditions imposed by these mechanisms (which usually entail filling in a form and sending it to the class representative's solicitor) is that they are barred from taking any future legal action, against the entities and persons on the receiving end of the class action, with respect to the subject matter of the Part IVA proceeding.[112] In GIO, on the other hand, failure to return Form C simply meant that they were no longer class members but their rights to start individual proceedings or another class action were preserved.[113]

### C. Dominance of only two plaintiff law firms

Despite the growth of the investor class actions "industry" and the judicial endorsement of closed classes and closing the class mechanisms, before the emergence of commercial litigation funders the employment of the Part IVA regime was rapidly declining. In the four year period between 4 March 2003 and 3 March 2007, only 28 Part IVA proceedings were commenced. As the Law Council of Australia explained in 2006:

> it is generally not viable for most law firms to fund representative proceedings on a conditional basis. … The price of failure is high, too high for many to risk it again. Only major firms with significant capital reserves have the financial capacity to fund large-scale commercial litigation - and generally not more than one at a time, due to the high risk and cost involved. While law firms are able to facilitate access to justice for some, this work is but a fraction of the overall assistance required for plaintiffs in this area.[114]

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[108] *King v AG Australia Holdings Ltd (formerly GIO Australia Holdings Ltd)* [2003] FCA 980, paras 7-9 (per Moore J).

[109] *King v AG Australia Holdings Ltd (formerly GIO Australia Holdings Ltd)* [2003] FCA 1420, para 24 (per Moore J).

[110] As explained by Justice J Forrest J of the Supreme Court of Victoria, "class closure is a different concept to that of a closed class. This expression means … that a court may require group members to identify themselves by a certain point in time as having an interest in any judgment or proposed settlement. Failing a declaration of such interest (normally achieved by registering with a court or a firm of solicitors by a certain date), any subsisting entitlement to damages of the group members relating to the claim may be extinguished": *Matthews v SPI Electricity and SPI Electricity Pty Ltd v Utility Services Corporation Ltd (Ruling No 13)* [2013] VSC 17, para 23.

[111] *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Ltd* [2016] FCAFC 148, para 190 (per Murphy, Gleeson and Beach JJ). See also *Inabu Pty Ltd v Leighton Holdings Ltd* [2014] FCA 622, para 21 (per Jacobson J); and *Earglow Pty Ltd v Newcrest Mining Limited* [2016] FCA 1433, para 30 (per Murphy J). See, however, *Winterford v Pfizer Australia Pty Ltd* [2012] FCA 1199, paras 7-8 (per Bromberg J); *Jackson v GP & JM Bruty Pty Ltd (Ruling No 1)* [2016] VSC 717, paras 33-34; and Morabito, above n 88, 353-354.

[112] See *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Ltd* [2016] FCAFC 148, para 189 (per Murphy, Gleeson and Beach JJ); *Inabu Pty Ltd v Leighton Holdings Ltd* [2014] FCA 622, paras 13-17 (per Jacobson J); *Jackson v GP & JM Bruty Pty Ltd (Ruling No 1)* [2016] VSC 717, para 28 (per J Forrest J); and *Collin v Aspen Pharmacare Australia Pty Ltd* [2013] FCA 952, para 4 (per Davies J).

[113] Morabito, GIO, above n 107, 53.

[114] Law Council of Australia, *Litigation Funding* (submission to the Standing Committee of Attorney-Generals; 14 September 2006), para 33.

Only two plaintiff law firms, Maurice Blackburn and Slater & Gordon, have fully matched the description set out above. The outcomes of their class actions have been vastly superior to the outcomes secured by other law firms.[115] The willingness and capacity of these firms to run class actions on a no win - no fee basis has been of particular importance in those areas which have been largely ignored by commercial litigation funders. One such area, which is explored in Part V below, is the competition law area. Even more significant is the fact that many vulnerable claimants were able to secure access to the Federal Court and, in some cases, some form of legal redress, thanks to class actions funded pursuant to conditional costs agreements by these firms, [116] including the class actions that secured the country's two largest settlements arising out of devastating bushfires,[117] and run by Maurice Blackburn on a no win - no fee basis.

### D. Liability for adverse costs awards

No win - no fee agreements entered into by lead plaintiffs with their solicitors do not usually provide that the solicitors in question will cover costs that may be awarded against the lead plaintiffs.[118] Accordingly, in the absence of a costs indemnity provided by litigation funders, other third parties[119] or class members,[120] class representatives will continue to be solely responsible for the costs awarded to their adversaries. However, recent developments suggest that, as a result of the growth of After the Event/adverse costs insurance,[121] plaintiff solicitors might in the future be more willing to indemnify lead plaintiffs for adverse costs awards.

In June 2015, Slater & Gordon secured an order in the *Creighton v Australian Executor Trustees Ltd* Part IVA proceeding authorising it to send to class members a notice advising them of the commencement of the proceeding and the costs arrangements made for the litigation. Most relevant for present purposes is that this notice explained to class members that the lead plaintiff had obtained an adverse costs indemnity from Slater & Gordon; that Slater & Gordon had, in turn, secured adverse costs insurance in respect of this indemnity and that the cost of this insurance will form part of the legal costs for which reimbursement will be sought in the event that the claim is successful. This notice also revealed to class members that Slater & Gordon believed that these funding arrangements "will produce a substantially better outcome for group members than if a commission-based litigation funding had been preferred".[122]

## V. COMMERCIAL LITIGATION FUNDERS

Combined with the ban on contingency fees, the repeal of maintenance and champerty in a number of Australian states,[123] provided fertile ground for the development of a financing model comprised of underwriting legal fees in exchange for a share of class members' compensation. Currently,

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[115] V Morabito, *Class Action Facts and Figures* (An Empirical Study of Australia's Class Action Regimes; First Report; December 2009), 35-36; and Morabito, Fourth Report, above n 11, 10.
[116] Morabito & Ekstein, above n 72, 87.
[117] *Matthews v AusNet Electricity Services Pty Ltd & Ors* [2014] VSC 663; and *Rowe v AusNet Electricity Services Pty Ltd* [2015] VSC 232. Similarly, a Part IVA proceeding, filed with respect to faulty hip implants, which produced the country's third largest settlement fund was also run on a no win - no fee basis: *Stanford v DePuy International Ltd (No 6)* [2016] FCA 1452.
[118] A Watson & M Donelly, "Funding Access to Justice: Third-Party Litigation Funding and Class Actions in Australia" (2014) 55 *Canadian Business Law Journal* 17, 21. See, however, Grave *et al*, above n 23, 773.
[119] See, for instance, *Hall v Australian Finance Direct Limited* [2005] VSC 306, para 118 (per Hollingworth J).
[120] See, for instance, *Kelly v Willmott Forests Ltd (in Liquidation)* [2012] FCA 1446, para 98 (per Murphy J); and *Hall v Australian Finance Direct Limited* [2005] VSC 306, para 117 (per Hollingworth J).
[121] See also M Papadakis, "ATE Insurance to Open Litigation Funding Market", *Australian Financial Review*, 7 November 2014; and *Kelly v Willmott Forests Ltd (in liq) (No 4)* [2016] FCA 323, para 105 (per Murphy J).
[122] *Creighton v Australian Executor Trustees Ltd* (Order by Middleton J; 26 June 2015), Annexure A, p 3.
[123] See, for instance, *Maintenance, Champerty and Barratry Abolition Act 1993* (NSW); *Wrongs Act 1958* (Vic), s 32; *Crimes Act* 1958 (Vic), s 322A; *Criminal Law Consolidation Act 1935* (SA), Sch 1, s 1(3).

Australian funders charge an average 30 per cent commission,[124] but this may range between 20 and 50 per cent of the compensation received by class members.[125]

Additionally, while it is not strictly necessary for funders to indemnify lead plaintiffs against adverse costs,[126] as Australian courts have broad powers to award costs against those that support and finance litigation[127] typically most litigation funders do so, and where they do not indemnity may be sought from legal expense insurers.[128] Furthermore, Australian courts also have the power to order security for costs,[129] and funders therefore may be called upon by lead plaintiffs to make such arrangements for the matter to proceed.[130]

### A. Similarity between Australia and UK

When considering the design of the CAT class action regime, the United Kingdom Government was clear that it wished to avoid a situation where class law firms acting on a contingency fees and litigation funders were entitled to initiate competition claims. The government wanted only genuinely representative bodies or the claimants themselves to be able to initiate class proceedings.[131] This view, insofar as the ban on damages based fees was concerned, was justified on the basis of perceived conflicts of interest between the class action law firm and class members and largely derived from poor settlement outcomes experienced in the US.[132]

The government also remained firmly opposed to the possibility of claim assignment to special purpose vehicles ("SPVs") that might be established by funders or other third party investors to aggregate claims. Consequently, the funding constraints eventually adopted by the United Kingdom to a certain extent have thus been moulded (whether intentionally or not) to match the conditions underpinning the development of the Australian commercial funding model.[133]

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[124] V Morabito & V Waye, "Reining in Litigation Entrepreneurs: A New Zealand Proposal" [2011] *New Zealand Law Review* 323, 346. See generally *Earglow Pty Ltd v Newcrest Mining Limited* [2016] FCA 1433, paras 167 - 177 (per Murphy J).

[125] US Chamber Institute for Reform, *Third Party Litigation Financing in Australia – Class Actions, Conflicts and Controversy* (2013) pp 3 - 4 - Appendix to Submission to the Australian Productivity Commission, Access to Justice Arrangements Inquiry available at http://www.pc.gov.au/inquiries/completed/access-justice/submissions [accessed 23 February 2016].

[126] *Jeffery & Katauskas Pty Ltd v SST Consulting Pty Ltd; Jeffery & Katauskas Pty Ltd v Rickard Constructions Pty Ltd (subject to Deed of Company Arrangement)* (2009) 239 CLR 75.

[127] Thus in *Gore v Justice Corporation* (2002) 119 FCR 429 a commercial funder was ordered to pay the costs of a successful defendant. Rule 42.3(2)(c) of the Uniform Civil Procedure Rules 2005 (NSW) which previously insulated litigation funders from adverse costs and which was considered by the High Court in *Jeffery & Katauskas Pty Ltd v SST Consulting Pty Ltd* (2009) 239 CLR 75 has since been repealed.

[128] In *Wepar Nominees Pty Ltd v Schofield (No 2)* [2014] FCA 225, para 46, for example, the funder required the lead plaintiffs to pay the premium for insurance against adverse costs orders which the funder had agreed to indemnify.

[129] Security for costs was ordered against the class representatives in *De Jong v Carnival PLC* [2016] NSWSC 347 and *Madgwick v Kelly* (2013) 212 FCR 1.

[130] See *Green (as liquidator of Arimco Mining Pty Ltd) v CGU Insurance Ltd* (2008) 67 ACSR 105, para 51 (per Hodgson JA) and para 88 (per Campbell JA) suggesting that the presence of a litigation funder may make a court readier to award security for costs.

[131] Department for Business Innovation and Skills, above n 4, paras 5.30-5.32.

[132] Ibid. For a discussion of the potential conflicts that may arise please see further, JC Coffee Jr, above n 8, 136-149.

[133] There is one caveat to this conclusion. *Competition Act 1998* (UK), s 47C(8) makes damages based agreements unenforceable with respect to 'opt out' proceedings. The *Courts and Legal Services Act 1990*, s 58AA(3) definition of a damages based agreement may be broad enough to include litigation funding as it is not exclusively limited to legal services. The query would be whether s 59B which addresses litigation funding and which was inserted in 1999 but never brought into force suggests that litigation funding is excluded from the definition of a 'damages based agreement'. See however, Civil Justice Council, above n 86, sec 10 and R

Nonetheless, there is one important difference between the United Kingdom's CAT regime and Australia's class action framework. In Australia, standing for class representatives is generally limited to those with an interest in the proceedings.[134] As a result it is not possible for representative associations to initiate class proceedings unless, as explained above, there are statutes that confer on them standing with respect to the substantive claims in question. By contrast, while assignment of claims to SPVs does not seem possible, the CAT regime does envisage the formation of an SPV or foundation to act as a class representative.[135] In determining whether authorisation to act as class representative will be granted to such a body the CAT must consider the antecedents of the association/SPV (for example is it pre-existing and formed for a purpose that includes the promotion of class interests), its ability to effectively manage the proceedings and govern the class, and whether there is any conflict of interest between the proposed representative and the class members.[136] Given the latter criterion, it seems unlikely that a third party funder or law firm using an SPV will be able to act as a class representative and through that mechanism ensure that its funding commission or success fee is secured against class proceeds. First, the CAT has indicated that it will be reluctant to authorise such an SPV as the "potential conflict between the interests of a law firm or third party funder and the interests of the class member may mean that such a body is unsuitable to act as a class representative".[137]

Second, *Competition Act 1998*, s 47C(6) makes it clear that payments to class representatives in respect of the costs they have incurred can only be made from unclaimed damages. Enacting s 47C(6) consequently reflects a legislative intention to reject any US style common fund approach that would allow funders and law firms to extract success fees and commissions from the class compensation fund,[138] except to the extent that the CAT chooses to do so on a discretionary basis from an indeterminate amount of unclaimed compensation.[139] It may also contradict the principle of full recovery for victims of breach of competition law encapsulated within the EU Directive on Damages for Breach of Competition Law.[140] Thus, while theoretically funders and law firms can initiate and control opt-out class proceedings through the use of SPVs, the inability to secure certainty regarding their return on investment if the claim is successful and the CAT's likely antipathy toward them combine to make this a highly unlikely scenario.

In light of Australian developments, the likelihood of funder involvement by way of a contractual arrangement with a pre-existing association that can easily establish its class representative credentials or a contractual arrangement direct with claims holders as an alternative is examined further below.

### B. Emergence of commercial litigation funders in Australia's class actions

As noted previously, prior to the High Court of Australia's decision in *Fostif Pty Ltd v Campbells Cash & Carry Pty Ltd,*[141] which found that litigation funding of class actions did not constitute an abuse of process, the number of class actions instigated in Australia's Federal Court had been

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Mulheron, "England's Unique Approach to the Self-Regulation of Third Party Funding: A Critical Analysis of Recent Developments" (2014) 73 *Cambridge Law Journal* 570, 590-596.

[134] *Federal Court of Australia Act 1976* (Cth), s 33D.

[135] *Competition Appeal Tribunal Rules 2015*, R 78.

[136] *Competition Appeal Tribunal Rules 2015*, R 78(2).

[137] Competition Appeal Tribunal, *Guide to Proceedings* (2015), para 6.30.

[138] Higgins & Zuckerman, above n 6, 13.

[139] Mulheron, above n 6, 310.

[140] Directive 2014/104/EU of the European Parliament and Council on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union, Art 3. See Mulheron, above n 6, 310. However see contrary Higgins, above n 6, 462

[141] (2006) 229 CLR 386.

declining.[142] The decline coincided with increases in legal fees,[143] expert fees[144] and court fees,[145] as well as a substantial increase in litigation risk due to growing legal and procedural complexity and an upsurge in the number of expensive and delay inducing interlocutory skirmishes.[146] Despite the dire predictions of some commentators,[147] while the advent of litigation funding in Australia signaled the end of the decline, it did not lead to "an avalanche" [148] of new class action claims. In the first 12 years of the operation of the Part IVA regime, a total of 189 class actions were filed in the Federal Court.[149] In this period, the involvement of litigation funders in federal class action litigation was limited to a subsidiary of IMF Bentham Ltd providing financial support to the lead plaintiffs in the final stages of two Part IVA proceedings.[150] In the next 12 years, despite the extensive involvement of litigation funders the total number of Part IVA proceedings decreased to 181.[151]

IMF Bentham Ltd was an early leader in the Australian litigation finance market. As noted above, its involvement in Australian class proceedings began in December 2001 when, through one of its subsidiaries, it provided greatly-required funding with respect to two existing Part IVA proceedings that had been filed in 1998 and 2000 with respect to the so-called Waterfront industrial dispute.[152] The next Part IVA proceeding that IMF Bentham Ltd supported was the *Aristocrat* shareholder action which was filed in March 2004. IMF Bentham Ltd remains the principal provider of finance for Australian class actions and between 2010 and 2014 underwrote 54 per cent of all funded Australian class actions.[153]

Together with other smaller domestic players, a variety of off shore funders have also entered the Australian class action market including International Litigation Funding Partners Pte Ltd (based in Singapore), Harbour (based in the United Kingdom and Hong Kong) and Comprehensive Legal

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[142] V Morabito, *Litigation Funders, Competing Class Actions, Opt Out Rates, Victorian Class Actions and Class Representatives* (An Empirical Study of Australia's Class Action Regimes; Second Report; September 2010), 13-14.

[143] According to Australian Bureau of Statistics figures, in 2001-2002, the Australian legal profession generated $10.6 billion and provided average returns to barristers of $206,900 per annum. In 2007-2008, the legal profession generated $18 billion in income and barristers earned on average $271,300 per person employed. See further, Australian Bureau of Statistics, *Legal Services in Australia, 2007-2008* available at http://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/8667.02007-08?OpenDocument [accessed 22 February 2016].

[144] For example in 2005 increasing costs associated with the inefficient use of expert witnesses in litigation led to recommendations by the New South Wales Law Reform Commission that the court control expert evidence, expert witnesses should only be used when reasonably required, a single expert engaged by the court or parties is desirable, and more experts can be used in the interests of fairness but no more than is necessary: New South Wales Law Reform Commission, *Expert Evidence* (Report 109; 2005). Similar recommendations were made by the Victorian Law Reform Commission, *Civil Justice Review* (Report 14; 2007), ch 7.

[145] According to the Australian Productivity Commission, *Report on Government Services* (2008), Table 7A-16, in 2006-2007 real average civil court fees per lodgement in the Supreme and Federal Courts was $1,298. The Australian Productivity Commission *Report on Government Services* (2002), Table 9A.18 found that average civil court fees per lodgement in the Supreme and Federal Courts in 2000-2001 was $921.

[146] Recognition on the part of the Federal Court itself, of the existence of this problem, is furnished by the Court's release in July 2010 of a practice note on Part IVA. This practice note explained that one of its two aims was to ensure "that the issues that are in contest are exposed at an early date and that representative proceedings are not unnecessarily delayed by interlocutory disputes": Federal Court of Australia, *Practice Note CM 17* - Representative Proceedings Commenced under Part IVA of the *Federal Court of Australia Act 1976* (Cth), para 1.3(b).

[147] See, for instance, Norton Rose Fullbright "Class action tsunami on the horizon" *Lexocology*, 29 July 2010; and B Baxt, "Opening the Litigation Floodgates" *Company Director Magazine* (1 October 2006).

[148] Chief Justice Allsop, "Class Actions", Keynote address at Law Council seminar, Sydney, 13 October 2016, 4.

[149] Morabito, Fourth Report, above n 11, 2.

[150] V Morabito, Second Report, above n 142, 37.

[151] Morabito, Fourth Report, above n 11, 2.

[152] Morabito & Waye, NZLR, above n 124, 340.

[153] Allens Linklaters, *Class Actions: A Ten Year Survey* (May 2015).

Funding LLC (based in the United States). More recently a number of new domestic funders have also been established including the International Justice Fund[154] and JustKapital Litigation Partners.[155] A total of 18 commercial litigation funders have provided funding to lead plaintiffs in Part IVA proceedings filed during the review period. Nonetheless given the dominance of IMF Bentham Ltd it remains difficult to gauge whether the market is competitive. Commentators have noticed, for example, that despite the entry of new players, litigation funding commissions have remained stable at around 30 per cent.[156]

### C. Regulation of litigation funders

It is relatively easy for either a domestic or a foreign litigation funder to establish itself in the Australian class action finance market as regulatory requirements are minimal. Litigation funders are exempt from Australia's financial and consumer credit regulations provided they satisfactorily demonstrate that they manage conflicts of interest between themselves, class members and the class law firm.[157] ASIC has issued a Regulatory Guide stipulating how funders can comply with this obligation.[158] These include the establishment of procedures to identify, assess and address potential conflicts of interest, compliance monitoring of those procedures by senior managers, and written disclosure of potential conflicts of interest to all class members.

The Regulatory Guide also recommends that funding agreements should incorporate a "cooling off period",[159] a clause providing that class members' instructions to the class law firm will prevail in the event of a conflict of interest between the funder and class members,[160] and make provision for full disclosure of the contents of the agreement between the funder and lawyers as well as the terms of any proposed settlement.[161] The emphasis of the Regulatory Guide is thus on the processes around conflict management and disclosure rather than on substantive matters such as the size of the litigation funder's commission, interest charged, ancillary fees, or the degree of control the funder exercises over the conduct of proceedings.

Given that disclosing conflicts of interest rarely enhances rational consumer decision making and that disclosure may in fact lull consumers into a false sense of security,[162] questions must therefore be raised about the value of these ASIC safeguards. All the same, there have been no reports of consumer dissatisfaction with litigation financing arrangements of the kind raised against claims management companies in the United Kingdom.[163] Rather, Australian consumers seem quite happy that litigation funders provide an avenue for redress that would otherwise be unavailable to them.

Although litigation funders also remain statutorily unregulated in the United Kingdom,[164] permissible litigation funding of collective redress in the United Kingdom is currently limited to business to

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[154] http://internationaljusticefund.com.au/#
[155] http://www.justkapital.com.au/.
[156] US Chamber Institute for Reform, above n 125.
[157] *Corporations Regulations 2001* (Cth), Regs 5C.11.01; 7.1.04N; 7.1.06 (2A); 7.1.06 (2B); 7.6.01AB; 7.8.26; 7.9.98A.
[158] ASIC, Regulatory Guide 248, *Litigation Schemes and Proof of Debt Schemes: Managing Conflicts of Interest* (2013).
[159] Ibid RG248.71(b).
[160] Ibid RG248.71(c).
[161] Ibid RG248.71(e) & (g).
[162] See, for instance, DM Cain, G Loewenstein & DA Moore, "When Sunlight Fails to Disinfect: Understanding the Perverse Effects of Disclosing Conflicts of Interest" (2011) 37(5) *Journal of Consumer Research* 836; N Chater, S Huck & R Inderst, *Consumer Decision-Making in Retail Investment Services: A Behavioural Economics Perspective, Final Report* (European Commission, 2010).
[163] See J Spencer, "An unethical personal injury sector" [2014] *Journal of Personal Injury Law* 226.
[164] The Association of Litigation Funders of England and Wales implements a self-regulatory Code of Conduct for Litigation Funders, which has been recognised as sufficient by Lord Justice Jackson, *Review of Civil*

business claims unless the funder obtains a licence under the *Consumer Credit Act 1974*.[165] Firms providing consumers with "financial accommodation" must be authorised by the Financial Conduct Authority unless an exemption or exclusion applies.[166] Pertinent exemptions apply to business loans in excess of £25,000[167] or loans exceeding £60,260 where the borrower is a high net worth individual.[168] To date, the high level authorisation requirements under the consumer credit regime, including onerous prudential obligations, requirements related to employee training, the provision of mandatory information, systems and control rules, and creditworthiness assessment have discouraged commercial funders from engaging with consumers. Accordingly, in the United Kingdom, where funders are involved in opt-out proceedings involving large numbers of consumers it is much more likely that they will enter into a funding arrangement with the SPV or association that has been authorised to act as the class representative rather than directly with consumers themselves. Entry into contractual arrangements with representative associations will also reduce barriers to CAT approval that might otherwise be faced by funder controlled SPVs.

### D. Wider impact of litigation funders

As well as being a leading player in the financing of class actions, IMF Bentham Ltd has also acted as an important driver of jurisprudence regarding mechanisms to support the growth and profitability of class action financing in addition to being a driver of substantive law employed in class actions such as the *Sons of Gwalia* decision which, via misleading and deceptive conduct remedies, turned shareholders into ordinary creditors.[169] Initially IMF Bentham Ltd was wary of "opt out" class actions and preferred to fund traditional multi-plaintiff or representative proceedings. This wariness was based on the fear that the value of its investment would be undermined by "free riders" who did not enter funding agreements and contribute to the cost of conducting the class action.[170]

In the *Aristocrat* proceedings, the membership of the class was restricted to persons who had entered a retainer agreement with the solicitors on file, Maurice Blackburn. A term of the retainer agreement, in turn, imposed the requirement that the class members also enter into a funding agreement with Insolvency Litigation Fund Pty Ltd (a wholly-owned subsidiary of IMF Bentham Ltd). Justice Stone found that this arrangement subverted the "opt out" principle underpinning Part IVA; thus, the proceeding could not continue as a Part IVA proceeding as long as this restriction remained in the description of the represented group.[171] As a result, this proceeding was turned into an open class proceeding; that is, it was brought on behalf of all relevant shareholders. Because a large number of high value claimants had already entered into the retainer and funding agreements, the matter proceeded to settlement despite Stone J's ruling.[172]

As we noted previously, a few years later in *Multiplex Funds Management Ltd v P Dawson Nominees Pty Ltd*,[173] another matter funded by a predecessor company of IMF Bentham Ltd, the Full Federal

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*Litigation Costs* (Final Report; 2010), para 2.4. Among other things, the Code provides that the funder must be appropriately capitalized, maintain client confidentiality and not engage in misleading and deceptive conduct.

[165] See further *Conister Trust Ltd v John Hardman & Co* [2008] EWCA Civ 841, [2008] All ER (D) 273 - non recourse loan to fund legal expenses insurance and disbursements held to fall within the *Consumer Credit Act 1974.*

[166] *Consumer Credit Act 1974*, s 21.

[167] *Financial Services and Markets Act 2000 (Regulated Activities) Order*, Art 60C.

[168] *Financial Services and Markets Act 2000 (Regulated Activities) Order*, Art 60H; Financial Conduct Authority, Perimeters Guidance Manual, 2.7.19J G.

[169] *Sons of Gwalia Ltd v Margaretic* (2007) 231 CLR 160. This decision was later overturned by legislative provision: *Corporations Act 2001* (Cth), s 563A(2).

[170] J Walker, S Khouri & W Attrill, "Funding Criteria for Class Actions" (2009) 32 *University of New South Wales Law Journal* 1036, 1037-1038.

[171] *Dorajay Pty Limited v Aristocrat Leisure Limited* (2005) 147 FCR 394.

[172] The total value of this settlement was $144.5 million: *Dorajay Pty Ltd v Aristocrat Leisure Limited* [2009] FCA 19, paras 12 & 30 (per Stone J).

[173] (2007) 164 FCR 275.

Court upheld the "closed class" device that shut out free riders from enjoying the fruits of the class claim unless they entered into both retainer and funding agreements. The decision paved the way for IMF Bentham Ltd to expand its financing of class actions and encouraged others to follow suit. The result is that closed classes have been employed in approximately 58 per cent of all the Part IVA proceedings filed during the review period which were supported by litigation funders. There have also been several instances of competing class actions filed with respect to the same legal disputes by different lawyers supported by different litigation funders.[174]

In conjunction with class law firms, other funders have also been proactive in attempting to persuade Australian courts to adopt measures to minimise free rider risk. In *Pathway Investments Pty Ltd v National Australia Bank Ltd (No. 3)*[175] and *Farey v National Australia Bank*[176] orders were made during settlement approval to deduct from unfunded class members' compensation amounts equivalent to what would have been paid by class members if they had entered into funding agreements. Other courts have preferred equalisation orders where a deduction of the funder's commission is made from each non-funded class member, added to the total compensation pool and then distributed pro rata to all class members (funded and unfunded).[177] These measures are intended to prevent non-funded members from receiving a windfall at the expense of funded members, but concerns have been raised by some that such orders undermine the consensual nature of funding agreements.[178] Paradoxically, no such concerns arise regarding the distribution of legal costs among all group members irrespective of signing a retainer with the class law firm.[179]

For analogous reasons and in the absence of legislative imprimatur, in August 2015 Justice Wigney of the Federal Court was not prepared to go as far as Canadian courts and adopt a common fund approach to spreading the cost of litigation financing across all class members at the commencement of class proceedings.[180] But fourteen months later, in *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Ltd*, the Full Federal Court made a common fund order which required all class members (and not just those class members who had entered into a litigation funding agreement with the litigation funder) "to pay the same pro rata share of legal costs and the funding commission from the common fund of any amount they receive in settlement or judgment in the case".[181] At the same time, the Full Court declined to set the funding commission rate as it believed that it was preferable to leave judicial approval of this rate at a later stage when more complete and probative information will be available to the Court.[182]

The Full Court explained that common fund orders would produce a number of significant benefits in funded class actions. These benefits include a greater protection of the interests of class members, through judicial oversight of the funding commissions charged by litigation funders, and providing access to justice to a greater number of claimants by encouraging the use of open, rather than closed, class devices in funded class actions.[183] The Full Federal Court also believed that this encouragement of the open class device would result in a reduction in the number of competing class actions and in the potential for conflicts of interest between the class representative's solicitors and unfunded non-client class members and between funded registered class members and unfunded class members.[184]

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[174] See Morabito, Connecticut, above n 76, 276-277 & 290-296.
[175] [2012] VSC 625.
[176] [2014] FCA 1242.
[177] *Modtech Engineering Pty Ltd v GPT Management Holdings Ltd* [2013] FCA 626, para 57 (per Gordon J).
[178] US Chamber Institute for Reform, above n 125, 22-29.
[179] *Modtech Engineering Pty Ltd v GPT Management Holdings Ltd* [2013] FCA 626, para 24 (per Gordon J).
[180] *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers and Managers Appointed) (In Liq)* (2015) 325 ALR 539.
[181] [2016] FCAFC 148, para 8 (per Murphy, Gleeson and Beach JJ).
[182] Ibid paras 11, 35, 67 and 79.
[183] Ibid paras 11, 14, 79, 167, 193 and 205.
[184] Ibid paras 14, 196-199 and 205.

It is too early to tell whether the benefits expected by the Full Federal Court will eventuate.[185] A similar conclusion applies with respect to the accuracy of the predictions made by several commentators and class actions lawyers that *Money Max* will generate a number of highly undesirable scenarios.[186] What can be stated with some certainty is that, if there is in fact an increase in the percentage of funded federal class actions that employ open classes, it will not result in a dramatic change in the federal class action landscape. This is because in the three years ending on 25 October 2016 - the day before the *Money Max* judgment was delivered by the Full Court - only one-third of all funded Part IVA proceedings were closed class proceedings.

Conversely, at least insofar as damages awards are concerned, the common fund approach seems doomed to failure in the United Kingdom. As we have already indicated, *Competition Act 1998*, s 47C(6) reflects a legislative intention to prohibit class representatives from passing on their funding costs or solicitor success premiums to class members when a damages award is made except to the extent that these can be recovered from unclaimed damages. All that the Court may do is make a costs order for or against the representative party, thus enabling it to recover its party-party costs.[187] Moreover, that the CAT is expressly empowered to approve the terms of a collective settlement as to the payment of costs, fees and disbursements[188] yet such a power is absent regarding the award of damages is telling. Presumably such a power is broad enough to incorporate the payment of a funder's fee independent of class damages and approved by the CAT as part of its power to determine whether the settlement is just and reasonable. Outside of settlement therefore, it is unlikely that any other general power might be used to order payment of funder commissions.

All of the above suggests that, subject to the requirements of the *Consumer Credit Act 1974*, funding agreements will have to be enforced independently of assistance from the CAT as private contracts with individual claimholders or with the class representative. As it happens, this is actually what occurred in Australia apropos class members until recently. Although reference was made to funding agreements by Australian courts from time to time, they were not approved by Australian courts during the initial stages of the class proceeding nor during settlement approval. But the Full Federal Court's adoption of the common fund approach in October 2016 means that commercial litigation funders can now seek, at the outset of the class action, the approval of the Court. And, as a result of the November 2016 ruling by Justice Murphy of the Federal Court in *Earglow Pty Ltd v Newcrest Mining Limited*, the following principle applies with respect to the judicial review of class action settlements:

> if in a settlement approval the Court considers the proposed settlement is fair and reasonable except that the funding commission is excessive or exorbitant, the Court has power to approve the settlement and reduce the funding commission to be deducted pursuant to the terms of the settlement.[189]

A significant aspect of *Earglow* is that in determining the reasonableness of the funding commission, proposed in the settlement agreement pursuant to the funding equalisation technique, Justice Murphy applied the factors that were suggested by the Full Federal Court in *Money Max* in another context, namely, with respect to the determination of the funding commission pursuant to a common fund order. [190]

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[185] See generally V Waye and V Morabito, "When pragmatism leads to unintended consequences: a critique of Australia's unique closed class regime" (2017) 18 *Theoretical Inquiries in Law* (forthcoming). It is interesting to note though that only 25 per cent of the post-*Money Max* funded Part IVA proceedings filed before the end of 2016 were open class proceedings.

[186] See generally Justice Murphy and V Morabito, "The First 25 Years: has the Class Action Regime Hit the Mark on Access to Justice?" in D Grave and H Mould (eds), *25 Years of Class Actions in Australia* (Ross Parsons Centre of Commercial, Corporate and Taxation Law; 2017), ch 3.

[187] *Competition Appeal Tribunal Rules 2015*, R 98.

[188] *Competition Appeal Tribunal Rules*, R 94(9) (a); 97(7)(a).

[189] [2016] FCA 1433, para 157 (per Murphy J).

[190] Ibid paras 162 - 198.

As noted previously, the ability of SPVs and foundations to initiate opt-out proceedings provides a point of difference between Australia and the United Kingdom. It may be possible for a funder to enter a contractual agreement with an association or SPV, and if the association or SPV is able to secure a favourable settlement for them to recoup their funding costs as part of the settlement terms. From the funder's perspective this arrangement would reduce the cost of recruiting individual claimholders and facilitate the sharing of such costs with the association/SPV. Unfortunately, however, if the proceedings result in a damages award as we noted above it appears that the association/SPV will not be able to pass these costs onto class members except out of unclaimed damages.

As Higgins argues, such an arrangement immediately creates a conflict of interest between the association/SPV and class members arising out of the association/SPV's need to discourage as much claiming from the fund as possible.[191] However, arguably this conflict could be easily solved if class members entered into a separate agreement with their association/SPV to pay the association/SPV equivalent to a pro rata proportion of the funder's fees if their claims are successfully resolved, which, in turn, could be subject to a charge in favour of the funder. While this tripartite arrangement may simply transfer recruitment costs from the funder to the association, if the association is a pre-existing one with purposes that align with class members' interests, it may be cheaper and easier for the association to undertake recruitment. Moreover, taking a leaf from group buying websites, it may be possible for the association to garner member commitment to participation in a non-recourse class action scheme on the condition that a critical mass of members are recruited. On the other hand, a funder with no pre-existing relationship with class members may find it comparatively difficult to credibly represent itself to them.

IMF Bentham Ltd's portfolio of class action investments and the portfolios of other Australian class action financiers are still dominated by shareholder and investor actions, which comprise approximately 76 per cent of all funded Part IVA proceedings filed during the review period.[192] More recently IMF Bentham Ltd and other funders have expanded into claims for property and economic loss against utility suppliers arising from their role in natural disasters such as flooding and bushfires. All of these actions followed on from public inquiries that investigated the causes of the disasters and the part played by the utility suppliers. Many of the reasons why litigation funders favour these types of proceedings have been canvassed elsewhere.[193] The participation of large scale institutional investors that create scale and off-set free rider risk is another factor that encourages litigation funders to invest in securities claims. As a result, funders offer large scale claimholders smaller commissions to attract them to the class and thus make the class action as a whole financially feasible. The practice of discounting commissions for large scale claim holders has passed the courts without comment,[194] presumably on the basis that the judiciary accepts that smaller claims are more costly to administer.

Clearly, preferences for investor proceedings will have important implications for the efficacy of private forms of collective redress, which in the United Kingdom and Australia are now heavily reliant upon litigation financing, altruistic organisations, or law firms of sufficient scale and breadth to bear the substantial litigation risk inherent in class proceedings. Funders' penchant for investor

[191] Higgins, above n 6, 461.
[192] Morabito, Fourth Report, above n 11, 9.
[193] See, for instance, S Issacharoff, "Litigation Funding and the Problem of Agency Cost in Representative Actions" (2014) 63 *DePaul Law Review* 561, 574 - arguing that litigation funders find it difficult to address the moral hazard associated with long term physical injury claims and Walker *et al*, above n 170, 1053, noting the ease of quantifying loss in securities and property and economic loss matters. See also M Papadakis, "Class action litigation, corporate suits set to surge", *Australian Financial Review*, 4 January 2016.
[194] See, for instance, *Modtech Engineering Pty Ltd v GPT Management Holdings* [2013] FCA 626, para 20 (per Gordon J); *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* (2015) 325 ALR 539, para 45 (per Wigney J).

matters significantly narrows access to justice for consumers and businesses with small individual claims that fall outside of this category.

### E. Competition class actions

To date there have only been five competition class actions in Australia and the last of these proceedings was filed back in September 2007.[195] Only one of these proceedings has involved a funder. In the Air Cargo Cartel case, IMF Bentham Ltd provided an indemnity for costs including security for costs, and paid all legal disbursements, but did not underwrite the class action law firm's legal fees.[196]

However, whether this constitutes a warning that the Australian litigation funding model is a poor fit for competition law matters elsewhere is debatable. Arguably, the negligible number of funded competition actions reflects difficulties peculiar to the Australian competition law framework. A recent review of Australia's competition laws found that they were unnecessarily complex and therefore difficult to enforce, and that they did not have sufficient extraterritorial reach.[197] Further, the review found that the current competition provisions impeded private follow on actions for loss arising from contravening conduct because there was a great deal of uncertainty as to whether private parties could access and adduce evidence collected by the ACCC [198] The review therefore recommended that Australia's competition laws should be simplified and that private parties should be allowed to adduce evidence of admissions made to the regulator.

Apart from difficulties accessing evidence collected by the ACCC, IMF Bentham Ltd has raised two further impediments to litigation funding of competition class actions that may apply in the United Kingdom. [199] The first relates to class dispersion. Class members in investor class actions are comparatively easier to identify and recruit than persons who might have been harmed by anti-competitive conduct, which in theory could extend to every consumer and business in Australia. In these circumstances, many of the consumer and small business claims would be for very low amounts that would be proportionately quite costly to administer. For this reason, the class in the Air Cargo Cartel case was limited to persons who spent more than $20,000 on air freight.[200] The onerous authorisation requirements imposed by the Financial Conduct Authority pursuant to the *Consumer Credit Act 1974* discussed earlier provide an even stronger reason why commercial funding of competition class actions will be constrained to sizeable claims pursued by business in the United Kingdom or with large scale consumer representative associations.

Secondly, the extent of the harm that the consumers and businesses affected by anti-competitive conduct suffer is also much more variable than the extent of harm suffered in securities matters, which is usually determined by relatively simple mathematical formula that relate to the duration and size of a constrained set of investment transactions. Cartel conduct, on the other hand, is likely to involve many different types of transactions that occur in various contexts over a lengthy period of time, generating the need for extensive and expensive economic modelling and the collection of vast

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[195] Morabito, Fourth Report, above n 11, 11.
[196] Morabito, Second Report above n 142, 39. This Part IVA proceeding was settled for $38 million: *De Brett Seafood Pty Ltd v Qantas Airways Ltd (No 7)* [2015] FCA 979.
[197] Australia, *Competition Policy Review: Final Report*, 2015 available at http://competitionpolicyreview.gov.au/final-report/ [accessed 25 February 2016].
[198] Ibid, Part 2, Findings and Recommendations. See also R Gilsenan, "Could the Harper Review recommendations revive private enforcement of cartel prohibitions?" (2016) 24 *Australian Journal of Competition and Consumer Law* 6.
[199] Walker *et al*, above n 170, 1050 - 1053.
[200] Ibid 1051. In the Netherlands the Air Cargo case funded by CFE; CFE advises that it will only accept assignments for claims involving more than €1million in air freight. See European Air Cargo Cartel available at http://claimsfundingeurope.eu/projects/project-air-argo-artel/ [accessed 25 February 2016].

amounts of data from the relevant markets.[201] As a result, IMF Bentham Ltd advises that it is reluctant to fund competition class actions unless the claims appear to be strong.[202]

### F. Outcomes of funded class actions

The success rate of completed federal class actions funded by litigation funders is approximately 90 per cent. Funded class actions also generally result in higher settlements than non-funded actions. Mean and median settlements for all Part IVA proceedings settled before the end of 2016 appear below.

*Non-funded class actions*
Mean gross settlement fund = $16,987,659.
Median gross settlement fund = $3,100,000.

*Funded class actions*
Mean gross settlement fund = $48,218,333.
Median gross settlement fund = $38,500,000.

The figures above echo the nature and size of class actions that attract litigation funders rather than any inherent capacity to secure a better return for claim holders, but also demonstrate that the extensive due diligence undertaken by funders prior to underwriting proceedings[203] pays off as the difference between the mean and median gross settlements indicates that there are few overly cheap settlements. One would expect a much larger gap between average and median gross settlements if there were a substantial number of low ball settlements.[204]

Even so, there is no doubt that the transaction costs associated with litigation funded class actions are high compared to the transaction costs associated with mass dispute settlement schemes instigated by regulators or by external dispute resolution bodies.[205] The average proportion of settlement funds secured in funded Part IVA proceedings, destined for class members, is approximately 58 per cent. This compares poorly with data from the US. In a study of recoveries and fees between 1993 and 2008 conducted by Eisenberg and Miller, it was found that class action attorneys working on a contingency fee basis have a mean fee to recovery ratio of 23 per cent, with a substantial scale effect that saw the mean fee to recovery ratio drop to 12 per cent for class actions where total claims exceeded $175 million.[206]

However, American class action lead plaintiffs and attorneys are not usually subject to the risk of adverse costs, which in Australian class actions can range beyond $10 million. Despite the lack of vigorous competition in the litigation funding market, the large exposure of funders to such adverse costs has led to a consensus among the courts and policy makers that the commissions charged by funders are appropriate.[207] Consequently, notwithstanding that private class actions incur high transactions costs and that funded private actions incur even higher transaction costs, the general view in Australia is that such vehicles are essential to augment and strengthen regulatory action, provide

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[201] *Bray v F Hoffman-La Roche* [2003] FCA 1505, para 8 (per Merkel J) explaining how difficult it was to ascertain the link between complex and long lasting cartel behaviour and the range of transactions, products and consumers involved.
[202] Walker *et al*, above n 170, 1053.
[203] Ibid.
[204] See A Bryman, *Social Research Methods* (Oxford University Press; 2016), 338
[205] Waye & Morabito, JCLS, above n 34.
[206] T Eisenberg & GP Miller, *Attorneys' Fees and Expenses in Class Action Settlements: 1993-2008* (October 30, 2009). NYU Law and Economics Research Paper No. 09-50; Cornell Legal Studies Research Paper No. 1497224, at pp 11 - 12. Available at SSRN: http://ssrn.com/abstract=1497224 or http://dx.doi.org/10.2139/ssrn.1497224 [accessed 26 February 2016].
[207] See, for instance, *ASIC v Richards* [2013] FCAFC 89, para 52 (per Jacobson, Middleton & Gordon JJ); Australian Productivity Commission, above n 17, 635.

consumers with more compensation than they would otherwise receive, and ensure strong deterrence against harmful activity.[208]

## VI. CONCLUSION

The analysis provided in this article of the funding strategies that Australian lead plaintiffs have implemented in order to avail themselves of the federal class action regime has revealed the great difficulties that they have confronted as a result of the desire, on the part of the drafters of this regime, to demonstrate to the public (and class action opponents in particular) that their regime would not produce the same problems that in the US have been attributed, by some commentators, to their class action regimes. Unfortunately, this (legitimate) desire on their part made them reject the mechanisms that the ALRC recommended in order to overcome the significant barriers that are faced by claimants desiring to seek relief on behalf of groups of similarly-situated claimants. Class representatives were not provided with any satisfactory sources of funding. As a result, a number of class actions have been run without adequate resources and/or adequate legal representation. Some of the "victims" of this state of affairs have included those who were intended to be among the main beneficiaries of the class action procedure, namely, vulnerable and disadvantaged persons.

It has also been shown that the subsequent legislative authorisation, at the state level, of conditional costs agreements and the extensive involvement of commercial litigation funders over the last fifteen years or so have not completely addressed this problem. These developments have created their own problems, such as the exclusion from class action litigation of claimants who are unwilling or unable to execute agreements regarding the funding of the litigation. But we have also seen that commercial litigation funders have recently persuaded the Full Federal Court to introduce a common fund mechanism, inspired by North American regimes, not unlike that recommended by the ALRC to determine the remuneration of the solicitors acting for lead plaintiffs. This is part of a recent recognition, on the part of the Federal Court, of the need to ensure (a) that the interests of class members are protected in funded class actions; and (b) that funded class actions provide access to justice to as many claimants as possible.

Given that similar fears regarding unbridled US style class actions have also created significant constraints on funding in the United Kingdom's CAT opt out proceedings, we predict that like Australia's federal class action regime the United Kingdom regime will be dominated by few law firms and even fewer funders. As a result of uncertainties regarding financiers' return on investment, instead the CAT regime appears to favour representative associations but largely those acting on an altruistic basis. Previous experience in the United Kingdom demonstrates that, while this may avoid some of the difficulties that have arisen with Australia's system of closed classes, only a small number of opt out proceedings are likely to be instigated.

[208] Australian Productivity Commission above n 17, 607, 623-624.