Ai GROUP SUBMISSION

Parliamentary Joint Committee on Corporations and Financial Services

Corporations Amendment (Improving Outcomes for Litigation Funding Participants) Bill 2021

5 November 2021

Introduction

The Australian Industry Group (**Ai Group**) welcomes the opportunity to make a submission on the *Corporations Amendment (Improving Outcomes for Litigation Funding Participants) Bill 2021* (**Litigation Funding Bill**).

Ai Group and our members have a significant interest in the proposed reforms. Businesses are being targeted in a class action boom that is being driven by litigation funding firms that are pursuing excessive profits at the expense of businesses, plaintiffs and the broader community.

Insurance costs for businesses, driven by the large increase in class actions in Australia, have risen by up to 600 per cent.[1]

Those opposing reforms to class action and litigation funding laws often dress up their arguments with liberal references to access to justice in order to take the focus off the excessive profits that they are earning from class actions. Implementing carefully considered changes to class action laws to achieve a fairer outcome for plaintiffs and businesses, will not impede access to justice. The current laws are only operating in the interests of litigation funders and the law firms they are partnering with.

A recent Australian Law Reform Commission report on class actions proceedings and third-party litigation funders reported that in cases involving litigation funders, the median return to plaintiffs was only 51 per cent of the amount awarded, while in cases not involving litigation funders, the median return to plaintiffs was 85 per cent.[2]

Class actions have a genuine role to play in ensuring that where a large number of parties have suffered common harm or damage, they are properly compensated. However, the current poorly regulated system is allowing litigation funders to take a disproportionate share of any award or settlement.

The Litigation Funding Bill is based on an earlier draft *Treasury Laws Amendment (Measures for Consultation) Bill 2021* which was the subject of a round of consultation in October 2021. Many of the points raised in this submission were made in our submission of 6 October 2021 in support of that Bill and its associated Regulations.

In addition, Ai Group has made the following submissions calling for reforms to class action and litigation funding laws:

- Ai Group submission to the Parliamentary Joint Committee's Inquiry into Litigation Funding and the Regulation of the Class Action Industry (**PJC Inquiry**) (15 June 2020).

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[1] Submission of Marsh to the PJC Inquiry, 11 June 2020.

[2] Australian Law Reform Commission, *Integrity, Fairness and Efficiency—An Inquiry into Class Action Proceedings and Third-Party Litigation Funders* (Final Report), December 2018. Published in Parliament on 24 January 2019.

- Ai Group submission responding to the Consultation Paper: *Guaranteeing a minimum return of class action proceeds to class members*, prepared by the Treasury and the Attorney-General's Department (28 June 2021).

- Ai Group submission on the proposals in Consultation Paper 345 – *Litigation Funding Schemes: Guidance and Relief*, published by the Australian Securities and Investments Commission (20 August 2021).

By effecting targeted reforms to implement a number of important recommendations of the PJC Inquiry, the Litigation Funding Bill compliments necessary amendments made by the *Corporations Amendment (Litigation Funding) Regulations 2020* which require operators of litigation funding schemes to hold an Australian Financial Services Licence and subject litigation funding schemes to the managed investment scheme (**MIS**) regime in Chapter 5C of the *Corporations Act 2001* (Cth) (**Corporations Act**).

Ai Group strongly supports the Litigation Funding Bill.

Considering that the reforms are not retrospective, it is important that the Litigation Funding Bill is passed by the Australian Parliament without delay.

Class members should consent to litigation funding agreements

The Litigation Funding Bill would ensure that prospective class members are not 'railroaded' into participating in class actions without their consent. The Bill would appropriately:

- Limit the definition of a 'member' of a class action litigation funding scheme to those claimants in a class action who have agreed in writing to enter the scheme and be bound by the terms of the scheme's constitution (s. 9(b));

- Require litigation funding schemes to have a constitution which includes a claim proceeds distribution method (s. 601GA(5)(a)(ii)); and

- Ensure that funding agreements for class action litigation funding schemes are not enforceable and have no effect if the Court makes a common fund order (s. 601LF).

The availability of common fund orders encourage speculative litigation as they remove much of the expense of 'book building' and remove the risk that insufficient class members will agree to the funder's commission. There are very few other circumstances under which such significant legal rights are waived without an individual's express or implied consent.

The reforms proposed appropriately deal with the incentive for funders to sign class members up without their knowledge or understanding of their rights.

Subjecting funding agreements to the laws of Australia

The recent huge increase in foreign litigation funding firms becoming involved in Australian class actions necessitates appropriate reforms geared toward ensuring that such funders are subject to the laws in force in Australia.

The Litigation Funding Bill would ensure that litigation funding schemes are bound by a constitution which provides that each funding agreement for the scheme must:

- Include words to the effect that the agreement is subject to the law in force in a particular State or Territory (s. 601GA(5)(b)(i)); and
- Include words to the effect that the only courts in which the agreement can be enforced are the courts of the Commonwealth or the courts of a particular State or Territory (s.601GA(5)(b)(ii)).

As stated in the PJC Inquiry Final Report:[3]

> *If a foreign litigation funder seeks to profit from class action litigation in Australia, it is only appropriate that its funding arrangements are subject to, and in accordance with, Australian law. There should be no question as to the Federal Court's jurisdiction to adjudicate and resolve any issues arising from a litigation funding agreement pertaining to a class action in its own jurisdiction.*

Funders should pay the costs of litigation funding fees assessors and contradictors

There is significant benefit in ensuring that class members in funded proceedings are protected by ensuring that a Court has the benefit of an independent litigation funding fees assessor or a contradictor who assists and informs the Federal Court's assessment of the claims distribution method.

The Litigation Funding Bill would put in place appropriate protections for plaintiffs by:

- Requiring that the Court consider the report of a person appointed to inquire into and report on the fairness and reasonableness of the claims distribution method or consider the representations of a contradictor representing the scheme's members before making an order approving or varying a funding agreement for a class action litigation funding scheme, unless it is not in the interests of justice to do so (s. 601LG(6));

[3] Report of the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into litigation funding and the regulation of the class action industry, December 2020, [11.57].

- Requiring the constitution of a class action litigation funding scheme to provide that any litigation funding agreement must contain an undertaking by the litigation funder to pay the reasonable costs of the fees assessor and the contradictor (s. 601GA(5)(a)(v)).

These reforms would guarantee that, unless the circumstances otherwise provide, the Federal Court is furnished with appropriate independent information to assist it in making an appropriate order under s.601LG.

By imposing the cost of providing such assistance upon the litigation funder, a proportionate incentive is generated for the funder to moderate funding fees.

The disgraceful conduct of certain lawyers and the litigation funder involved in the Banksia class action highlights the vital role of contradictors.

In this matter, barristers Norman O'Bryan and Michael Symonds, solicitor Anthony Zita, and litigation funder Australian Funding Partners Limited were found by the Victorian Supreme Court to have engaged in "egregious conduct in connection with a fraudulent scheme" to benefit at the expense of the class action members. They deceived the Court about their fees and they went to extraordinary lengths to conceal major conflicts of interest. Their conduct only came to light after a contradictor was appointed by the Court. They have been ordered to pay $11.7 million to approximately 16,000 group members as well as in excess of $10 million in costs for the Court proceedings. O'Bryan and Symonds have been removed from the roll of barristers and Zita has been ordered to show cause why his name should not be removed from the roll of practitioners.[4]

Appropriate limitations should be imposed on litigation funders' profits

The regulatory system governing litigation funding arrangements should ensure that the class action regime is not misused as an avenue for litigation funders to make unreasonable profits at the expense of class members and businesses.

In the Final Report of its Inquiry into *Class Action Proceedings and Third-Party Litigation Funders*, the Australian Law Reform Commission analysed settlement amounts arising out of representative proceedings and compared the median proportionate return from each settlement to the law firm, third-party funder and group members from 2013 - 2018.[5] The median proportion of the settlement returned to the class was significantly lower in funded actions (51%, compared with 85% in unfunded actions). In one example included in this report, the group members received only 29% of a $6.6 million settlement and the litigation funder received 62% of the settlement.[6]

[4] *Bolitho v Banksia Securities Ltd (No 18) (remitter)* [2021] VSC 666.

[5] Australian Law Reform Commission, *Integrity, Fairness and Efficiency—An Inquiry into Class Action Proceedings and Third-Party Litigation Funders* (Final Report), December 2018, p. 83. Published in Parliament on 24 January 2019.

[6] *Farey v National Australia Bank Ltd* [2016] FCA 340.

This is not an isolated example. In May 2019, Lee J of the Federal Court criticised an agreement involving Adero which would have provided UK-based Harbour Litigation Funding with 40% of any settlement or decision or 400% of legal costs whichever was the greater.[7] Claiming that the Agreement was, "fantastic in the true sense of the word", Lee J said that the arrangement was "a real worry" and said:

> "You get to a stage where even if a 60 per cent of their claim offer was made, you would be in a situation where people are getting less than a quarter, on the analysis, of their claim.
>
> And that raises real issues about the ability for the court to regard any settlement, in these circumstances, fair and reasonable in the interests of group members."

In one case referred to the Victorian Law Reform Commission in its inquiry into litigation funding and group proceedings, once costs were paid out of the awarded amount, the plaintiffs received nothing of the proceeds.[8] The case concerned a claim made by trustees for former employees of Huon Corporation Limited against CBL Insurance Ltd. The action was initiated on behalf of 336 former employees with final orders made in May 2015. Out of the final settlement amount of $5.1 million, the litigation funder received 36% of the award.[9] Once legal fees, accounting and administrative costs and the liquidator's fee were taken out, no part of the award was available for the plaintiffs on whose behalf the action was brought.

In its submission to the Victorian Law Reform Commission inquiry, the National Union of Workers relevantly stated:

> "**'The legal system is rigged against us'**
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> The circumstances of *Laurence Andrew Fitzgerald and Michael James Humphris in their capacity as trustees for certain former employees of Huon Corporation Pty Ltd ('Huon") v CBL Insurance (formerly called Contractors Bonding Limited), Supreme Court of Victoria Proceeding No. c1-2011-5405* (hereinafter referred to as 'the subject proceedings') are well documented.
>
> The subject proceedings were part of an eleven year series of events. Our members who were only paid a part of their redundancy entitlements four years after their final payment were patiently waiting for the result of the litigation….
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> - - -
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> **Cost Breakdown**
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> **$5,107,259** were received from CBL as the ordered sum, interest and costs. This amount was dispersed as follows:
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> | LCM | $1,848,259 |
> | Piper Alderman | $1,792,000 |
> | Barristers | $885,000 |
> | Holding Redlich | $235,000 |
> | Grant Thornton | $211,000 |
> | PPB - Liquidator | $50,000 |

[7] Marin-Guzman, D., *'A real worry': Judge slams litigation funding fees* (Australian Financial Review) 30 May 2019.

[8] *Fitzgerald & Anor v CBL Insurance Ltd* [2014] VSC 493.

[9] Victorian Law Reform Commission, *Access to Justice - Litigation Funding and Group Proceedings* (Report) March 2018, p. 29.

Other Lawyers	$86,000
Total	**$5,107,259**

The actual plaintiff - the beneficiaries to the Trust who were NUW members - received no entitlement. This is in spite of the large order that was made by the court. All monies were taken by the various representatives acting ostensibly on our members behalf, in the lead up to, during and subsequent to the trial. For its part, we note that our members have not paid one dollar in membership since their formal employment separation. Nor were we ever seeking backpay of membership dues in the event of a further distribution from the trial.

We believe that this is not a good public policy outcome. Those who were clearly wronged decided to prosecute their claim in spite of all of the various tactical legal barriers put before them and won an outcome that should have meant a disbursement to them after 11 years. Our Victorian system of justice however did not produce this outcome. It is clear to us that some form of market regulation needs to occur to prevent this result from occurring again."

In a keynote address to a Class Action Conference held by litigation funder IMF Bentham, Justice Lee criticised the returns being pursued by some litigation funders. He said:[10] (emphasis added)

> **Hon Michael Lee:** It is rightly a scandal for there to be situations where group members in proceedings where there has not been a massive change in prospects since the commencement of proceedings recovering only a very very small return for their claim and in circumstances where legal costs have become extraordinarily large. And and funding commission taking on top of that means they're recovering very little. Now one hopes that you have practitioners people who a duties to the Court that makes sure make sure that that doesn't happen or seek to minimise the prospect of that happening. And one I'm sure the Court would expect that certainly senior practitioners involved in those sort of cases would be saying they're not putting things up for approval unless things change. But those sort of matters are ones that candidly the Court would expect to see put before it on a settlement approval.

As stated in the PJC Inquiry Final Report:

> *5.23 The data indicate that, in many cases, litigation funders are obtaining windfall profits well in excess of the risks they are taking. And those windfall profits are coming at the expense of the class members' share of the proceeds from a successful outcome. For example, the Attorney-General highlighted the Australian Law Reform Commission finding in its Final Report that 'when litigation funders were involved in a class action, the median return to class members was just 51 per cent, compared to 85 per cent when a funder was not involved'*
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> *5.24 To be clear, the incidence of windfall profits is not restricted to isolated instances of illegal or egregious behaviour. Rather, there appears to be a systemic and inappropriate skewing of the proceeds of a successful class action in favour of litigation funders at the expense of class members. This clearly fails the test of a reasonable, proportionate and fair division of the returns between class members, lawyers and litigation funders.*

[10] IMF Bentham, 'Keynote Address, The Hon Justice Michael Lee', 27 June 2017, transcript.

Later in the Final Report, the Committee relevantly stated:

13.53 Litigation funders appear to be making windfall profits from Australia's class action system at the expense of class members and defendants. Litigation funders ought to be reimbursed for the costs incurred and make a profit which is reasonable and proportionate to the risk undertaken. However, the slice of settlement sums going to litigation funders is often disproportionate to the costs incurred and risk undertaken. The current percentage-based billing practice contained in litigation funding agreements enables windfall profits to be obtained. Currently, the difference between the capital a litigation funder has put at stake and the profit made is often unreasonable, disproportionate and unfair. The unfairness is primarily borne by the class members because their share of the settlement is significantly reduced by the excessive proportion going to litigation funders.

13.54 The committee is not persuaded by the argument that it is better for class members to get 50 per cent of something with the involvement of a litigation funder, as opposed to 100 per cent of nothing without the involvement of a litigation funder. The committee considers that such arguments ignore the possibility that class members could receive substantially more than 50 per cent of something, with litigation funders still receiving a return that is reasonable, proportionate and fair for the risks they have taken.

The Litigation Funding Bill would appropriately implement reforms to prevent the misuse of the legal system by litigation funders pursuing unfair windfall profits by:

- Ensuring that the claims distribution method in a funding agreement for a class action litigation funding scheme is fair and reasonable (s. 601LG(1)(a));

- Introducing a rebuttable resumption that a claim proceeds distribution method is not fair and reasonable if more than 30% of the claim proceeds for the scheme are to be paid or distributed to entities who are not members of the scheme as a whole (s. 601LG(5)).

A rebuttable presumption that there be a 70% return to plaintiffs is obviously fair and reasonable, despite the claims by those with vested interests who are seeking to preserve their excessive profits from speculative litigation.

Returns to litigation funders, whether they be based on a settlement sum or an amount awarded by a Court, should be proportionate to the cost and risk undertaken, and should avoid the potential for profits which have been described by various judgments as 'stratospheric', 'arguably excessive' and 'not fair and reasonable'.[11]

[11] *Tredrea v KPMG Financial Advisory Services (Australia) Pty Ltd* (No 3) [2019] NSWSC 871, [89], [94]; *Endeavour River Pty Ltd v MG Responsible Entity Limited* [2019] FCA 1719.

In his ex-tempore reasons for approving a recent settlement of three class actions regarding the Commonwealth's use of allegedly toxic firefighting foam, Lee J acknowledged the value of the availability of class actions but noted that the phrase 'access to justice' is often misused by finders to justify "what at bottom is a commercial endeavour to make money out of the conduct of litigation".[12]

The financial incentive for litigation funders to take an unfair proportion of settlement proceeds or an award from litigation proceedings fills investors' pockets at the expense of group members. Many of these investors are located overseas and pay no taxes in Australia.

In order to avoid undermining the policy basis for allowing representative proceedings in Australia, the Litigation Funding Bill would implement appropriate limits on the profits which litigation funders can extract from class action proceedings. The proposed reforms would go a long way toward avoiding the misuse of the Court system as an avenue to turn an easy profit or to gamble on speculative litigation.

Anti-avoidance provisions

Provisions have been inserted into the Bill which are aimed at preventing funders from structuring their arrangements to avoid being subject to the regulatory regime to be imposed on class action litigation funders in proposed s. 9AAA(2) of the Corporations Act.

Ai Group supports the inclusion of these proposed anti-avoidance provisions to ensure that funding entities are unable to enter into contrived arrangements that would undermine the policy justification for the amendments.

Conclusion

The Litigation Funding Bill implements vital reforms.

We urge the Committee to recommend that the Bill is passed without delay.

[12] Eveleigh, A., '"A significant inequality of arms": Funding led to better outcome in PFAS class action, judge says', *Lawyerly* 9 June 2020.

ABOUT THE AUSTRALIAN INDUSTRY GROUP

The Australian Industry Group (Ai Group®) is a peak employer organisation representing traditional, innovative and emerging industry sectors. We are a truly national organisation which has been supporting businesses across Australia for nearly 150 years.

Ai Group is genuinely representative of Australian industry. Together with partner organisations we represent the interests of more than 60,000 businesses employing more than 1 million staff. Our members are small and large businesses in sectors including manufacturing, construction, ICT, transport & logistics, engineering, food, labour hire, mining services, the defence industry and civil airlines.

Our vision is for thriving industries and a prosperous community. We offer our membership strong advocacy and an effective voice at all levels of government underpinned by our respected position of policy leadership and political non-partisanship.

With more than 250 staff and networks of relationships that extend beyond borders (domestic and international) we have the resources and the expertise to meet the changing needs of our membership. Our deep experience of industrial relations and workplace law positions Ai Group as Australia's leading industrial advocate.

We listen and we support our members in facing their challenges by remaining at the cutting edge of policy debate and legislative change. We provide solution-driven advice to address business opportunities and risks.

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