Australian Securities and Investments Commission, Consultation Paper 185: Litigation schemes and proof of debt schemes: Managing conflicts of interest

Submission from the U.S. Chamber Institute for Legal Reform

Introduction

The U.S. Chamber Institute for Legal Reform (“ILR”) is pleased to submit this response to the Australian Securities and Investments Commission’s (“ASIC”) Consultation Paper 185: Litigation schemes and proof of debt schemes: Managing conflicts of interest.

ILR is a not-for-profit public advocacy organization affiliated with the U.S. Chamber of Commerce, the world’s largest business federation representing the interests of more than three million businesses of all sizes and sectors, as well as state and local chambers and industry associations. ILR’s mission is to ensure a simpler, fairer and faster legal system. Since ILR’s founding in 1998, it has worked diligently to limit the incidence of litigation abuse in courts around the world and has participated actively in legal reform efforts in the United States and abroad.

As part of its core mission, ILR has been studying the effects of litigation funding for several years. It has sponsored a number of nonpartisan symposia and conferences, as well as the publication of articles on the effects of litigation funding, and has engaged in public advocacy with several governments, including the federal government of Australia, related to litigation funding.

Because many of ILR’s members have substantial business activities in Australia, ILR is deeply invested in the orderly administration of justice here. In addition, because Australia is in many respects a pioneer in the use of litigation funding, and is looked to for litigation funding precedent the world over, Australia’s decisions will have a global impact. ILR joins the debate concerning the future of litigation funding in Australia to ensure that the interests of its constituents will be adequately heard.

Background – The Dangers of Litigation Funding

ILR commends ASIC on its proposal to address conflicts of interest in litigation funding in class actions. The government’s focus on conflicts of interest, as reflected in its request to ASIC, is a welcome start to eliminating the many problems associated with litigation funding. ILR recognizes that the government asked ASIC only to propose rules to address the conflicts of interest inherent in litigation-funding
relationships, and, in this respect, ASIC has carried out its objective. We discuss the substance of ASIC’s admirable proposal below.

At the outset, however, we note that addressing conflicts of interest is only a start. Litigation funding is an inherently problematic practice, and ameliorating the risks it poses to civil justice – especially in class actions – is a critically important area of further study for the government. Although it was not within ASIC’s purview, ILR believes that litigation funding must be subject to a robust regulatory regime – covering far more than conflicts of interest – in order to protect consumers, defendants, and the administration of civil justice in Australia. Accordingly, before addressing ASIC’s specific proposal, ILR takes the opportunity to discuss the broad dangers posed by litigation funding.

Litigation funding inherently presents a number of policy and ethical dangers. Of greatest concern: (i) it diminishes client control over lawsuits and weakens lawyers’ loyalty to their clients; (ii) it threatens the independence of the legal profession and transforms the judicial process from a means to settle disputes between parties into an investment vehicle for unrelated third parties; and (iii) it increases the number of active lawsuits, causing slower case processing and impeding the administration of justice.

The first and foremost problem with litigation funding is that it undercuts claimant control over lawsuits, because litigation funders inherently want to protect their investment and therefore seek control over strategic decisions in the lawsuit. This is troubling, because it reduces a justice system designed to adjudicate cases on their merits to a litigation system effectively controlled by third parties interested solely in profit. Moreover, this process robs claimants of their autonomy. A litigation funder will prosecute a case in pursuit of its own interest in profits, even if the interests of the claimant in vindicating his or her rights diverge.¹

Similarly, because the litigation funder is the one funding the lawsuit and paying the lawyer’s fees, there is a serious risk that the lawyer will feel more beholden to the funder than to the client, leading to conflicting loyalties. Litigation funding arrangements thus risk placing the power to make strategic decisions about a case in the hands of the litigation funder, whose duties are to its investors – instead of the lawyer, whose duties are to the client. In addition, since both litigation funding companies and lawyers are repeat players in the litigation market, it can be expected that relationships among them will develop over time, under which lawyers will steer clients to favored litigation funding companies, even if the clients’ particular circumstances suggest that a different firm may be more appropriate.

These dangers are especially acute in class actions, where, because each claimant generally has only a small amount of money at stake, the lawyers usually run the

¹ Anne Urda, Legal Funding Gains Steam But Doubts Linger, Law360 (Aug. 27, 2008) (quoting a Huron Consulting Group Vice President as saying, “clients may have to relinquish some decision-making authority to the funder” and “the client’s interests may diverge from the funder”).
litigation with little accountability to the class members. When a litigation funding company is instructing the claimants’ lawyer and collecting a substantial portion of any award to the claimants, class actions become even further removed from the consumers they are supposed to benefit. The ongoing class actions against several Australian financial institutions illustrate this problem. The claimants in these cases were recruited by a company called Financial Redress, a subsidiary of Australia’s largest litigation funding company, IMF (Australia). Potential claimants who attempt to contact Maurice Blackburn, the law firm representing the class, are referred to Financial Redress. Thus, the connection between the claimants and their supposed lawyers is all but nonexistent. These claimants, who have agreed to pay twenty-five percent of any award to IMF (Australia), have been reduced (in the words of the High Court’s minority in Fostif), to a “means of generating profit” for IMF (Australia).

Defendants are also harmed by this shift in control from claimants to litigation funding companies as well, because funders typically attempt to shroud their investments in a “veil of secrecy.” As a result, a defendant in litigation may not even realize who is guiding litigation strategy and decisions on the other side, making it difficult to defend itself fairly in the case. Currently, disclosure of a litigation funding relationship is only required in representative proceedings in the Federal Court and in group proceedings in the Victoria Supreme Court (and even in these limited circumstances, claimants need not disclose information they think may confer an advantage on the defendant, which is a broad and vague exception).

These are not idle concerns. In Fostif, the litigation funding company selected and retained the claimants’ trial counsel, prohibited counsel from contacting the claimants directly and instructed counsel throughout the proceeding, including retaining power to settle the proceeding. A minority of the High Court noted that “public confidence in, and public perceptions of, the integrity of the legal system are damaged by litigation in which causes of action are treated merely as items to be dealt with commercially.”

The second problem presented by litigation funding is that it diminishes the independence of the legal profession. From the beginning, the legal profession has been a tightly regulated profession whose practitioners are highly trained, must take an oath before practicing, and are bound by ethical rules. Obviously, as the majority

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3 See Campbells Cash and Carry Pty Ltd v. Fostif Pty Ltd, [2006] 229 ALR 58, at 54.


5 [2006] 229 ALR 58, at 43-44.

6 Id. at 50.
noted in *Fostif*, lawyers make money practicing law, but their chief goals are to zealously represent their clients and to advance their clients’ interests.

Today, the traditional relationship between the lawyer and the client is being threatened by litigation funding. Under current ethical rules, law practices are managed in a manner that protects client interests and upholds the principles of the legal profession. These core values are threatened by the prospect of non-lawyer moneymen gaining influence over lawyers. Permitting litigation funding to intrude upon the traditional practice of law carries with it the substantial risk that the litigation funders will focus only on their own profit, rather than client interests or the advancement of the legal profession.

Current ethical rules do not accommodate litigation funding because litigation funding fundamentally changes the nature of civil litigation. Legal ethics contemplate a legal system designed to resolve disputes between parties. Litigation funding drops a stranger into the lawsuit whose goal is to make money from the parties’ disagreement. As the minority of the High Court put it in *Fostif*, the “purpose of court proceedings is not to provide a means for third parties to make money by creating, multiplying and stirring up disputes in which those third parties are not involved and which would not otherwise have flared into active controversy.”

The third problem with litigation funding is that it leads to more lawsuits, straining judicial resources. Defenders of litigation funding say that the practice increases “access to justice.” What this really means, however, is that litigation funding makes it easier for a claimant to file a lawsuit and force a defendant to incur costs to appear and defend against it. Indeed, the managing director of IMF (Australia) bragged on ABC TV’s *Lateline* that the increased availability of litigation funding in Australia is behind the growing number of class actions and large litigation cases here.

The United States has had its own experiment with increasing “access to justice” – contingent lawyers’ fees. As it has turned out, many observers agree that contingency fees are a primary cause of the runaway tort system in the United States. Contingency fees and litigation funding are strikingly similar – in both cases, a claimant can pass off the risk of pursuing a lawsuit to a third party on a nonrecourse basis, meaning that the claimant has every incentive to roll the dice and file a claim. But at least in the case of contingent lawyers’ fees, the ultimate decision of whether a claim is worth filing sits with a lawyer who is bound by ethical rules. In the case of litigation funding, however, the person deciding whether or not a claim is worth filing

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7 *Id.* at 54.

8 *Id.* at 50.


is a third-party investor who owes no duties to the potential claimant. Thus, while a contingency-fee lawyer will decide whether or not to file a claim based at least in part on the strength of its legal merit, a litigation funding investor looks only at the present value of the expected return, of which the legal merit is only a part.

Moreover, as more lawsuits are filed, the burdens on Australia’s courts increase. Increased litigation funding in Australia has been found to be “associated with slower case processing, larger backlogs, and increased spending by the courts.” This is not surprising when an increased number of cases are being filed.

But these results show an additional problem with litigation funding as well: Cases funded by litigation funding tend to remain on court dockets longer than unfunded cases because both the litigation funding providers and the claimants they fund will be inclined to reject reasonable settlement offers. A claimant who must pay a finance company out of the proceeds of any recovery can be expected to reject what may otherwise be a fair settlement offer and hold out for a larger sum of money. By the same token, the financing company can be expected to pressure claimants to accept only settlement offers that are sufficient to cover the amount financed after subtracting the claimant’s share of the recovery.

Ultimately, whether by lowering the bar to filing lawsuits or by keeping them on court dockets longer, litigation funding increases the number of active lawsuits in Australia, imposing additional burdens on court personnel. As cases move more slowly through the civil justice system, justice is delayed for those claimants who are legitimately harmed and deserve to be awarded compensation, and for those innocent defendants who deserve to be exonerated.

Overview of Possible Safeguards

In light of all the dangers litigation funding poses to the administration of civil justice in Australia, ILR supports the implementation of a comprehensive regime of safeguards aimed at protecting the interests of both consumers and defendants who are swept into the legal system. ILR appreciates that ASIC crafted its proposal in response to a government request, and we discuss Corporations Amendment Regulation 2012 (No. 6) on its merits below. Nevertheless, we urge the government to further consider a comprehensive regulatory regime including robust safeguards against abuses by litigation funders that could ameliorate the risks posed by litigation funding.

In addition to the conflicts of interest rules proposed by ASIC, safeguards that would help mitigate the problems of litigation funding include:


12 The Supreme Court of the U.S. state of Ohio recognized that litigation funding is an “absolute disincentive” to settlement in Rancman v. Interim Settlement Funding Corp., 789 N.E.2d 217 (Ohio 2003).
Safeguards against claimants losing control over their lawsuits

- **A ban on any funder control over litigation and settlement decisions.** After *Fostif*, litigation funders are able to exercise almost complete control over lawsuits in pursuit of their own profits. This safeguard would help restore the client as the master of the claim and ensure that the claim is prosecuted to vindicate the client’s interests.

- **A requirement that litigation funding companies fund cases to conclusion once funding begins.** This safeguard would induce funding companies to analyze potential investments carefully and also would protect consumers against litigation funding companies exerting influence over the direction of the lawsuit by threatening to cut off funding.

- **Disclosures.** The existence and terms of any litigation funding arrangement must be disclosed to the opposing party, regardless of where the civil action is pending. This will give courts the opportunity to review the fairness of any arrangements and will afford defendants the right to know the identity of their accusers.

- **A ban on funding contracts directly between funders and lawyers.** After *Fostif*, the role of the client in cases funded by litigation funding has been marginalized. This safeguard would help assure that the client is the master of the claim. In addition, by separating the repeat players – the lenders and the lawyers – this rule would also reduce the risk that lawyers and lenders will develop relationships aimed at maximizing their own profits at the client’s expense.

Safeguards against the diminished independence of the legal profession

- **Licensing and registration requirements.** Litigation funders should be subjected to licensing and oversight by an appropriate government entity, which would help ensure that the funders meet appropriate probity requirements.

- **A ban on law firms having ownership interests in funding companies, and vice versa.** Litigation funders’ involvement in law firm management would threaten to further dilute the already diminishing role of the client because lawyers may feel pulled by the interests of influential investors more than by the interests of their clients. This safeguard would help counteract this trend.

- **A ban on lawyer-funder referral fees.** Lawyers and funders should not be permitted to accept fees for referring clients to each other. Such fees compromise lawyer objectivity and independence, and might influence a lawyer to refer a client to a particular funder that is not in the client’s best interests.
Safeguards against the danger of increased litigation

- **A ban on litigation funders soliciting unrepresented potential claimants.** After the High Court’s *Fostif* decision, litigation funding providers are able to gin up litigation by contacting claimants who otherwise would not have been inclined to file a lawsuit – as in the ongoing bank-fees litigation. This safeguard would help limit this undesirable practice.

- **A requirement that litigation funders satisfy – and demonstrate the means to satisfy – any security or adverse costs orders.** Litigation funding supporters boast that litigation funding leads to more lawsuits. Requiring litigation funders to pay the expenses incurred by the opposing party if it is successful in such a suit is fair.

- **A ban on securitizing or otherwise assigning interests in investments.** Litigation funders should not be able to create and profit from derivative interests in lawsuits, thus offloading any risk from their investments onto unsuspecting investors. In addition to protecting the investment community, this safeguard also would incentivize litigation funders to carefully analyze their funding decisions by requiring them to bear the full risk of any loss.

These safeguards are designed to protect against the dangers posed by litigation funding. As an additional overarching safeguard, ILR supports meaningful sanctions for violations, through which companies that violate any legislation, regulations or rules that embody the above safeguards must be subject to enforcement, including fines and license revocation. This will protect both consumers and defendants against unscrupulous practices by litigation funding companies. Even then, focusing a regulatory regime for litigation funding solely on the funders will only address part of the problem. Court rules requiring parties to disclose litigation funding arrangements and professional-conduct rules that apply to lawyers dealing with litigation funding are also necessary for a truly comprehensive approach to the problem.

In the long term, ILR urges Australian policymakers to adopt these safeguards, which are specifically tailored to protect consumers from unethical and abusive practices by litigation funding providers, and to protect corporations from being forced to expend substantial resources and time defending frivolous actions. In the near term, ILR again commends ASIC on its proposal to address conflicts of interest, which ILR comments on below with respect to litigation schemes.

**Potential Conflicts of Interest**

ILR agrees that the situations identified in paragraphs 14–17 are areas where there are potential conflicts of interest between the funder, lawyers and members in a litigation scheme. It should be noted that where the lawyers act for both the funder and the members they have a clear duty-duty conflict as they would owe professional and fiduciary duties to both the funder and the members. Further, a conflict may require
the lawyer to cease acting for both the funder and the members. ASIC refers to “a pre-existing relationship” between the funder, lawyers and/or members. Further clarification of the relationships that ASIC has in mind would be useful. ILR deals with lawyer’s interests in litigation funders below in relation to proposal D7.

Additional conflicts that may arise, include:

- the structuring of the litigation (e.g., choice of defendants such as whether to sue some or all of a corporate entity, its directors, its advisers) as this can impact prospects of success, costs exposure, length of litigation, and the likely recovery, with funders and members having different interests;

- choice of litigation vehicle (e.g., class action, joinder or test case) as different obligations may fall on members depending on the vehicle chosen (although the Corporations Amendment Regulation 2012 (No. 6) has effectively favoured class actions through granting exemptions to a litigation scheme), and

- who is included in the proceeding (e.g., is the group definition open or closed, consumers and/or institutions) as this can impact the cost of organising and prosecuting proceedings, whether strong and weak claims are combined and the distribution of any settlement.

ASIC identifies that the terms of the funding agreement may give rise to potential conflicts of interest. It would be helpful to elucidate in more detail the types of conflicts that may arise, such as: percentage to be paid to the funder, factors influencing the percentage such as passage of time, size of the member’s claim (e.g., number of shares held) and events in the litigation (appeals), other fees charged by the funder such as project management and claim investigation costs, provisions dealing with obligations on members in exchange for funding (e.g., provision of affidavits, discovery or testimony), rights given to the funder to make or participate in decisions affecting the litigation scheme (e.g., entry into alternative dispute resolution, settlement, appeal) and grounds for termination.13

Further elucidation of the conflicts arising in the terms of the funding agreement would seem to be crucial in educating funders, lawyers and members if the funder is to be left to develop their own arrangements and policies for managing conflicts of interest.

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13 A summary of three litigation funding agreements is contained in Michael Legg, Litigation Funding in Australia: Identifying and Addressing Conflicts of Interest for Lawyers (February 2012) available at http://www.instituteforlegalreform.com/doc/litigation-funding-in-australia-identifying-and-addressing-conflicts-of-interest-for-lawyers. ASIC may find this publication helpful in describing the range of conflicts of interest that can arise in the terms of the funding agreement.
Proposal B1

B1 We propose that each funder and each lawyer should:

(a) be responsible for determining their own arrangements to manage interests that may conflict with their duties; and

(b) be able to demonstrate that they have adequate arrangements to manage conflicts of interest, including documenting, implementing, monitoring and reviewing their arrangements.

ILR would have preferred to see a more stringent duty in relation to conflicts of interest than the requirement to have adequate arrangements to manage conflicts. For example, in relation to a managed investment scheme regulated by Chapter 5C of the Corporations Act 2001 (Cth), the requirement is that a responsible entity is subject to a duty to “act in the best interests of the members and, if there is a conflict between the members’ interests and the interests of the responsible entity, give priority to the members’ interests.”

Alternatively, requirements similar to those imposed on financial advisers so that they must act in the best interests of their clients, subject to a “reasonable steps” qualification, and to place the best interests of their clients ahead of their own when providing personal advice to retail clients would be welcome.

As a stronger form of conflict avoidance obligation has not been adopted, ILR believes that ASIC should consider whether the contractual exclusion of fiduciary obligations that may otherwise arise from the funder-member relationship should be prohibited. It is common practice for litigation funding agreements to seek to exclude fiduciary relationships. ILR submits that the exclusion of a fiduciary relationship would be inconsistent with the requirements in Corporations Amendment Regulation 2012 (No. 6), especially the obligation to protect the interests of members in the scheme, as excluding a fiduciary duty deprives members of important protections, including avoiding conflicts of interest, not obtaining any unauthorised profit from the fiduciary relationship and acting in good faith.

Subject to the above reservation, ILR supports each funder and each lawyer being responsible for identifying conflicts of interest and adopting arrangements to manage those interests, but with more guidance from ASIC as to what constitutes a conflict of

14 Section 601FC(1)(c) of the Corporations Act 2001 (Cth). The same duty is imposed on officers of the responsible entity by Corporations Act 2001 (Cth) s 601FD(1)(c).


16 It is open to the parties to a contract to exclude or modify the operation of fiduciary duties: Hospital Products Ltd v United States Surgical Corp (1984) 156 CLR 41 at 97, Chan v Zacharia (1984) 154 CLR 178 at 196.

interest. The funder and lawyer are better placed to know their own interests and where conflicts may arise based on the specific arrangements that they have with members. Arrangements are able to be more tailored and fact-specific. However, ASIC should also adopt prescriptive minimum standards to ensure that the interests of members are protected. ASIC’s other proposals seek to do this and should be commended. ILR’s comments on those proposals are below.

Proposal B2

B2 We propose that our guidance to manage divergent interests will only apply to funders and lawyers involved in a litigation scheme or proof of debt scheme to the extent that they:

(a) rely on the exemptions under the Corporations Amendment Regulation for such activities; or

(b) conduct their activities under an AFS licence.

No comment.

Proposal B3

B3 We propose that any exemptions we have previously given litigation schemes or proof of debt schemes from the requirements in Chs 5C and 7 of the Corporations Act will be revoked.

No comment.

Proposals C1, C2 and C3

C1 We propose that the funder should provide prospective members with:

(a) information that is likely to assist them to understand the different significant interests of the funder, lawyers and members, and how they may conflict; and

(b) details of any dispute resolution options that are available to a member who has a dispute with the funder.

C2 We propose that there should be mechanisms in place so that if the funder or lawyers become aware of a significant divergence in their interests, and which has not already been disclosed, they should tell each affected member at the first reasonable opportunity.

C3 We propose that the disclosure of the diverging interests of the funder, lawyers and members, and how they may conflict, should:
(a) be timely, prominent and specific; and

(b) contain enough detail for members to understand the potential impact of the diverging interests on the litigation scheme or proof of debt scheme.

ILR endorses proposal C1(a), with one reservation. Proposal C1(a) requires disclosure of information that is likely to assist prospective members to understand the different significant interests of the funder, lawyers and members, and how they may conflict. This proposal will require funders to reflect on the conflicts that may exist and make members aware of them. Proposals C2 and C3 will require this to be conducted on an ongoing basis. ILR’s reservation is the use of the word ‘significant’ to qualify ‘interests’. This would seem to be unnecessary and inconsistent with the wording of regulation 7.6.01AB(2)(b) which refers to ‘any’ conflict of interest.

Proposal C1(a) could be improved through also being prescriptive about a minimum level of disclosure rather than leaving it completely to the funder to identify the interests to be disclosed. This could include:

(a) all fees/payments to funder;

(b) obligations and rights of funders, especially the level of control over decision making in the litigation and termination rights;

(c) obligations and rights of lawyers;

(d) obligations and rights of plaintiff/representative party;

(e) obligations and rights of members;

(f) any advice received by the funder on the litigation’s prospects of success; and

(g) estimate of costs.

ILR further believes that the proposals should explicitly prohibit funders from making or participating in decisions affecting the litigation scheme. Strategic decisions such as who to sue, causes of action, settlement/discontinuance and appeal should be within the control of the members, or the members’ representative. ILR does not believe that these decisions should be made by the funder, nor should the funder have input on these decisions. It must be remembered that the cause of action belongs to the member and not the funder.

In addition, ILR believes that the proposals should explicitly prohibit funders from withdrawing funding before the conclusion of a case. Permitting a funder to terminate funding while a case is pending creates a clear conflict of interest, because the funder will want to be able to exit an unprofitable funding agreement as quickly and easily as possible, while members will want to avoid the loss of funding, especially in relation to the protections against liability for legal costs and any adverse cost order.
Prohibiting funders from withdrawing funding will protect consumers and incentivize funders to analyze their potential investments carefully.

ASIC’s proposal creates an incentive for funders to make dispute resolution options available. This is to be welcomed; however, it does not go so far as to impose ASIC oversight. This can be contrasted with an AFSL holder who must provide a dispute resolution system that consists of: an internal dispute resolution procedure that covers complaints against the licensee made by retail clients in connection with the provision of all financial services covered by the licence; and membership of one or more external dispute resolution schemes. Both types of scheme must be approved by ASIC.

**Proposal D1 and D2**

D1 We propose that the funder and lawyers should be able to demonstrate that they have processes and procedures to:

(a) identify divergent interests and where conflicts may arise;

(b) assess those interests and potential conflicts; and

(c) decide upon and implement an appropriate response to those divergent interests and potential conflicts.

D2 We propose that the funder and lawyers should be able to demonstrate that the processes and procedures they adopt are:

(a) tailored to the nature, scale and complexity of the litigation scheme or proof of debt scheme, including the number of members that are party to the scheme;

(b) documented;

(c) effectively implemented;

(d) regularly monitored and reviewed, and updated as needed; and

(e) overseen by a designated senior person (or persons) within the funder or law firm who takes responsibility for their implementation and monitoring.

Based on the current state of regulation, ILR supports proposals D1 and D2. ASIC should require that the designated senior person or persons does not themselves have any conflicts of interest.
Proposal D3

D3 We propose that the funder and lawyers should ensure that they have in place appropriate policies and procedures so that when they are faced with a conflict between their interest and the interests of members, the members’ interests are adequately protected.

ILR agrees with this proposal, but as set out above in relation to proposal B1, the protection of the interests of members should not be diminished through excluding pre-existing protections that may arise in equity from the funder-member relationship.

Proposal D4 and D5

D4 We propose that the funder and/or lawyers recruiting members for a litigation scheme or proof of debt scheme should have arrangements to ensure that conflicts do not result in misleading or deceptive conduct, including having a senior person with designated responsibility to oversee recruitment practices.

D5 We do not propose to require particular terms in the agreement relating to the litigation scheme or proof of debt scheme. However, we propose that, as part of the obligation to control situations where conflicts may arise, the funder and/or lawyers should review the terms of agreements to which they are a party in light of the existing body of law on unfair contracts and unconscionability, where relevant.

ASIC’s proposals confirm the need to comply with the statutory prohibitions on misleading or deceptive conduct, unconscionable conduct and unfair contract terms. ASIC’s concern in relation to the recruitment of members is certainly justified as shown by these two decisions:

In *Johnstone v HIH Ltd* [2004] FCA 190, a letter was sent by the applicant’s solicitor to group members which contained a misleading statement, namely that group members could participate in the class action if they paid a fee to the solicitors. Tamberlin J required that a letter of correction be sent to the group members who had received the original letter.

In *Jarra Creek Central Packing Shed Pty Ltd v Amcor Limited* [2008] FCA 575, after the provision of the opt out notice to group members, the solicitor for the plaintiffs made public statements to various media bodies concerning the anticipated amount of damages the Court would award if the plaintiffs were successful. The solicitor’s comments were misleading, as they were based on comments attributed to the Australian Competition and Consumer Commission (ACCC) which the ACCC never made. Tamberlin J ordered that the plaintiffs’ solicitor publish a correction of the misstatements and extended the date by which class members could opt out of the proceeding.
**Proposal D6**

D6 We propose that if there is no direct contractual relationship between the lawyers and members, the funder should ensure that they engage the lawyers on terms that make clear that if there is a divergence of interests between the funder and the member, the lawyers must ensure that the members’ interests are adequately protected.

The member’s interests are best protected if there is a direct retainer between the lawyer and each member. Further, the lawyer should act for the members only and not the litigation funder, so as to prevent the inevitable conflict of interest that would arise.

**Proposal D7**

D7 We propose that there should be either:

(a) independence between the funder, lawyers and members; or

(b) if there is no such independence, the relationship should be disclosed to members.

The ownership of litigation funders has not attracted a great deal of attention in Australia to date, with the focus being on the relationship between funders and members.\(^{18}\) However, in the UK lawyers have started to create litigation funding vehicles “to allow partners to invest in litigation in a tax-efficient manner.”\(^{19}\) However, if lawyers are able to “own” or control a litigation funding entity in Australia, lawyers could use the funding vehicle to side-step the prohibition on lawyers charging a contingency fee. Further, where a lawyer is both lawyer and owner or controller of the litigation funding vehicle this may create a further level of conflicts of interest. For example, the funder may accept lucrative charge-out rates for the lawyer knowing that in a successful litigation scheme the legal fees will ultimately be borne by the members and/or the defendant in the litigation. There is no incentive to minimise legal fees. Of course, if the litigation is unsuccessful the funder pays the legal fees, but this is really the lawyer being obligated to pay themselves. Conflicts of interest are best managed if lawyers and funders are independent from each other.

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\(^{19}\) See Katy Dowell, Stewarts Law sets up litigation funding vehicle, *The Lawyer*, 16 July 2012 available at http://www.thelawyer.com/stewarts-law-sets-up-litigation-funding-vehicle/1013458.article
Proposal E1

E1 We propose to adopt one of the following options when proceedings have not been issued:

Option 1

The terms of any settlement agreement of a litigation scheme should be approved by either:

(a) a panel comprising at least one independent person; or

(b) counsel (or senior counsel if involved).

Option 2

Any settlement offer in a litigation scheme to be made by the members, or the acceptance of any settlement offer received by the members, should be approved by either:

(a) a panel comprising at least one independent person; or

(b) counsel (or senior counsel if involved).

The class action legislation states that a proceeding may not be settled or discontinued without the approval of the Court: Federal Court of Australia Act 1976 (Cth) s33V. This is usually accompanied by a requirement for notice to the group members: Federal Court of Australia Act 1976 (Cth) s33X. Federal Court of Australia, Practice Note CM17, “Representative Proceedings Commenced under Part IVA of the Federal Court of Australia Act 1976,” 1 August 2011 provides guidance as to the test for approving a settlement and the procedure that may be adopted.

ASIC proposes that settlements achieved without proceedings being commenced should be subject to oversight. This is in addition to the current requirements and is supported. However, ASIC should also consider the situation where proceedings have commenced and a settlement is proposed or has been received. Prior to seeking court approval, a decision needs to be made on whether to propose or accept a settlement offer. This situation can create conflicts between funders and members. ASIC’s proposal E1 could be made applicable to this situation. Indeed, most litigation funding agreements currently employ a “QC clause” where a senior barrister is asked to resolve differences of opinion about a settlement. The senior barrister should not have been involved in the proceedings previously and should be independent from the funder and the members.
Proposal E2

E2 We propose that in reviewing a settlement agreement or offer, the panel members or counsel must be satisfied that the settlement agreement or offer is fair and reasonable, taking into account the claims made on behalf of the members who will be bound by the settlement and potential conflicts between the funder and/or lawyers and the members as well as between the group members. In satisfying themselves that the proposed settlement is fair and reasonable, the panel members or counsel should take into account, among other things, the following factors:

(a) the amount offered to each member;

(b) the prospects of success in the proceeding (i.e. the weaknesses, substantial or procedural, in the case advanced by the members);

(c) the likelihood of members obtaining judgement for an amount significantly in excess of the settlement sum;

(d) whether the settlement sum falls within a realistic range of likely outcomes;

(e) the terms of any advice received from counsel or an independent expert on the issues that arise in the case;

(f) the attitude of the group members to the settlement;

(g) the likely duration and cost to members of proceedings if continued to judgement;

(h) whether the funder might refuse to fund further proceedings if the settlement is not approved; and

(i) whether the settlement involved any unfairness to any member or categories of members for the benefit of others.

ASIC should consider Federal Court of Australia, Practice Note CM17, “Representative Proceedings Commenced under Part IVA of the Federal Court of Australia Act 1976”, 1 August 2011.