

Parliamentary Joint Committee on Corporations and Financial Services

Submission by Omni Bridgeway Limited

17 June 2020

Omni Bridgeway Limited welcomes the opportunity to provide a submission to the Parliamentary Joint Committee on Corporations and Financial Services inquiry into litigation funding and the regulation of the class action system.

As the Attorney-General, the Hon. Christian Porter MP, said in announcing the inquiry: “Nothing in this parliamentary process of scrutiny proposes an end to class actions or litigation funding.”¹

We support the Attorney-General’s statement given the important role that both class actions and litigation funding play in our economy and society. However, we agree with the Attorney-General that there are opportunities to improve the class action system in Australia and the role of litigation funding within it to ensure fair and equitable outcomes for plaintiffs.

We look forward to participating in the Committee process.

Summary

- Omni Bridgeway has long supported additional regulation of litigation funding and believes this would increase transparency and confidence in the class action system.
- Increased regulation must be carefully designed to avoid jeopardising the availability of litigation funding for the people it protects – ordinary Australians seeking access to justice – and other unintended consequences, such as undermining the continuous disclosure regime and increasing the cost of capital for Australian listed companies.
- Litigation funding of class actions provides ordinary Australians, who often have no other avenue for redress, with access to justice and potential damages for misconduct.
- The courts play a significant role in protecting the interests of group members, especially in relation to settlements, and are just one of a number of checks and balances that can serve to regulate legal costs and funders’ fees.
- Litigation funding fees should not be analysed by cherry-picking cases, by ignoring the risks of losing assumed by the funder, or the costs of running the funding business, or by comparing funded cases with non-funded cases or other different types of investments.
- Returns to Omni Bridgeway in funded cases are proportionate to the costs and risks the company accepts in funding a case, especially the uncapped nature of the costs and the

¹ Commonwealth, *Parliamentary Debate*, House of Representatives, 13 May 2020, 3343 (Christian Porter, Attorney General)

uncapped cover for adverse costs. These returns are before operating overheads and the costs of running the business are taken into account. Returns on individual matters should not be conflated with net profit.

- Without clear legislative guidance, courts have been required to determine the rules of the class action system.
- Recent decisions of the courts, including endorsement of common fund orders, have had the effect of encouraging a 'rush to court' and duplicate actions, putting an undesirable burden on the courts and defendants. Notwithstanding this, credible research finds there has been no 'explosion' in the number of class actions, including securities class actions, in Australia
- The proposed introduction of contingency fees for lawyers in Victoria would make that situation worse, introduce untenable conflicts and encourage jurisdiction shopping.

Omni Bridgeway recommendations

- Support the proposed licensing regime for litigation funders operating in Australia recently proposed by the Treasurer. A licensing regime should include minimum onshore capital adequacy requirements, disclosure obligations and reporting standards in addition to the current conflicts management requirements
- Support the application of the managed investment scheme (MIS) regime to future funded class actions in Australia (i.e. grandfathering existing class actions), conditional on appropriate modifications to the MIS framework to ensure it is fit for purpose in a litigation funding context
- Introduce legislation to require a minimum return to group members in a funded Australian class action of no less than 50 per cent of the gross proceeds from the action
- Introduce legislation to end the use of common fund orders and prevent the introduction of contingency fees for lawyers in Australia
- Introduce legislation to give the Federal Court exclusive jurisdiction over securities class actions and any other class actions involving Federal law
- Introduce from May 2020 a six-month moratorium on new Australian class actions that are associated with COVID-19-related disclosures²

² Omni Bridgeway first publicly supported a six-month moratorium on new Australian COVID-19-related class actions in its [ASX announcement of 14 May 2020](#)

About Omni Bridgeway

Omni Bridgeway is Australia's largest and most experienced litigation funder and is a global leader in dispute resolution finance. The company was known as IMF Bentham Limited in Australia until it completed the acquisition of Europe-based Omni Bridgeway in November 2019 and adopted a single global name. The company listed on the Australian Securities Exchange in 2001, specifically to promote transparency in what was at that time a new industry.

Today, approximately 95 per cent of its 4200-plus individual shareholders are Australian. The company employs approximately 70 people in Australia and is an Australian resident for tax purposes.

Omni Bridgeway currently has a diversified portfolio of approximately 270 funded claims around the world, with a clear majority now outside Australia. Omni Bridgeway is currently funding 14 Australian class actions, including five securities class actions on behalf of shareholders. In a large part because of the ongoing uncertainty surrounding the class action landscape, the company has not funded a new Australian shareholder class action in more than 12 months.

Omni Bridgeway funds claims from its own balance sheet or from one of seven specialist funds it has established with a range of investors.

Omni Bridgeway funds a wide range of claims, including:

- single-party disputes, which include general commercial disputes, claims against estates and trustees, building and construction disputes, patents, professional indemnity claims, contract disputes, and claims against insurers;
- insolvency proceedings, including claims for insolvent trading, preferences and breach of directors' duties as well as third-party claims;
- class actions, including securities class actions, cartel claims, claims involving the provision of financial services, defective building products, and claims in connection with land contamination;
- international commercial arbitration and investment treaty claims; and
- enforcement proceedings.

Since listing on the ASX, Omni Bridgeway has been involved with 83 class actions, generating more than \$1.6 billion in recoveries, of which approximately \$1.0 billion – 62.1 per cent³ – has been returned to class action group members. Of the balance of the recoveries, \$217 million covered the legal and other 'project costs' of preparing and prosecuting the actions paid by Omni Bridgeway. Over this 19 year period, Omni Bridgeway has earned a commission of approximately \$395 million - or 24.5 per cent of the recoveries - after covering legal and other project costs (before the company's operating costs).

The group members in these class actions comprise both what are described as 'mums and dads' and also sophisticated institutional investors.

Omni Bridgeway funds only 3-5 per cent of all applications for funding it receives worldwide, demonstrating its commitment to support only genuine actions with reasonable prospects of a successful outcome for claimants. This also recognises Omni Bridgeway's obligation to the courts and the public not to burden the courts with meritless claims.

³ This statistic is based on 71 actions won, settled or lost. The balance was withdrawn. This statistic is based on the amount of project costs paid by Omni Bridgeway. In some circumstances the lawyers may have been paid additional amounts out of the settlement monies and the settlement amount may have earned interest before distribution to group members.

Further information on Omni Bridgeway can be found on its website at www.omnibridgeway.com, including its latest financial results and its Annual Report to shareholders.

The Terms of Reference

(1) What evidence is available regarding the quantum of fees, costs and commissions earned by litigation funders and the treatment of that income?

Announcing this inquiry, the Attorney-General asked “why the returns to the litigation funders appear to be so excessive”. We will argue in this submission they are not excessive and that the returns generated by litigation funders are appropriate and proportionate.

Key points

1. Analysis of litigation funders’ fees cannot be addressed by cherry-picking certain cases, including one case celebrated in the media that was not even a class action⁴, and ignoring others. An examination is required of returns across all funded cases in a litigation funders’ portfolio, including those that were lost, and of the costs of running the business.
2. Any comparison between returns to group members in funded class actions with returns in unfunded class actions is invalid, as in most instances without funding the case would not have proceeded at all.
3. When examining the level of returns, regard has to be had to the risks being assumed. As the Federal Court has recognised, these risks must be assessed at the time they were assumed and not once the case has finished with the benefit of hindsight⁵. Litigation funders typically provide limited recourse funding (recourse limited to a recovery), with an open chequebook to pay the legal costs and any adverse costs, over an uncertain time period, with incomplete information in respect of the case and an outcome that cannot be predicted with certainty. And even if the case is successful, the defendant may be unable to pay or the insurance may be depleted or extinguished.
4. Part of the monies received by a litigation funder from the settlement of a class action will normally include reimbursement of the legal costs the funder has paid. It can be extremely expensive to prosecute large complex class actions against well-resourced defendants. To the extent that settlement monies are eroded by such costs, that is a function of the costs of litigation in Australia and not a reflection on litigation funding. If the real concern is with returns to group members, the size of the costs of litigation and potential adverse costs orders should also be examined.
5. The courts will only approve a settlement of a class action if it considers the settlement to be fair and reasonable and in the interests of group members⁶. This includes an examination of what the group members will receive after costs and funder commission and, in many cases, a review of confidential legal opinions that are relevant to the risks of the case. This is one of the many checks and balances in the system that protect plaintiffs from unreasonable fees.

⁴ *Fitzgerald v CBL Insurance Ltd* [2014] VSC

⁵ *Endeavour River Pty Ltd v MG Responsible Entity Limited* [2019] FCA 1719, para 27.

⁶ All settlements of class actions must be approved by the court.

Omni Bridgeway's model

It is worth providing some clarity about Omni Bridgeway's funding model in Australia.

Firstly, Omni Bridgeway's funding for class actions is provided on a limited-recourse, open cheque basis – that is, we pay the claimant's costs⁷ as the case proceeds and are only reimbursed if successful.

Omni Bridgeway supports 'closed' or opt-in class actions, which, until the increased use of open class actions supported by 'common fund orders' (CFOs) after the *Money Max* decision in 2016⁸, were the primary avenue for funding class actions⁹. In a closed class action, each member must sign a litigation funding agreement (LFA) with the litigation funder. This agreement – disclosed by Omni Bridgeway and provided to the court and the defence lawyers¹⁰ – clearly sets out fees the litigation funder may be entitled to in the event of a successful outcome.

Omni Bridgeway does not provide legal services. Instead, it provides a broad range of services to assist clients and the lawyers in relation to the conduct of the proceedings.

In funded class actions, Omni Bridgeway plays a key role in informing potential claimants of the opportunity to join the class action to enforce their rights – a role that has been accepted by the High Court¹¹. This can include covering the cost of potential members seeking their own independent legal advice about the terms of the LFA.

In the claims that it funds, Omni Bridgeway provides funding for the claimants' own legal fees and disbursements including counsels' fees, witness expenses, court costs and adverse costs (together, these are referred to by Omni Bridgeway as the project costs).

In addition to funding, Omni Bridgeway provides other services to its clients that it does not separately charge for. These include investigating the claims and the prospects of them being resolved by means other than litigation, including by direct negotiation with the defendant or through alternative dispute resolution processes, such as mediation or expert determination. These processes are always conducted in conjunction with the claimants' lawyers, and mediation is overseen by current or former judges or practising senior officers of the court, such as a SC or QC.

Omni Bridgeway also oversees the litigation, negotiates litigation budgets with the claimants' lawyers, ensures so far as possible that the legal costs and strategies are proportionate to the sums at stake, and liaises with the lawyers on a day-to-day basis (subject always to the representative claimant's rights to override Omni Bridgeway's instructions and the lawyers' paramount professional duties to the claimants). Omni Bridgeway also assists the claimants on litigation strategy and attends and participates in mediations.

There are other costs absorbed by Omni Bridgeway that reduce its overall returns. For example, Omni Bridgeway has a Client Team that undertakes many of the administrative tasks relating to managing group members' claims at no additional charge to group members. The alternative is

⁷ On some occasions, the lawyers agree to carry some legal costs.

⁸ *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Ltd* (2016) 245 FCR 191.

⁹ Cases that started as closed class actions were often opened and then closed in advance of settlement discussions to facilitate an outcome and provide finality for a defendant.

¹⁰ Commercially sensitive information is typically redacted

¹¹ *Campbells Cash and Carry Pty Ltd v Fostif* [2006] HCA 41. At paragraph 202, the High Court stated "By 'organising' persons into a legal action for the vindication of their legal rights, representative proceedings are not creating controversies that did not exist. Controversies pre-existed the proceedings, even if all those involved in them were unaware of, or unwilling earlier to pursue, their rights. A litigation funder, ..., does not invent the rights. It merely organises those asserting such rights so that they can secure access to a court of justice that will rule on their entitlements one way or the other, according to law."

for these functions to be performed by the lawyers and form part of the legal costs that the group members are asked to pay.

Crucially, Omni Bridgeway also agrees to pay any adverse costs orders in the event that the claims are unsuccessful, and will meet any security for costs that the court may order Omni Bridgeway's clients to provide. In effect, this represents an 'open cheque' for the period of the case. Even if a funder takes out an 'after the event' insurance policy, these typically have a limit of indemnity and may not cover adverse costs in the event the lawyers or clients want to discontinue what turns out to be a poor case before judgement.

Further, other funders (or lawyers acting on a no win, no fee basis) may pass on the costs of an 'after the event' insurance policy to group members. Omni Bridgeway does not generally pass on these costs in Australian matters. This exposure to adverse costs, which represents about 70 per cent of the clients' costs (assuming only one separately represented defendant), is reflected in the amount of the commission charged by Omni Bridgeway.

In return for Omni Bridgeway's promise of funding and assumption of the risks of commencing and prosecuting the class action, claimants agree to assign to Omni Bridgeway a share of any damages or settlement proceeds that are recovered from the opposing parties to their claims. The LFA – made at the commencement of a class action and before the outcome is known – includes reimbursement of all amounts Omni Bridgeway has paid and a percentage of the recoveries. In some cases, the fee is based on a multiple of the costs spent by the company in the proceedings.

Ultimately, the litigation funders' fee depends on the claim size, estimated recoverable amount, estimated costs, estimated duration to resolution and the risks undertaken.

Litigation funders' returns

For industry-wide figures, Omni Bridgeway considers the empirical reports of Professor Vince Morabito¹² the best sources of analysis on funding fees in Australia.¹³ Professor Morabito's reports, some of which have been funded by Omni Bridgeway¹⁴, have been relied on by several Federal Court judges in recent class action decisions, including in settlement approval judgments.

In the *Sirtex Medical* settlement approval decision,¹⁵ for example, Justice Beach elaborated on funding commission rates and concluded that the rate sought in the action – a 25 per cent funding commission on the gross settlement sum – was well within the range that he considered to be reasonable and proportionate for the risks undertaken by the funder:¹⁶

"I do not subscribe to any 'race to the bottom' philosophy in setting commission rates. As a corollary, I do not accept that rates should be set that do not properly provide a reward for the risk undertaken."

¹² Professor Vince Morabito is in the Department of Business Law and Taxation at Monash University's Monash Business School.

¹³ For example, "*Common Fund Orders, Funding Fees and Reimbursement Payments*", January 2019, chapter 2.

¹⁴ Omni Bridgeway has also provided funding to other Australian academics and institutions, such as the University of NSW. Professor Morabito's research has also been funded by the Federal Government's Discovery Grant from the Australian Research Council, the Victoria Law Foundation and law firm Herbert Smith Freehills.

¹⁵ *Kuterba v Sirtex Medical Limited (No 3)* [2019] FCA 1374 (23 August 2019). The claimants and group members were funded by Omni Bridgeway.

¹⁶ The risks included that Sirtex's assets would be removed from the jurisdiction (see *Kuterba v Sirtex Medical Limited (No 2)* [2018] FCA 1489).

He had regard to class action statistics published by Professor Morabito¹⁷ and said he did not require any further inquiry into the rates and had confidence in Professor Morabito's statistics as, at least, a suitable *prima facie* benchmark.

In his 2019 report, Professor Morabito presented statistics in relation to funding fees based on data gathered from judicially approved class action settlements.¹⁸ He presented the data in several ways, including calculating for each of the identified settlement agreements in his possession the percentage paid to funders, with respect to their funding commissions, and then determined the median funding commission rate. He concluded that the median percentage of settlement funds "consumed" by funding fees in funded federal class actions, and also in all funded class actions, settled during the review period was 25 per cent.

Professor Morabito said these figures were substantially lower than he had been expecting and concluded:

"As far as I have been able to ascertain, the higher figures that have frequently been mentioned in the media and the legal literature appear to be attributable, to some extent, to: (a) reliance on only the better-known class action settlements; and/or (b) incorrectly treating funding commissions and the total payments received by litigation funders, pursuant to class action settlement agreements, as being the same thing.

*"In order to ensure that readers of this report do not make the same mistake outlined in point (b) above, it is important to draw attention to the fact that pursuant to settlement agreements executed in class action litigation, funders usually receive reimbursements for all or some of the costs they incurred in the course of the litigation plus a funding commission or fee, usually calculated as a percentage of the total compensation secured on behalf of the claimants."*¹⁹

Professor Morabito has also examined a very similar review period to a study carried out by the Australian Law Reform Commission (ALRC) – between 2013 and 2018.²⁰ He concluded that the median percentage of settlement funds "consumed" by funding fees in funded federal class actions settled during the period from January 2013 to December 2018 was 26 per cent and the median percentage of settlement funds "consumed" by funding fees in all funded class actions settled during this period was 25.5 per cent.

Professor Morabito found that:

*"The first median figure above of 26%, for funded federal class actions, is somewhat lower than the figure of 30% that the ALRC arrived at on the basis of its more limited database."*²¹

And that:

*"...in approximately two-thirds of all funded cases settled during the review period more than 50% of the settlement proceeds were left for distribution to class members. Class members receiving (collectively speaking) more from class action settlements than solicitors, funders, barristers and various experts combined, in two out of every three Australian class actions settled over the last 27 years, may be said to be a positive thing."*²²

¹⁷ Supra, note 14

¹⁸ Ibid, page 10. This data represented (a) 85% of all judicially approved settlement agreements in Australian funded class actions and (b) 87% of all judicially approved settlement agreements in federal funded class actions as at the end of 2018.

¹⁹ Ibid, page 11.

²⁰ ALRC Final Report. The conclusions reached by the ALRC were drawn from a small sample size of only 30 cases that had finalised in the Federal Court (in the period 2013 – October 2018) which the ALRC's report acknowledged had limitations. Due to confidentiality orders and incomplete data, these were the only cases on which the ALRC held enough information about legal and funding fees to calculate the returns to group members in that period.

²¹ Supra, note 14, page 12.

²² Ibid, page 12.

Examples of returns to claimants of less than 50 per cent of gross proceeds are the minority for Omni Bridgeway-funded cases. Those outcomes are sometimes produced by adverse developments in the underlying case, unfavourable evidence that is discovered after the commencement of the proceedings, a change of law, or if there is insufficient loss suffered by group members.

Omni Bridgeway believes that where returns are less than 50 per cent, the funder should be required to carry that burden, not the claimants. That is what Omni Bridgeway strives to do and why we support a legislated minimum return to group members of 50 per cent of gross recoveries in funded class actions.

In a number of matters, Omni Bridgeway has voluntarily reduced its entitlement to recoveries to ensure a larger return for group members. These include the unsuccessful class action against several Australian banks over customer fees, in which Omni Bridgeway opted to return 25 per cent of a settlement to NAB class members who were entitled to no returns as the case had been lost (this figure has been erroneously used by the ALRC in its calculation of average returns to members)²³, and the class actions against the Department of Defence over contamination caused by the use of toxic firefighting chemicals on Defence facilities in Williamstown in NSW, Oakey in Queensland and Katherine in the Northern Territory.

The court-approved funding commission payable to Omni Bridgeway across the three contamination class action investments represented 24 per cent of the settlement amount. Omni Bridgeway reduced its contractual entitlements across the three class actions by approximately 30 per cent. This decision was made before the announcement of this parliamentary inquiry.

²³ Australian Law Reform Commission, *"Integrity, Fairness and Efficiency – An Inquiry into Class Action Proceedings and Third-Party Litigation Funders"*, ALRC Report 134, tabled in parliament on 24 January 2019, (**ALRC Final Report**), at 88 and 320. The ALRC misinterpreted the data from a class action funded by Omni Bridgeway (then known as IMF Bentham) – *Farey v National Australia Bank Limited [2016] FCA 340*. This case resolved successfully for \$6.6 million but was part of a wider set of actions brought on behalf of approximately 130,000 customers over bank fees. The actions included a test case which was unsuccessful on appeal and Omni Bridgeway paid approximately \$30 million in costs and adverse costs. Omni Bridgeway had been entitled to all of the proceeds of the NAB settlement to defray some of our costs on the other bank fees cases, including the test case. However, Omni Bridgeway waived that right and returned approximately 25 per cent of the settlement proceeds to the NAB group members. Contrary to the ALRC's conclusions, Omni Bridgeway did not receive a funding commission of 62% of the settlement proceeds and in fact received no funding commission on that case.

Risk and return

Omni Bridgeway believes there needs to be a balanced discussion about the adequacy of returns to allow the litigation funding industry to exist and the considerable risks that litigation funders assume. Too often, superficial commentary about litigation funders' returns is based on isolated cases – in some cases, such as the oft-cited Huon Corporation matter, entirely inaccurately.

(The Huon Corporation case was not a class action, but a claim brought by two trustees against an insurance company. The Victorian Law Reform Commission subsequently noted that the “safeguards that exist in insolvency proceedings and class actions did not apply in this case”.²⁴)

More sophisticated analysis considers returns across a portfolio of cases and recognises that returns calculated for the risk of funding litigation are not comparable with the returns, for example, on a government bond, as the risks are not comparable. With litigation, the outcomes are binary. The case is either won (judgement or settlement) or lost. The funder only gets paid if the case is won. If the case is lost, the funder loses its investment and typically has to pay approximately 70 per cent of the costs of the other side. At the time of funding, the funder cannot know with certainty the quantum of these costs or if the case will be won.

Most importantly, the financial risks assumed by litigation funders – running to tens of millions of dollars in many cases – cannot be examined with the benefit of hindsight once the outcome of a case is known.

Litigation funders are required to evaluate and then assume these risks upfront, before the first court hearing, when there are material uncertainties in terms of the time it will take to resolve the matter, the legal and other costs of the case and, of course, the outcome.

In the *Murray Goulburn* class action, Justice Murray discussed the considerations for assessing the “reasonableness of a funding commission”:

“The litigation risks of providing funding in the proceeding ... is a critical factor and the assessment must avoid the risk of hindsight bias and recognise that the funder took on those risks at the commencement of the proceeding.”²⁵

And in approving the settlement in the Williamstown, Oakey and Katherine contamination matters, Justice Lee made the following statement:

“...in assessing ‘justice’ in this context, it is important that the assessment not be distorted by hindsight bias...”

“On any view of it, this was complex litigation attended by some risk. Moreover, it is appropriate to focus on the risk when the funding agreements are entered into, not assess the risk after the making of implicit findings (following the reports of referees being adopted) and all the work preparing for hearing had essentially been done. Although I am conscious of the complaints of some group members as to the size of the funding fee deduction, when one compares this to other settlements and the risks involved, the amount of 25 per cent commission across the three proceedings could not be stigmatised as being unreasonable in all the circumstances.”²⁶

In Omni Bridgeway's case, returns on successful cases must be balanced against costly losses in other parts of its portfolio – approximately \$30 million in the case of the Omni Bridgeway-funded

²⁴ Victorian Law Reform Commission, “Access to Justice – Litigation Funding and Group Proceedings”, March 2018, at 28.

²⁵ *Endeavour River Pty Ltd v MG Responsible Entity Limited* [2019] FCA 1719, para 27.

²⁶ *Smith & Ors v Commonwealth of Australia* (Federal Court, NSD 1908 of 2016/ NSD 1155 of 2017/ NSD 1388 of 2018, Justice Lee, 5 June 2020), para 87

action on behalf of bank customers over various bank fees – and the outsized risks that come with pursuing litigation against large, well-funded defendants over long periods.

For example, in the class actions Omni Bridgeway has funded since 2001, the potential adverse cost order exposure has been estimated at substantially more than \$150 million – or approximately 70 per cent of the project costs provided by Omni Bridgeway. The average length of a class action funded by Omni Bridgeway is 2.6 years. This is effectively the period of investment required by the company before its first return – and only then if the funded client is successful in the matter.

In the class actions for chemical contamination at Williamstown, Oakey and Katherine, the matters ran for 4.5 years and Omni Bridgeway faced potential costs of more than \$50 million in the event it was unsuccessful.

While Omni Bridgeway has delivered reliable returns to its investors across its portfolio and over the longer-term, the company has reported losses on individual cases and for full financial years, including in 2017-18 and 2018-19. Only a company that takes a portfolio-wide view of risk and reward – rather than assessing returns on an individual case basis – could manage combined net losses of \$44 million over these two financial years. Omni Bridgeway has reported losses before tax in six of the 19 years since listing on the ASX.

In fact, analysis of Omni Bridgeway's gross margins compared to other ASX-listed entities belies the myth that litigation funders make outsized profits.

In the 2018 calendar year, Omni Bridgeway's gross margin was 12.8 per cent compared to an average of 40 per cent for the ASX200 companies and 60 per cent for the financial (banking) sector.²⁷ In calendar 2019, Omni Bridgeway's gross margin was 27 per cent compared to 40 per cent for the ASX200 and 59 per cent for financials.²⁸ Omni Bridgeway's average return on equity for the past five years is -0.2 per cent.

Unsophisticated analysis attempts to compare returns made by litigation funders on individual cases – or an average of returns on individual cases – to other investment benchmarks, such as bond yields, which unlike litigation funding are typically considered a risk-free return. This is an entirely misleading comparison because returns on individual cases fail to deduct the cost of operating the underlying business that supports the litigation funding.

Litigation funders employ a significant infrastructure that manages the process of raising capital, sourcing potential litigation investments, conducting due diligence to assess the merits of litigation investments, drafting and negotiating the relevant funding documents and then, ultimately, managing the drawn-out process that is litigation. The blended uncertain returns from their risky investments must cover the cost of running the business and ultimately providing an acceptable return to investors that provide capital.

The returns of litigation funding should be measured against the returns to investors – namely those that provide the equity capital – in the same way as they would otherwise provide capital to other ASX200 companies. In the past decade, Omni Bridgeway's total return to shareholders has been 19.5 per cent per annum (including reinvestment of dividends). While this exceeds the 30-year ASX average total shareholder return of 9 per cent per annum, it is in line with many other successful growing companies on the ASX, such as CSL and NextDC.

²⁷ Citi Global Markets Australia 'ASX200 gross margins' analysis, May 2020

²⁸ Ibid

Checks and balances

It is important to note that the courts retain considerable oversight of litigation funding fees, a power exercised most recently in the Murray Goulburn class action.²⁹

And court approval is just one of numerous checks and balances that already exist in the legal system to regulate and, in some cases, moderate litigation funders' commissions.

There are opportunities to improve these measures, which we support, but taken individually and together they already provide a significant degree of protection for claimants in class actions from unreasonable litigation funding fees. As such, the accusation that litigation funders are unfettered price-setters is patently false.

These safeguards include:

1. Litigation Funding Agreements (LFA)

LFAs set out the commission to be earned by the funder. The LFA also includes a cooling-off period, support for members to obtain their own independent legal advice and standard terms regarding the management of conflicts. In the event of a dispute between any of the claimants, lawyers and funders, the LFA stipulates the appointment of an independent QC to resolve the issue.

The LFA is provided to the court and the defence lawyers before the first directions hearing.

The Federal Court's Class Action Practice Note makes clear that any litigation funding agreement must be disclosed to the defendant and to the court.

2. Lawyers' obligations

Members in a funded class action are represented by two groups of lawyers: solicitors retained directly by members (not the funder) and independent barristers. The LFA makes it clear that the lawyers' obligation is to the client not the funder. (Explored further in our responses to Questions 3 and 4.)

3. Officers of the court

A lawyer's over-riding obligation and fiduciary duty is to their client. As officers of the court, lawyers have a duty to the court and their conduct is supervised by state law societies and Bar associations. (Explored further in our responses to Questions 3 and 4.)

4. Existing regulation and legislation

Since 2013, litigation funders have been required by the Australian Securities and Investments Commission (ASIC) to have "adequate practices for managing any conflicts of interest that may arise". The regulations are backed by sanctions for non-compliance. (Explored further in our responses to Questions 5 and 6.)

²⁹ *Endeavour River Pty Ltd v MG Responsible Entity Ltd* [2019] FCA 1719.

5. Mediated settlements

Mediations and settlements are typically overseen by current or former judges or practising senior officers of the court, such as an SC or QC. It is routine in settlement approval applications for the appointment of an independent expert to review reasonableness of legal costs.

6. Group members' rights

Group members have the right to opt out of class actions and the right to object to settlements. Group members also have general law protections, covering issues such as unconscionable conduct, misleading and deceptive conduct and unfair contracts.

7. Court powers

The courts retain significant powers throughout proceedings with the potential to impact the role and returns of funders. These include the ability: to address the duplication of class actions; to stay proceedings; to declass a class action; to grant a respondent a summary judgement or strike out if the case is without merit; to order costs directly against the funder; to order security for costs; and to appoint an amicus or contradictor for the group members' benefit.

8. Court approval

In all class actions settlements must be approved by the court.

The court will only approve a settlement of a class action if it considers the settlement to be fair and reasonable and in the interests of group members. This includes an examination of what the group members will receive after costs and the funders' commission.

The court will usually be provided with confidential material by the plaintiff's lawyers concerning the prospects of the success of the case and the risks involved. Because the material is confidential it can sometimes be difficult for third parties to fully appreciate the risks the funder has assumed. Accordingly, the court is best placed to protect the interests of group members and determine what is a fair and reasonable outcome.

In the Federal Court, judges are obliged to consider litigation funders' commissions. The Federal Court Practice Note says:

*"Where a proposed settlement contemplates that any part of the payments to be made to class members will be applied toward reimbursement of the unrecovered legal costs of the proceeding, or toward payment of litigation funding charges, the Court will usually require that the material filed in support of the application should demonstrate that reasonable steps were taken to alert class members to the likelihood of such deductions as soon as practicable after that became apparent, so that class members were, at the relevant time, able to take such steps as may have been practicably available to them to negotiate as to legal costs or as to litigation funding charges as applicable, or to remove themselves from the class action."*³⁰

The Note goes on to warn that a "more extensive examination of the litigation funder's records may be required where:

(a) the class members include persons who are not clients of the applicant's lawyers or of the litigation funder;

³⁰ Clause 16.1.

(b) the deduction per class member constitutes a significant proportion of the settlement amount otherwise payable to each class member; or

(c) the litigation funder imposes charges beyond the percentage commission set out in the litigation funding agreement ...”³¹

9. Australian Securities Exchange obligations

As an ASX-listed entity, Omni Bridgeway, unlike unlisted funders, faces additional requirements in terms of the disclosure of its returns and capital position.

Reporting returns

Omni Bridgeway is fully transparent – to group members, the courts and its investors – about the returns it generates from funded class actions. Omni Bridgeway regularly reports the outcomes of its class actions to the ASX in line with – and often exceeding – its continuous disclosure requirements.

In the event of successful actions, it reports to the ASX the gross income it is entitled to, the profit generated, the return on invested capital (ROIC) and the internal rate of return (IRR) – before and after capitalised overheads. An example of these announcements can be found at: www.imf.com.au/docs/default-source/site-documents/116-b-australian-class-actions---settlement-update.

In the event of unsuccessful actions, Omni Bridgeway reports its costs and losses.

The introduction of a 50 per cent minimum return for class members in a funded case would result in the funder making no income in some successful cases. In fact, in some extreme cases, the funder could report a loss because the costs it has paid on behalf of its client represent more than 50 per cent of the amount the defendants pay to settle the case.

Recommendation: *Introduce legislation to guarantee a minimum return to group members in a funded class action of no less than 50 per cent of the gross proceeds from the action*

(2) The impact of litigation funding on the damages and other compensation received by class members in class actions funded by litigation funders.

The argument advanced by opponents of litigation funding – that claimants get greater returns from unfunded class actions than they do from funded class actions – is a statement of the obvious. Funders recover their costs and fees from any recoveries, reducing returns for claimants. The real issue is how many claimants in those funded class actions would have received nothing because they were unable to take action as individuals without the support of litigation funding.

One example, funded by Omni Bridgeway, is the class action taken by the 6700 victims of the mismanagement of Queensland’s Wivenhoe Dam during the 2011 floods.

Lead claimant representative, Vince Rodriguez, says:

“Without funding from Omni Bridgeway, I would not have been able to successfully pursue my claim and run an action against such powerful entities. They agreed to back the Brisbane flood class action for me and thousands of other people who suffered damage from the flooding in January 2011.

³¹ Clause 16.4.

"I found the funding process fair and reasonable for the claimants, understood the terms of the Funding Agreement and Omni Bridgeway and the lawyers kept me fully informed during the claim and the litigation process.

"Funders take on a massive risk if they lose (not just the legal and other fees they have paid for, but also potential adverse costs). The case has been hard fought and still in May 2020 has not yet finally resolved. It is fair that funders recover their expenses and a commission for taking on the risk. Without them, claimants would recover nothing at all.

"I would support a requirement for a minimum of 50 per cent of any of the recoveries going to claimants in class actions. That would be a fair arrangement for all concerned. I also support the requirement that funders have a financial services licence."

In approving the settlement in the Williamstown, Oakey and Katherine contamination matters, Justice Lee said the case would have been "impossible to bring without a funder". He made the following observation about the role of litigation funders:

"There is a live contemporary controversy about litigation funding. I do not propose to enter the arena of this policy debate save to make a few comments.

*The term "access to justice" is commonly misused, most often by some funders who fasten upon it as an inapt rhetorical device. To those with a long and close involvement with litigation funding, it is evident that there is not only a danger in generalisation (and assuming all funders are the same), but there is also a danger of using well-worn phrases to obscure the reality that litigation funding is about putting in place a joint commercial enterprise aimed at making money. As I said in *Turner v Tesa Mining (NSW) Pty Limited* [2019] FCA 1644; (2019) 290 IR 388 (at 401 [41]): 'the funder is not so much facilitating access to justice by the funded party as itself gaining access to justice for its own purposes'.*

But recognition of this reality does not diminish the importance of litigation funding in allowing these class members to vindicate their claims against the Commonwealth. Without litigation funding, the claims of these group members would not have been litigated in an adversarial way but, rather, they would likely have been placed in the position of being supplicants requesting compensation, in circumstances where they would have been the subject of a significant inequality of arms ... But it strains credulity to think that claims of this complexity and attended by such potential expense could have been litigated to a conclusion without third party funding of some sort. It seems to me a testament to the practical benefits of litigation funding, that these complex and costly claims have been able to be litigated in an efficient and effective way and have procured a proposed settlement. It must be recalled that an acceptable settlement was only forthcoming after a vast outlay of resources, and the assumption of risk of a third party funder for potential adverse costs."³²

In that matter, fewer than 3 per cent of group members lodged objections to the litigation funder's commission or the fees and costs of the lawyers. The Court said that the settlements achieved "can fairly be described as excellent"³³. It said each of the three class actions settled for an amount either just under or just exceeding 100 per cent of the likely best possible quantum recoverable should the class members' claims succeed at trial.

In his study of the 122 shareholder class actions filed since 1992, Professor Morabito found that 101, or 82.8 per cent, were supported by litigation funders, with most of the balance funded through no win, no fee arrangements.³⁴

³² *Smith v Commonwealth of Australia (No 2)* [2020] FCA 837, paras 83-85

³³ *Ibid*, paragraph 68.

³⁴ Professor Vince Morabito, *Shareholder class actions in Australia – myths v facts*, November 2019, at page 20.

This is not surprising given claimants without a litigation funder behind them are exposed to adverse cost orders and potential bankruptcy. Funded class actions can also give defendants a degree of comfort that their costs will be covered in an event of an unsuccessful class action.

Critics of litigation funders compare median returns to group members in funded cases (51 per cent of recoveries) to median returns in unfunded cases (85 per cent), citing the Australian Law Reform Commission's report on class actions and litigation funders, handed to the Attorney-General in 2019.

As discussed above, we believe the comparison is meaningless. However, the figures were also based on a small sample size and incorrect analysis (in at least one instance) .

The conclusions reached by the ALRC were also drawn from a sample of only 30 cases that had finalised in the Federal Court (in the period between 2013 and October 2018). They comprised 19 funded and 11 unfunded class actions. Due to confidentiality orders and incomplete data, these were the only cases on which the ALRC held enough information about legal and funding fees to calculate the returns to group members in that period. The ALRC's report acknowledged it was aware of the limitations of small sample sizes. (The ALRC held incomplete data on an additional 61 cases in total that had finalised in the Federal Court since 1997.)

We know that in one case, the ALRC misinterpreted the data – a class action funded by Omni Bridgeway (then known as IMF Bentham), *Farey v National Australia Bank Limited* [2016] FCA 340. (See Footnote 25)

While we do not have complete information about the 11 unfunded class actions included in the ALRC's calculation of median returns, it is apparent from court and other documents that some of these cases were conducted on a no win, no fee basis with a so-called 'person of straw' as the representative plaintiff, that is, someone who has no assets. For example, the representative plaintiff in two class actions against Cash Converters was described as "a pensioner and grandmother from western Sydney". This means, in effect, that there is no way that a defendant who is successful in an action could recover their costs unless the representative plaintiff has taken out sufficient 'after the event' insurance cover.

This is relevant because in unfunded cases, there are often significant risks for both the representative plaintiff and the defendant if the case is lost and adverse costs are ordered. In the settlement approval decision in the unfunded DePuy hip implants class action (one of the 11 unfunded class actions included in the ALRC's calculation), the judge said:

*"To put it bluntly, the risk of the applicants failing completely could not be excluded. That would have meant no recovery by the applicants and group members at all, and the likelihood of an adverse costs order against the applicants for potentially many millions of dollars."*³⁵

In a class action against the Royal Bank of Scotland in relation to financial products sold to a group of investors (another of the 11 unfunded class actions), the judge in the settlement approval decision said:

*"The reason why his Honour makes reference to an external litigation funder is that it is invariably the case that when a funder is involved, an indemnity is given by that funder to an applicant against adverse costs. Here there was no litigation funder, and the applicants were exposed, in a difficult and highly expensive proceeding, to the prospect of financial damnation in the event that the proceeding failed."*³⁶

These situations are very different to the majority of cases in which a funder is involved and, as explained in the above quote, indemnifies the claimant for any adverse costs on an uncapped

³⁵ *Stanford v DePuy International Ltd (No 6) (DePuy Hip Implants)* [2016] FCA 1452 at [125].

³⁶ *Dillon v RBS Group (Australia) Pty Limited (No 2)* [2018] FCA 395 at [73].

basis. Funded cases provide not only the representative plaintiff but also the respondent and the court with comfort that, if the claim is lost, adverse costs will be paid.

Finally, some of the unfunded class actions included by the ALRC were self-funded by a subset of group members in those cases. However, the judgments approving the settlement in some of those actions indicated that the court considered the fact that the group members may not be able to continue to fund the litigation as a factor in approving a settlement³⁷.

Accordingly, although group members may have received more of the pie absent a funders' involvement, it was potentially a smaller pie. Commercial funding provides group members with comfort that the case will be pursued to its best possible return and not settled early because of financial constraints.

Another argument advanced by opponents of litigation funding is that litigation funders use the negative publicity of a shareholder class action to shame companies into an early settlement, regardless of the merits of the action, in the interests of avoiding sustained reputational damage.

It is argued that such settlements produce better returns for litigation funders, which do not have to fund the costs of preparing for and then going to trial. This, it is claimed, creates an inherent conflict between the interests of litigation funders (to generate the greatest return in the shortest period with the minimum outlay) and members (to secure a fair and equitable outcome).

Conversely, however, it has also been argued, as recently as the *Williamstown* matter, that litigation funders have an interest in prolonging matters because this can produce greater fees and commissions.

Neither argument is supported by facts and, in *Omni Bridgeway's* case, the resolution of every class action is considered on its individual merits and in line with both our and the lawyers' obligations to clients and the courts.

Firstly, as discussed in detail in our response to Question 4, lawyers have an over-riding obligation to their clients that balances the financial interests of any third-party litigation funder. Both the ASIC regulations and the Federal Court's Class Action Practice Note make this clear.

Secondly, the quantum of settlements in shareholder class actions – tens or hundreds of millions of dollars in many cases – puts paid to the claim that these are not meritorious actions for serious instances of misconduct.

The great majority of settlement monies are paid by insurers, which, by their nature, do not pay out hundreds of millions to avoid shame falling on their policyholders. The payment of these very large settlement amounts reflects a hard-nosed assessment of the probabilities surrounding the question of whether a higher amount will have to be paid by the insurer after trial.

Professor Morabito also found that more than 64 per cent of resolved funded class actions were ultimately resolved through judicially approved settlement agreements. He says: "This finding is clearly not consistent with the claim that commercial litigation funders have supported meritless class action litigation."³⁸

³⁷ For example, see *Robert William Lee & Anor v Bank of Queensland Limited* [2014] FCA 1376 at [24].

³⁸ Professor Vince Morabito, "Will 2020 mark the beginning of the end for class actions in Australia?", *Lawyerly*, 27 May 2020, at page 4.

It is also worth noting that the risk of not securing monetary compensation in shareholder class actions increased significantly after the judgement of Justice Beach of the Federal Court in the Myer class action last year.³⁹ Justice Beach found Myer had misled shareholders over its profit forecasts but ruled they had not suffered any loss and ordered both sides to pay their costs, estimated at more than \$10 million each in legal fees alone.

The logical outcome of the Myer judgement – coupled with the dismissal of the class action in the Babcock & Brown matter⁴⁰ – is that litigation funders will be required to take on much more risk in the matters they elect to fund and that companies and their insurers may in future be less likely to settle class actions and instead opt to take matters to trial.

(3) The potential impact of proposals to allow contingency fees and whether this could lead to less financially viable outcomes for plaintiffs.

Put simply, the reason that contingency fees are currently prohibited in Australia, is that “they create a more serious conflict of interest than conditional [i.e. no win, no fee] costs agreements”.⁴¹

In 2013, then attorney-general George Brandis QC signalled the Commonwealth Government was disinclined to support the introduction of contingency fees when he said the inherent “conflicts of interest and moral hazards should be addressed”⁴². Mr Brandis was responding to plaintiff law firm Maurice Blackburn’s involvement with litigation funder Claims Funding Australia, which was structured as a discretionary trust whose beneficiaries were principals of Maurice Blackburn.

Under the current system, lawyers and funders act as a check on each other, with both subject to court supervision. The lawyers owe their fiduciary duties to the litigants and can be relied upon to prevent overreaching by the funder. LFAs always include provisions for managing conflicts of interest. Clients rely on the advice of their lawyers – not litigation funders – as to whether a settlement is ‘fair and reasonable’.

Allowing contingency fees – as proposed by the Victorian Government – removes the advantage of these checks and balances. Allowing legal firms to effectively act as both funders and litigators of class actions risks creating conflicts of interests that, at worst, could result in firms putting their own financial interests ahead of their clients’. This has the potential to affect returns to group members.

The Law Council of Australia and the NSW Bar Association have argued strongly against the introduction of contingency fees in Australia, with both warning that allowing lawyers to hold a direct financial interest in the outcome of a case risks seriously compromising the lawyer’s fundamental obligations to the court and their client.

Significant weight should be given to the lawyers’ views as they are in the best position to recognise the risks of conflicts.

The Supreme Court of Victoria made clear its position on these potential conflicts in the Banksia class action, in which Norman O’Byrne SC and Mark Elliott acted as both the lawyers representing the plaintiff and had financial interests in BSL Litigation Partners Limited, the funder of the class action.⁴³ Mr Elliott was also a director of the funder.

³⁹ *TPT Patrol Pty Ltd as trustee for Amies Superannuation Fund v Myer Holdings Limited* [2019] FCA 1747.

⁴⁰ *DIF III – Global Co-Investment Fund LP v Babcock & Brown International Pty Limited (No 2)* [2019] NSWSC 1578

⁴¹ C Parker and A Evans, *Inside Lawyers’ Ethics* (Cambridge University Press, 2007), 192.

⁴² Chris Meritt, “*Regulation is on the cards*”, *The Australian*, 7 November 2013,

⁴³ *Bolitho v Banksia Securities Limited (No 4)* [2014] VSC 582.

Justice Anne Ferguson, now Chief Justice of the Supreme Court of Victoria, said an “observer would be concerned that there is a sufficient risk that Mr Elliott’s (indirect) shareholding and position as a director of the Litigation Funder will give the appearance that his role as a solicitor and officer of the court is compromised. That would be detrimental to the integrity of the judicial process.”⁴⁴

“The court relies upon practitioners to apply an independent and objective mind when conducting a case on behalf of the client. There is a risk (which seems to be accepted) that that objectivity might be compromised to some degree where there is a ‘no win no fee’ arrangement because of the fees which the practitioner may have at stake. However, the Observer would likely conclude that the more that is at stake, the greater the risk that the lawyer will not bring or will not be seen to be bringing to bear the requisite degree of objectivity that the role of lawyer demands. The Observer would form the view that Mr Elliott may be influenced by the substantial financial interest that rests on the outcome of the case. The addition of his financial interest in what the Litigation Funder may gain or lose (dependent upon the outcome of the case) means that the risk that he will be, or will be perceived to be, unable to apply the necessary independence required as an officer of the court is a real risk that cannot be ignored (emphasis added).”⁴⁵

Omni Bridgeway can identify several situations in which a conflict could arise to the detriment of group members. These include:

- When the economics of a case change and a legal firm facing disbursements (typically around 40-50 per cent of total costs) and adverse costs will be under pressure to settle, which may not be in clients’ interests;
- When a case is going well but the legal firm needs the cashflow for other reasons, so advises clients to settle; or
- When the legal firm, to save money on disbursements and ensure a greater return, chooses not to use the Bar, affecting the quality of representation for the client.

Professor Morabito explained the conflicts that can arise:

“The most persuasive criticism of contingency fee agreements is the potential for conflict of interest which they create in relation to such matters as settlement of the client’s claim. The contingent nature of the lawyer’s remuneration creates a strong financial incentive for the lawyer to ‘accept a small settlement in order to ensure some fees, rather than risk losing at trial and recovering nothing’. This incentive to settle for sub-optimal amounts would appear to exist in relation to both uplift fees and percentage fees.

“An obvious response to this argument is to say that a client would not accept settlement terms which are contrary to his/her own best interests. Unfortunately, the fear of losing, ‘the client information disadvantage and the inability to evaluate’ the validity of the settlement package recommended by the lawyer may result in the client’s authorisation of inferior recoveries.

“The losses incurred as a result of the conflicts of interest which exist between principals and agents are described by economic scholars as ‘agency costs’. Given the unreliability of ‘monitoring’ by the client as a means of reducing agency costs, reliance must be placed on other safeguards such as the legal regulatory system and the importance placed by lawyers on maintaining a good reputation.

⁴⁴ Ibid, at page 22.

⁴⁵ Ibid, at page 21.

*"It is difficult to see, however, how the prospect of disciplinary action or loss of reputation can provide an effective means of eliminating agency costs in the context of settlements given that the lawyers in question are able to point to the 'objective' fact that they have achieved a victory on behalf of their clients. Furthermore, as Macey and Miller have pointed out, the devices to reduce agency costs 'are themselves costly'."*⁴⁶

Omni Bridgeway considers it unlikely the introduction of contingency fees will result in small or medium-sized claims that are not currently funded being funded. If such cases are presently unattractive to commercial litigation funders, it is unlikely that they would become attractive to fund when it is the lawyers who are providing the funding. As a result, permitting contingency fees is unlikely to improve access to justice.

Law Council of Australia President Pauline Wright says:

*"In most jurisdictions in Australia a 'no win – no fee' arrangement is available that enables civil claims matters to be taken on for clients without deep pockets and matters that merit litigation in the public interest. Public interest cases would not benefit from the introduction of percentage-based fee agreements, and neither would low income matters. Percentage-based fee agreements would only benefit large law firms that are already billing via conditional fee arrangements – generating a higher premium with no commensurate increase in risk."*⁴⁷

Omni Bridgeway believes that unless lawyers working under a contingency fee arrangement are subject to the same financial obligations (and proposed regulation) as litigation funders – liability for adverse costs and the requirement to hold capital reserves or insurance to cover those costs – there is the risk of an increased appetite for class action litigation. (The proposed Victorian legislation would require lawyers working under a contingency fee arrangement to pay adverse costs but does not have a capital adequacy requirement.)

If contingency fees are ultimately permitted and the traditional role of the lawyer changes to becoming a funder, Omni Bridgeway believes the lawyers should be subject to the same or similar obligations as third-party funders. The proposed licensing regime for litigation funders – supported by Omni Bridgeway – could achieve this requirement if extended to law firms acting as funders.

Unless that occurs, the introduction of contingency fees may place unmanageable costs and financial obligations on law firms who seek to act as both litigator and funder. As outlined in our response to Question 1, in complex class actions, the upfront legal and project costs and the potential adverse cost orders, even with 'after the event' insurance cover, are prohibitive to all but the most financially robust funders.

If courts order that law firms acting as funders put up security for costs – as they do with litigation funders – the firms will have both financial obligations and legal obligations to the clients. In a worst-case scenario, those conflicts could become so significant that the firm would need to stand down from continuing to act as the class lawyers, with flow-on effects for group members.

One argument that is raised in favour of contingency fees is that their introduction would allow more lawyers to compete with litigation funders, resulting in a reduction in funding fees. However, the market for litigation funding in Australia is already competitive. In 2018 it was

⁴⁶ "Federal Class Actions, Contingency Fees, and the Rules Governing Litigation Costs" (1995) 21 Monash University Law Review 231, 246 – 247 (citations omitted).

⁴⁷ Law Council Media Release – 'Contingency Fees opposed by Law Council', 13 March 2020

estimated there were approximately 25 funders operating domestically.⁴⁸ Even if the Government's proposed licensing regime is introduced, there is nothing to suggest the litigation funding industry in Australia will not remain highly competitive.

(4) The financial and organisational relationship between litigation funders and lawyers acting for plaintiffs in funded litigation and whether these relationships have the capacity to impact on plaintiff lawyers' duties to their clients.

The strict separation between the funder and the lawyers in respect of funded litigation, as it currently stands, is the best approach for minimising, and if they arise effectively managing, any conflicts of interest and ensuring that the lawyers provide objective advice to applicants and group members.

Solicitors and counsel should not have any interest, direct or indirect, in any third-party litigation funder – domestic or foreign – that is providing funding for a matter in which they act, and should fully disclose all relationships they have or had with the funder, so as to enforce as complete a separation between the funded claimants' legal representatives and the funder as possible. This disclosure enables the client to make an informed decision on the question of funding and its risks and benefits.

The identification and management of conflicts of interest should be a subject for discussion between the funder, the claimant and the claimant's lawyer and should be addressed in the funding agreement.

ASIC's Regulatory Guide stipulates that litigation funders must have "adequate practices for managing a conflicts of interest" that may arise⁴⁹ and the Federal Court Class Action Practice Note makes it clear that any litigation funding agreement "should include provisions for managing conflicts of interest (including of 'duty and interest' and 'duty and duty') between any of the applicant(s), the class members, the applicant's legal representatives and any litigation funder".⁵⁰

The Note says:

*"The applicant's legal representatives have a continuing obligation to recognise and to manage properly any conflicts of interest throughout the proceeding."*⁵¹

The agreement should expressly recognise that the lawyer who has the conduct of the claim owes his or her full professional and fiduciary duties to the claimant. The agreement may also provide that, in the event of a conflict of interest between the claimant and the funder, the lawyer may continue to act solely for the claimant, even if the funder's interests are adversely affected by him or her doing so.

This standard should be observed whether the lawyer is retained by the funder or by the claimant.

In Omni Bridgeway's case, the LFA meets these obligations. The standard terms of our LFAs that relate managing conflicts of interest are:

Omni Bridgeway will give day-to-day instructions to the Lawyers on all matters concerning the Claims and the Proceedings, however the Claimant may, in relation to the Claimant's Claims,

⁴⁸ See the ALRC Final Report, page 29. As at December 2018, there were around 25 funders active in Australian litigation, including class actions. "These entities, both domestic and foreign, include publicly listed corporations, private companies, private equity firms, and hedge funds. Some retain significant capital on their balance sheets; others access capital in a variety

⁴⁹ Corporations Regulations 2001 (Cth), reg 7.6.01AB(2).

⁵⁰ Clause 5.9.

⁵¹ Clause 5.10.

override any instruction given by Omni Bridgeway by giving the Claimant's own instructions to the Lawyers.

Except in relation to Settlement, which is dealt with below, if the Lawyers notify Omni Bridgeway and the Claimant that the Lawyers believe that circumstances have arisen such that they may be in a position of conflict with respect to any obligations they owe to Omni Bridgeway and those they owe to the Claimant, the Claimant and Omni Bridgeway agree that, in order to resolve that conflict, the Lawyers may:

- 1.1.1 seek instructions from the Claimant, whose instructions will override those that may be given by Omni Bridgeway;*
- 1.1.2 give advice to the Claimant and take instructions from the Claimant, even though that advice is, and those instructions are, or may be, contrary to Omni Bridgeway's interests; and*
- 1.1.3 refrain from giving Omni Bridgeway advice and from acting on Omni Bridgeway's instructions, where that advice is, or those instructions are, or may be, contrary to the Claimant's interests.*

In addition, Omni Bridgeway has a comprehensive Conflicts Management Policy, available on our website.⁵²

(5) The Australian financial services regulatory regime and its application to litigation funding;

Omni Bridgeway has long supported the introduction of a licensing regime for all litigation funders operating in Australia, most recently in its ASX announcements of 14 May and 22 May 2020. The company supports the proposal put forward by the Treasurer, the Hon. Josh Frydenberg MP, that all litigation funders operating in Australia obtain an Australian Financial Services Licence (AFSL) and conduct future class actions in compliance with a managed investment scheme (MIS) regime with appropriate modifications to make it fit for the purpose of applying to funded class actions.

Omni Bridgeway (then known as IMF Bentham) applied for and obtained an AFSL in 2005, believing at that time that litigation funding could be a financial product. Once it became clear that it was exempt from a licensing requirement, the company gave up its licence in April 2013 but continued to comply with the current regulations overseen by ASIC.

This regulatory model places a light compliance burden on litigation funders and poses minimal regulatory barriers to entry. In Omni Bridgeway's view, a difficulty with this 'light touch' approach is that there is no capital adequacy standard to guard against the risk of an under-capitalised funder failing to meet its financial obligations.

Third-party funding arrangements generally include obligations to pay significant sums. Prudential regulation would ensure those promises can be met and would offer valuable consumer protections, particularly where the funder is foreign-based or a private company (as opposed to an ASX-listed funder where regular financial information about the funding entity is public).

Omni Bridgeway considers that only a handful of funders operating in Australia have the capacity to fund large complex actions, including class actions.

⁵² Available to download from the [IMF website](#)

In its submission to the ALRC inquiry, ASIC questioned the merits of a licensing regime for litigation funders, stating: “We consider the courts are better placed to regulate litigation funders, through court rules and procedure, oversight and security for costs.”⁵³

It added: “A requirement that a litigation funder obtain an AFS licence will not of itself mean that the funder will be adequately capitalised to meet adverse costs orders, continue to fund litigation or distribute funds to shareholders.”⁵⁴

Omni Bridgeway believes a licensing regime that includes minimum onshore capital adequacy requirements, disclosure obligations and reporting standards would increase confidence in the Australian class actions system and reduce the incidence of rush to court actions.

Omni Bridgeway intends to reapply for an AFSL and will comply with the requirements of the MIS regime. We look forward to consultation with ASIC on the structure of the licensing regime and how they MIS regime will apply to funded class actions in the future.

The application of the MIS regime to class action litigation funding arrangements will need to be very carefully considered to ensure it is workable. Many of the concepts do not apply well to funded class actions. The typical concerns of the MIS regime are protecting other people’s money, whereas in a class action it is the funder’s money that is at risk. This begs the question as to what is the “scheme property”. The answer is critical to the proper discharge of obligations on the responsible entity, such as to take appropriate care of the scheme property, to value it and for audits to be conducted.

Other issues arise concerning the management of conflicts and accommodating the bespoke procedures of class actions, including rights to opt out, the court settlement approval process and the fact that the class action only determines issues common to the class, not all of the claims of group members, unless settled. Substantial modification may be required to avoid unintended consequences and confusion.

Omni Bridgeway cautions strongly against the retrospective application of the MIS regime to current class actions. Such a measure would throw in doubt the status of all existing class actions⁵⁵, creating significant uncertainty, disruption and possible delays for thousands of groups members, some of whom are involved in matters that have already been the subject of years of court proceedings. (Approximately 6700 victims of the Wivenhoe Dam mismanagement in 2011, for example, first filed their class action six years ago.)

One parallel, discussed in our response to Question 10, was the material uncertainty created by the Federal Court’s *Multiplex* decision in 2009, which required the Australian Securities and Investments Commission to grant interim relief to funded class action that would have been required to be registered as managed investment schemes under the *Corporation Act 2001*.

Recommendations: *Introduce a licensing regime for litigation funders that would include minimum onshore capital adequacy requirements, disclosure obligations and reporting standards – complementing existing regulations related to conflicts. Apply the managed investment scheme regime to future funded class actions in Australia, with appropriate modifications*

(6) The regulation and oversight of the litigation funding industry and litigation funding agreements.

⁵³ ASIC, “Australian Law Reform Commission Inquiry into class action proceedings and third-party litigation funders: Submission by the Australian Securities and Investment Commission”, September 2018 (**ASIC Submission**), at [76].

⁵⁴ Ibid, page 14.

⁵⁵ As at 26 May 2020: 96 current Representative Proceedings in the Federal Court nationally (plus 11 associated/related cases) - <https://www.fedcourt.gov.au/law-and-practice/class-actions/class-actions#statistics>

As detailed in our responses to Questions 3 and 4, Omni Bridgeway believes there is significant oversight of litigation funding through the existing Corporations regulations, the courts and the checks and balances outlined in our response to Question 1.

As stated in our response to Question 5, Omni Bridgeway supports a licensing regime for litigation funders operating in Australia and the application of the managed investment scheme regime to future funded class actions, with appropriate modifications.

(7) The application of common fund orders and similar arrangements in class actions.

Since the Federal Court's *Multiplex* decision in 2009 and prior to the *Money Max* decision in 2016, most funded class actions in Australia were 'closed', or opt-in, class actions⁵⁶.

Closed class actions require a process known as 'book building' to be undertaken at the outset of the action. This involves identification of class members, making contact, raising awareness and enrolling class members in the action. This process can be expensive and time-consuming but can ensure only class actions with genuine support and prospects for success go ahead.

The closed class system enabled Omni Bridgeway to return more than \$1 billion to class members before Australian courts began making CFOs.

The *Money Max* case was the first in which an order was made that enabled a litigation funder to collect a commission from all class members in an 'open' class and not only from those who had entered into a litigation funding agreement with the funder. As predicted at the time of the decision, this produced a rush to file class actions by law firms supported by litigation funders who could secure a CFO to ensure commissions from all class members, regardless of whether they signed an LFA. This is a valid criticism.

Just three years after the *Money Max* decision, the use of CFOs in class actions is in doubt. In December 2019, the High Court ruled in *BMW Australia v Brewster* and *Westpac Banking Corp v Lenthall* that neither the Federal Court nor the Supreme Court of NSW have the power to make CFOs, at least at the early stages of the proceedings.⁵⁷

The decision recognised that it remains open to a court to make a funding equalisation order (FEO) at the end of the case, which is an order redistributing costs and funder's fees from funded group members to all group members.

While Omni Bridgeway had hoped that the High Court's pronouncements would provide much-needed clarity about the court's role and ability to make CFOs, it is now apparent that legislative intervention is required to clearly demarcate the bounds of the courts' power as the jurisprudence surrounding CFOs is, with respect, still uncertain.

In *Brewster*, the High Court was critical of CFOs being used as a mechanism to bypass the book-building processes to ensure the financial viability of a proposed class action, stating that:

*"It is not appropriate or necessary to ensure that justice is done in a representative proceeding for a court to promote the prosecution of the proceeding in order to enable it to be heard and determined by that court. The making of an order at the outset of a representative proceeding, in order to assure a potential funder of the litigation of a sufficient level of return upon its investment to secure its support for the proceeding, is beyond the purpose of the legislation."*⁵⁸

⁵⁶ Cases that started as closed class actions were often opened and then closed in advance of settlement discussions to facilitate an outcome and provide finality for a defendant.

⁵⁷ *BMW Australia Ltd v Brewster* [2019] HCA 45.

⁵⁸ *Brewster*, at [3] per Kiefel CJ, Bell and Keane JJ.

However, the court left open the prospect of applying a CFO, or similar cost-sharing orders, at the conclusion of a proceeding:

*"[I]f the group members happen to be indebted to a litigation funder for its support of their claims, the value of the litigation funder's support to the group members will be capable of assessment and due recognition. That stage is the appropriate occasion for orders for meeting and sharing the cost burden of the litigation because the value of the litigation and the extent of the burden will have been rendered certain."*⁵⁹

Two weeks after the *Brewster* decision, the Federal Court signalled its willingness to continue to make CFOs or similar orders. On 20 December 2019, the Federal Court amended its Class Actions Practice Note to include the following passage:

*'Particularly in an open class action, the parties, class members, litigation funders and lawyers may expect that unless a judge indicates to the contrary the Court will, if application is made and if in all the circumstances it is fair, just, equitable and in accordance with principle, make an appropriately framed order to prevent unjust enrichment and equitably and fairly to distribute the burden of reasonable legal costs, fees and other expenses, including reasonable litigation funding charges or commission, amongst all persons who have benefited from the action. The notices provided to class members should bring this to their attention as early in the proceeding as practicable.'*⁶⁰

Since that time, and despite the updated Class Actions Practice Note, a divergence of views has emerged within the Federal Court as to whether the Court is empowered to make CFOs at the conclusion of proceedings, if at all.

In the *Vocus* class action, Justice Moshinsky said the High Court had not expressed a concluded view as to whether there was no power for the Court under section 33V of the *Federal Court Act 1976* to make a CFO.⁶¹ However, in approving the settlement, he declined to make a CFO, preferring instead to make a FEO because:⁶²

- (a) the CFO imposed an additional cost on the group by requiring more money to be paid to the litigation funder than would otherwise be the case;
- (b) the CFO proposal went further than was necessary to address the problem of 'free riding', whereas the FEO proposal sufficiently ensured that unfunded group members who obtained the benefit of the litigation contributed to the cost of the proceeding; and
- (c) the funder's risk was adequately recognised in the FEO proposal.

In *Uren v RMBL Investments Ltd*, Justice Murphy said the *Brewster* decision did not deny the Court the power to make a CFO when approving a settlement.⁶³ In approving the CFO, Justice Murphy was satisfied that it was "just" pursuant to the Act to order that 25 per cent of the gross settlement be distributed to the litigation funder, "so as to fairly and equitably distribute the burden of litigation funding expenses amongst all persons who have benefited from the action, and so as to avoid the unjust enrichment of the class member".⁶⁴

On the same day, Justice Foster declined to make a CFO at the conclusion of the *Volkswagen* class action and expressed his doubts as to whether the Court was empowered to make a CFO at any stage of the proceedings.⁶⁵

⁵⁹ *Brewster*, at [68] per Kiefel CJ, Bell and Keane JJ.

⁶⁰ Class Actions Practice Note (GPN-CA), paragraph 15.4.

⁶¹ *Fisher (trustee for the Tramik Super Fund Trust) v Vocus Group Limited (no 2)* [2020] FCA 579 at [72].

⁶² *Ibid*, at [74].

⁶³ *Uren v RMBL Investments Ltd (No 2)* [2020] FCA 647 at [52].

⁶⁴ *Ibid*, at [48].

⁶⁵ *Cantor v Audi Australia Pty Ltd (No 5)* [2020] FCA 637 at [418].

Omni Bridgeway believes this multiplicity of views will foster uncertainty and warrants legislative intervention. Omni Bridgeway supports the prohibition of CFOs so as to ensure that only funded class actions that are genuinely supported by enough engaged claimants, rather than funders or lawyers alone, are commenced.

Omni Bridgeway believes that the closed class system – restricted to those who sign a funding agreement – has several benefits over open class actions with CFOs, including that a closed class action:

- Demonstrates that a class action is supported by actual group members and is not merely a speculative endeavour by a litigation funder or entrepreneurial lawyers;
- Enables the litigation funder to determine whether it is commercially viable to fund the action. If there is insufficient group interest, the action will not proceed, consistent with the overarching purpose of not using the court's time to achieve an outcome that group members are not interested in participating in;
- Provides the group members with an avenue to express their preference for a particular funder, lawyer or case theory;
- Enables the funder and lawyers to gather information relevant to the claim, including the individual circumstances of group members;
- Enables feedback to be received from group members on prices and for individual terms to be negotiated and fashioned to address specific circumstances; and
- Enables settlements discussions to subsequently occur on the basis that:
 - The represented group represents the bulk of those interested in pursuing the case (opt-outs will be small or non-existent);
 - It is unlikely that there will be significant additional people who have not already signed a funding agreement wishing to participate in any settlement;
 - An estimate can be made of total claim size, both for the funded members and for unfunded members if the class is opened and then closed for settlement purposes. This promotes certainty and efficiency and maximises the prospects of reaching a settlement.

The Victorian proposal to introduce contingency fees (discussed in our response to Questions 3 and 4) would encourage a similar process to the use of CFOs in open class actions – the ability of law firms to launch proceedings without having conducted a book-building exercise to determine genuine support for a class action. This is one of the major reasons why contingency fees should be discouraged.

A fit-for-purpose MIS regime that could be applied to future funded class actions, as proposed by the Commonwealth Government, would also discourage open class actions.

While we are not opposed to open class actions, the use of CFOs in open class actions has had unintended adverse consequences. We would support a return to the pre-2016 system that encouraged funded closed actions, ensuring only those funded class actions genuinely supported by claimants proceed, but also permitted open class actions.

Further, amendments to Section 177 of the Corporations Act to allow access to share registers for the purpose of alerting shareholders to their status as potential class action members would help ensure that all members have the opportunity to vindicate their legal rights through the class action system.⁶⁶

Recommendation: Introduce legislation to end the use of common fund orders and prevent the introduction of contingency fees for lawyers.

⁶⁶ *IMF (Australia) Ltd v Sons of Gwalia Ltd (admin apptd)* (CAN 008 994 287) [2005] FCAFC 75.

(8) Factors driving the increasing prevalence of class action proceedings in Australia.

Research by Professor Morabito has found that, while the number of class actions in Australia was steadily increasing, it could not be quantified as an “explosion” as has been reported by critics of litigation funding.

Professor Morabito found that in the 10-year period starting on 1 January 2000 and ending on 31 December 2009, a total of 139 class actions were filed in the Federal Court.⁶⁷ Over the following 10 years, a total of 235 federal class actions were filed.⁶⁸ This is an increase of 69 per cent from an average of 13.9 per year to 23.5 per year.⁶⁹

He found that in only four calendar years were there more than 30 federal class actions and two of these calendar years were in the pre-litigation funding era.⁷⁰ And, importantly, “the upward trend that occurred in the period from 2015 to 2018 came to an end in 2019”.⁷¹

Professor Morabito also looked at the statistics for all class actions, including those brought on behalf of shareholders, consumers, employees and victims of events such as the mismanagement of Wivenhoe Dam in 2011 and the systemic underpayment of employees.

He says comparisons with previous periods are difficult because the number of courts handling class actions has expanded in the past 10 years from just the Federal Court and the Supreme Court of Victoria to include the Supreme Courts of NSW, Queensland and Tasmania.⁷²

In total, there have been 634 class actions filed federally and in Victoria, NSW and Queensland since 1992, when the class action regime came into being through the enactment of Part IVA of the *Federal Court of Australia Act*.⁷³ Professor Morabito found that there were 59 class actions filed in 2018-19 – just three more than the previous year and 15 more than in 2014-15.⁷⁴

In comparison, in Israel, a country with a population approximately one-third the size of Australia’s, there were 5,687 class actions between 2007 and 2015.⁷⁵

Professor Morabito concluded that “no balanced or objective assessment of Australia’s class action landscape could possibly lead to the conclusion that there has been an explosion of class actions in recent years”.⁷⁶

Professor Morabito also finds a “significant downwards trend” in class actions funded by litigation funders:

“In 2017, 69 per cent of Australia’s class actions were funded and in 2018, this percentage went down to 65 per cent. In 2019, 50 per cent of Australian class actions were funded whilst 38 per cent of the class actions filed in 2020, up to and including 15 May 2020, were supported by litigation funders.”⁷⁷

In terms of shareholder class actions, Professor Morabito identified 122 since 1992.⁷⁸ He found that since that time only 63 companies or group of companies have had class actions filed

⁶⁷ Above n38, at page 3.

⁶⁸ Ibid.

⁶⁹ Ibid.

⁷⁰ Ibid.

⁷¹ Ibid.

⁷² Ibid.

⁷³ Professor Vince Morabito, “Shareholder class actions in Australia – myths v facts”, November 2019, at page 12.

⁷⁴ Ibid, page 12.

⁷⁵ Ibid, page 13.

⁷⁶ Ibid, page 14.

⁷⁷ Above n38, page 4.

⁷⁸ Above n73, page 15.

against them on behalf of shareholders.⁷⁹ This compares with the estimated 2200 companies listed on the ASX.

Professor Morabito says:

"The shareholders of 34 companies or groups of companies filed class actions in the period from 1 July 2014 to 30 July 2019. That provides an annual average of 6.6 companies or groups of companies whose shareholders resorted to the class action device.

"In light of the information provided above, it can be confidently concluded that there has been no explosion of shareholder class actions in Australia either over the last 27 years or so or in recent years."⁸⁰

Professor Morabito also finds that shareholder class actions are declining as a proportion of total class actions.

"In the 2016-2017 financial year shareholder class actions constituted 44.7% of all the class actions filed in Australia in those 12 months. This percentage went down to 42.8% in the following 12 months and 32.2% in the last financial year."⁸¹

There are a number of factors behind the steady increase in class actions:

The overall increase in the size and sophistication of the Australian economy and Australian financial markets. As recognised by ASIC⁸² and other regulators, class actions can play a complementary role in ensuring the fair and efficient operation of financial markets. Securities class actions are not just supported by 'mum and dad' investors but by sophisticated institutional investors, including Australian superannuation funds and government-backed investment vehicles.

The Money Max decision that endorsed the use of common fund orders, encouraging 'open' class actions and reducing the barriers for filing class actions. This decision is partly responsible for an increase in the number of litigation funders operating in Australia, including foreign-based funders.⁸³ This has led to an increase in capital available to fund class actions, as well as competing class actions, in which separate law firms, each with a different litigation funder, begin proceedings against the same defendant for the same or similar sets of claims.

Well-publicised issues and examples of misconduct in corporate Australia, such as the banks' treatment of their customers, as exposed by the Hayne Royal Commission, the systematic underpayment of employees by some of Australia's biggest companies and the flammable cladding scandal. Professor Morabito notes the "numerous instances of misconduct" exposed by the *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry*. "A failure to bring class action proceedings on behalf at least some of the victims of these identified instances of misconduct would have raised legitimate questions as to the effectiveness of our class action regimes," he writes.

An increase in the number of related and competing class actions filed against one party, caused in part by the availability of CFOs in open class actions. Professor Morabito found that one third of all class actions filed in Australia as at 30 June 2019 were duplicates – "legal disputes that prompted the filing of other class actions either by the same solicitors (related class actions) or by other solicitors (competing class actions)". The 115 class actions filed in the past two years concern only 82 distinct legal disputes. For example, Quinn Emanuel Urquhart & Sullivan filed

⁷⁹ Ibid, page 16.

⁸⁰ Ibid, page 16.

⁸¹ Above n73, page 16.

⁸² ASIC Submission, at [47].

⁸³ In 2018 it was estimated there were approximately 25 funders operating domestically.

seven class actions in relation to dangerous airbags in cars. It is highly likely that a return to bookbuilding will reduce, if not eradicate, multiple class actions against the same defendant based on the same or similar claims.

An increase in the activity of law firms seeking to identify opportunities to be funded or to fund actions themselves. This situation would be exacerbated by the introduction of contingency fees.

(9) What evidence is becoming available with respect to the present and potential future impact of class actions on the Australian economy?

There is no credible, independent evidence that class actions are having a negative impact on the Australian economy. The evidence that does exist is strongly to the contrary.

In fact, it is acknowledged that class actions, by complementing action by regulators to enforce Australia's robust continuous disclosure regime, contribute to the integrity of the nation's financial markets, making them an attractive source of capital for Australian and international companies.

In its submission to the ALRC, ASIC said:

*"The continuous disclosure obligations are critical to protecting shareholders, promoting market integrity and maintaining the good reputation of Australia's financial markets The economic significance of fair and efficient capital markets dwarfs any exposure to class action damages."*⁸⁴

And:

*"Where private action can achieve a similar outcome to that which action by ASIC could achieve, it allows ASIC to allocate its enforcement resources to other priorities. Shareholder class actions provide a number of benefits to consumers and financial markets and play an important role in improving shareholder access to justice."*⁸⁵

As noted above, Professor Morabito's research found that the shareholders of only 34 companies filed class actions in the period from 1 July 2014 to 30 July 2019.

Professor Morabito found that total recoveries in all shareholder class actions since 1992 were \$889 million on behalf of 94,984 shareholders. These recoveries compared with the current capitalisation of the 2200 companies listed on the ASX of approximately \$1.7 trillion.

It is not credible to suggest, therefore, that class actions are causing economic damage to long-term shareholders, diverting company resources from investment opportunities to pay legal costs and distracting boards from their core duties.

Effect on insurance premiums

There is no doubt that there has been an increase in the cost of directors' and officers' (D&O) liability insurance, which has placed a burden on some particularly smaller companies, and the number of class actions is a factor.

However, there are other factors driving in the increase, including a correction to years of "chronic under-pricing"⁸⁶, global trends in the commercial insurance market (including in markets where securities class actions cannot be considered the primary driver) and evidence of

⁸⁴ ASIC Submission, at [4].

⁸⁵ Ibid, at [47].

⁸⁶ XL Catlin / Wotton + Kearney white paper, "Show me the money", September 2017, at page 15.

corporate wrongdoing, which increases the risk of regulatory and legal action against companies and directors and, as a result, increases insurance premiums.

One of the outcomes of the Hayne Royal Commission's findings was that ASIC would take a 'why not litigate?' approach to regulation of the financial services law. In January 2019, the findings of the Hayne Royal Commission were said to be the cause of "*pushing up already rocketing D&O premiums – doubling the cost on average – and increasing the excess payable by several times.*"⁸⁷

*"The fallout from the (Royal Commission) has increased premiums for professional indemnity insurance up to 400 per cent and prompted some insurers to exit that segment of the market altogether."*⁸⁸

XL Catlin and Wotton + Kearney in a joint white paper concluded that a principal driver of the sustained and growing unprofitability of the D&O market in Australia is the "*chronic under-pricing of ABC D&O business by insurers since at least 2011*".⁸⁹

In evidence presented to the ALRC review, Norton Rose Fulbright noted the tripling in D&O insurance premiums between 2011 and 2018 and concurred that it was "an overdue and necessary reaction to the realities of the Australian market".⁹⁰

The ALRC Final Report says:

*"Despite the concerns of insurers and brokers, Norton Rose Fulbright argued that 'there is presently no evidence to suggest that insurance is unaffordable or that there is a material underinsurance risk requiring policy intervention'. They expressed the view that: the recent increase in premiums for D&O cover is an overdue and necessary reaction to the realities of the Australian market. We also consider that the increase in pricing is one which the market can and will absorb."*⁹¹

The Australian experience is not unique. The Marsh *Global Insurance Market Index* has tracked rising commercial insurance premiums worldwide in the past year. It found financial and professional liability insurance, including D&O, rose 23 per cent in the first quarter of calendar 2020 in the US, 46 per cent in the UK, 12 per cent in Continental Europe and 33 per cent in the Pacific, including Australia.⁹²

It is also worth noting that D&O liability insurance policies do not just cover class actions but respond to a wide range of single and multi-party claims against directors and officers of a company.

Directors and officers of companies in Australia are subject to common law and statutory duties and they face a range of claims giving rise to civil and criminal liability for breaching those duties. Directors and officers may incur civil liability for damages or civil penalties to many parties, including their company, another director or officer of the company, a shareholder, employee, creditor or customers of the company or a regulator. The amount of these civil liabilities can be millions of dollars. Directors and officers may also be liable to pay a significant amount in criminal fines and penalties.⁹³

⁸⁷ <https://www.afr.com/companies/financial-services/royal-commission-fears-spark-mass-insurance-exclusions-20190102-h19mz1>

⁸⁸ Ibid

⁸⁹ XL Catlin / Wotton + Kearney white paper, "*Show me the money*", September 2017, at page 15.

⁹⁰ Norton Rose Fulbright, "*Submission to the ALRC: Inquiry into Class Action Proceedings and Third Party Litigation Funding*", July 2018, at page 9.

⁹¹ ALRC Final Report, at [9.86].

⁹² Marsh, *Insights: Global Insurance Prices Continue to Rise for Tenth Consecutive Quarter*, May 2020

⁹³ Directors' and officers' liability insurance in Australia, Practical Law Dispute Resolution.

As such, the price of D&O liability insurance reflects this multitude of claims faced by directors and officers as well as the significant costs incurred in the defence of such claims. In fact, class actions rarely target directors.

Professor Morabito's research found that:

"in just over three out of every four shareholder class actions no action was taken against the individual directors".

*"This practice has become even more prevalent in recent times. For instance, in only 10% of the shareholder class actions filed in the 2018-2019 financial year were directors included among the respondents/defendants."*⁹⁴

The reality is that the increase in the cost of D&O liability insurance is indicative of the extent of the wrongdoing, which historically companies have been reluctant to attempt to defend at trial. The appropriate response to increasing evidence of breaches of the law causing losses to Australian investors is not to curtail their ability to access the law, especially at the behest of insurers. The profitability of D&O liability insurance would increase if there was broader compliance with the continuous disclosure laws.

(10)The effect of unilateral legislative and regulatory changes to class action procedure and litigation funding.

The most notable example of a unilateral change that fundamentally affected the class action and litigation funding system followed the Federal Court's ruling in *Multiplex* that funded class actions should be registered under the MIS regime.

In 2010, then minister for corporate law Chris Bowen reversed the effect of the Federal Court's decision and instead tasked ASIC with establishing a compliance code for litigation funders via regulation.

The decision was made after extensive consultation – and was hailed at the time as a victory for common sense⁹⁵ and access to justice⁹⁶.

For this reason, any legislative or regulatory proposal with the potential to impact the class action system must be the subject of significant consultation and scrutiny through the parliament or other appropriate processes to test any unintended consequences and ensure the regime is workable. (This has been covered in our response to Question 5.)

In this submission, Omni Bridgeway has made several recommendations that would require legislative or regulatory intervention by government.

In Omni Bridgeway's view, for example, more clarity is needed on issues such as the use of CFOs and contingency fees and reasonable returns to group members.

Without clear legislative guidance, courts have been required to determine the rules of the class action system, with several recent decisions, including *Money Max*, fundamentally altering the behaviour of participants in and the conduct of class actions.

Ongoing uncertainty over the court's treatment of issues, such as funding orders, increases risks for funders and can lead to higher costs for plaintiffs – underlining the need for legislative or regulatory intervention.

⁹⁴ Professor Vince Morabito, *Shareholder class actions in Australia – myths v facts*, November 2019, at page 20.

⁹⁵ <https://www.abc.net.au/pm/content/2010/s2892454.htm>

⁹⁶ <https://ministers.treasury.gov.au/ministers/chris-bowen-2009/media-releases/government-acts-ensure-access-justice-class-action-member>

However, we would caution against any unilateral action by government and, in particular, against action that is confined to a single jurisdiction.

If the Commonwealth Government enacts changes to class action procedure and the litigation funding regime, it is critical those changes are adopted nationally to reduce complexity and prevent forum shopping.

The Victorian Government proposal to introduction contingency fees risks creating the most class-action friendly jurisdiction in Australia. It could encourage forum shopping and could prompt other states to introduction similar legislation, further complicating a complex court system.

Different rules between the Commonwealth and the states may also give rise to more circumstances in which “competing” class actions are filed in both federal and state courts.

Legislating to give the Federal Court exclusive jurisdiction over class actions related to federal laws, such as the Corporations Law, would help eliminate these risks. In the case of actions by shareholders against companies, this would provide greater certainty to and protections for corporate Australia.

Such legislation would also recognise – and fully utilise – the significant expertise in class action law that has been accumulated on the Federal Court bench.

Recommendation: *Introduce legislation to give the Federal Court exclusive jurisdiction over securities class actions and actions involving Federal law.*

(11) The consequences of allowing Australian lawyers to enter into contingency fee agreements or a court to make a costs order based on the percentage of any judgment or settlement.

See responses to Questions 3 and 4.

(12) The potential impact of Australia’s current class action industry on vulnerable Australian business already suffering the impacts of the COVID-19 pandemic.

COVID-19 and the efforts of governments worldwide to contain the pandemic, particularly through economic and social lockdowns, have had a profound impact on the community. Many companies, not just those in heavily exposed sectors such as travel and tourism, have suffered immediate and in some cases, permanent financial damage.

Omni Bridgeway itself has been required to dramatically change workplace practices, review all non-essential travel, spending and reassess its work program.

We are sympathetic to the concerns expressed by the Committee about the impact on vulnerable Australian businesses. ASX-listed companies, with their continuous disclosure obligations, are facing unique challenges in terms of keeping the market informed while having limited ability to accurately predict future economic and trading conditions. Nevertheless, companies can choose not to make forward-looking statements.

Omni Bridgeway notes the Compliance Update issued by the ASX on 31 March 2020, in which it acknowledged “the particular disclosure challenges for listed entities arising from the rapidly evolving and highly uncertain situation surrounding the coronavirus pandemic and that different listed entities are being affected in different ways by COVID-19”.⁹⁷

“ASX does not expect listed entities to announce information under listing rule 3.1 that comprises matters of supposition or that is insufficiently definite to warrant disclosure and

⁹⁷ [Listed@ASC Compliance Update](#)

that otherwise meets the requirements of all three limbs of listing rule 3.1A ... Nor does ASX expect listed entities to make forward-looking statements to the market unless they have a clear and reasonable basis for doing so."

As Omni Bridgeway expressed in its ASX announcements of 14 May and 22 May 2020, we support the introduction of a six-month moratorium, starting in May, on new Australian class actions that are associated with COVID-19-related disclosures. This is not to condone misbehaviour at the cost of others but to provide companies, directors and individuals with a period to manage the pandemic.

As discussed in the introduction to the submission, Omni Bridgeway has not funded any Australian securities class actions that have been commenced in the past 12 months.

Omni Bridgeway confirmed in its ASX announcement of 30 April 2020 that it had experienced an increase in volume of funding applications since the onset of the COVID-19 pandemic across all global markets. It is important to note that only one of these applications related to a potential COVID-19-related class actions. The balance related to the other services that Omni Bridgeway can provide to help companies manage their cashflows and liquidity, including support for existing litigation with the potential to deliver returns.

Recommendation: *Introduce a six-month moratorium, starting in May 2020, on new class actions that are associated with COVID-19-related disclosures.*

(13) Evidence of any other developments in Australia's rapidly evolving class action industry since the Australian Law Reform Commission's inquiry into class action proceedings and third-party litigation funders.

The most significant recent development in relation to funded class actions was the High Court decision on CFOs in December 2019, in which a majority of the court held that neither the Federal Court of Australia nor the Supreme Court of New South Wales have the power to make a CFO, at least not in the early stages of litigation.⁹⁸

As discussed in the response to Question 7, since that decision, there has been a divergence of views as to whether the Court is empowered to make CFOs at the conclusion of proceedings, if at all. It is Omni Bridgeway's position that this multiplicity of views will foster uncertainty and warrants legislative intervention.

Omni Bridgeway supports the prohibition of CFOs to help ensure that only funded class actions that are genuinely supported by enough engaged claimants, rather than funders or lawyers alone, are commenced.

As discussed above at Question 2, in November 2019, Justice Beach of the Federal Court found that Myer had misled shareholders over its profit forecasts but ruled they had not suffered any loss and ordered both sides to pay their own costs, estimated at more than \$10 million each in legal fees alone. This was one of the first shareholder class actions in Australia to reach judgement. This has had the effect of increasing the risks for plaintiffs and litigation funders in taking on shareholder class actions.

On 22 May 2020, the Treasurer, Mr Frydenberg, announced the proposed introduction of a licensing regime for litigation funders and said class actions would need to be conducted in compliance with the MIS regime. Subject to the comments made above in response to Question 5, Omni Bridgeway supports these proposals and looks forward to consultation with the Government and ASIC on these changes.

⁹⁸ *BMW Australia Ltd v Brewster and Westpac Banking Corporation v Lenthall* [2019] HCA 45. (Omni Bridgeway did not fund any of the parties in these actions.)

On 26 May 2020, Mr Frydenberg announced changes to the Corporations Act to provide companies with limited protections from class actions for a period of six months (discussed in our response to Question 12).

(14) Any matters related to these terms of reference.

Class actions, with the financial support of third-party litigation funders, are an essential component of Australia's legal framework. They keep corporates and government accountable, complement the actions of regulators, and provide access to justice for Australians who may lack the means, understanding or confidence to engage in the legal system⁹⁹.

Omni Bridgeway has long supported additional regulation of litigation funding, however any new regime must be prospective and must be carefully designed to avoid jeopardising the availability of litigation funding for the people it seeks to protect – ordinary Australians seeking access to justice.

The logical outcome of regulation that fatally undermines the litigation funding model as it pertains to class actions is either no actions or hundreds of individual actions – the very situation the designers of the original class action system were seeking to eliminate for the good of plaintiffs, defendants and the courts.

⁹⁹ For example, providing access to justice for the approximately 6700 group members of the 2011 Brisbane floods class action.