

Federal Court guidance on class action funding commissions

Summary

- **Federal Court outlines why a 25% funding commission which produced a 5.02x or 502%¹ return on invested capital (ROIC) was fair and reasonable.**
- **Reaffirmation that hindsight bias is to be avoided when assessing the risks taken by a litigation funder in funding a particular case.**
- **Confirmation that in considering the reasonableness of a commercial litigation funder's commission, a portfolio approach, taking into account the variability of returns over time, is relevant.**

Background and Context of Parliamentary Inquiry

Omni Bridgeway Limited (**Omni Bridgeway**) refers to its previous announcement dated 20 December 2019 regarding the approval by the Federal Court of Australia (**Court**) of the settlement in the securities class action against members of the Murray Goulburn group of companies (**Murray Goulburn Case**).

The Court published its reasons for judgment on 9 July 2020² which include some significant findings concerning the range of factors to be taken into account when determining whether a funding commission is within a fair and reasonable range. This judgment is timely, in the context of the Parliamentary Joint Committee on Corporations and Financial Services inquiry into litigation funding and the regulation of the class actions industry (**Inquiry**), given the terms of reference include a consideration of the impact of the fees paid to litigation funders in class actions.

Relevance of a portfolio approach

Justice Murphy in the Murray Goulburn Case ultimately determined that a commission rate which delivered a ROIC of 5.02x or 502% (which was greater than the return Omni Bridgeway ended up receiving – see footnote below) was within the fair and reasonable range. In arriving at this conclusion, Justice Murphy noted that it was appropriate to take into account the average rate of return a commercial litigation funder achieves on cases when determining the fairness of a

¹ Omni Bridgeway's announcement dated 20 December 2019 stated the ROIC on a cash basis was 3.43x. The reason for this reduction when compared to the ROIC of 5.02x referred to by Justice Murphy is due to the final costs figure having increased between the date of submission of evidence for the settlement hearing and the investment concluding. This increase in costs naturally reduced the investment profit on a dollar for dollar basis.

² *Endeavour River Pty Ltd v MG Responsible Entity Limited (No 2)* [2020] FCA 968

commission rate in a particular case. When commenting on Omni Bridgeway's long-term ROIC across its investment portfolio, Justice Murphy noted:

"Further, over the period from post August 2001 to November 2019 while [Omni Bridgeway] achieved high rates of return in some shareholder class actions and lesser or poor rates of return in others, over time it achieved an average rate of return which I would not describe as excessive or unreasonable. That is, the good results for [Omni Bridgeway] were balanced by some poor results.... I doubt that anybody would argue that a rate of return of 1.3 times or 130% is excessive in a risky, illiquid and essentially unsecured investment class like litigation funding"

Relationship between long term average return and the commission in question

The Court noted that the Omni Bridgeway ROIC in the Murray Goulburn case was approximately four-times greater than the company's long term global average ROIC of 130%. In analysing whether this was nonetheless fair and reasonable in the circumstances, the Court identified that the case settled at the upper end of the potential settlement range and at a time when legal expenditure was considerably lower than the full envisaged budget and that this "drove the rate of return". Further, Justice Murphy stated that:

"A competent litigation funder operating in a competitive market will price the risk it takes on in a particular case having regard to the knowledge that returns are variable between cases, with good, intermediate and bad results, including outright losses, to be expected over time."

Having taken the above context into account, the Court further outlined its reasons for considering the funding commission to be fair and reasonable, stating:

"A funding rate of 25% which provides a return of 502% may also be argued to be too high. The evidence however shows that the case faced risks of liability, and a risk that the quantum of any settlement or judgment would not be sufficient to justify the expense and risk of the proceeding and yet provide class members with a reasonable level of recovery. [Omni Bridgeway] took on the case... with budgeted legal costs of \$6.26 million and an exposure to substantial adverse costs....hindsight bias must be avoided, and [Omni Bridgeway] took on risks when the outcome on liability and quantum was uncertain "

Justice Murphy endorsed the Court's previous view that "the approval of funding commission rates should not become a 'race to the bottom' and noted that funding commission rates should provide an appropriate reward for the risk undertaken by a litigation funder".

In concluding his judgment, Justice Murphy cited the Full Federal Court decision in *Money Max* noting the courts:

"will approve funding commission rates that avoid excessive or disproportionate charges to class members but which recognise the important role of litigation funding in providing access to justice, are commercially realistic and properly reflect the costs and risks taken by the funder and which avoid hindsight bias"

Relevance of the case to the Inquiry

The Murray Goulburn Case demonstrates the protections afforded to group members under the existing class action system when the Federal Court is tasked with approving a settlement and

the associated return to the litigation funder. Justice Murphy appointed a contradictor to represent the interests of class members in relation to the funding commission issues and reduced, with the consent of Omni Bridgeway, the contractual funding commission entitlement by an amount of almost \$3 million.

This judgment of the Federal Court is in stark contrast to a number of ill-informed and sensationalist submissions which have been made to the Inquiry, some of which are devoid of supporting data and others which are reliant upon incomplete and inadequate data.

To have a fair and reasonable long term average ROIC (before taking into account the costs of running the business) in the litigation finance asset class, it is necessary to have some returns which are a multiple of that average in order to compensate for lower returns or losses where up to 170% of invested capital (or more) may be lost following a payment of adverse costs.

Omni Bridgeway background

Omni Bridgeway is a global leader in dispute resolution finance, with expertise in civil and common law legal and recovery systems, and operations spanning Asia, Australia, Canada, Europe, the Middle East, the UK and the US. Omni Bridgeway has built its reputation as a trusted provider of funding solutions and offers end-to-end dispute finance from case inception through to post-judgment enforcement and recovery.

Authorised by the Disclosure Committee

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