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Will 2020 mark the beginning of the end for class actions in Australia?

Class actions



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📍 Melbourne

The headline of this article is admittedly an extremely pessimistic (if not melodramatic) prediction as to the future of class actions in Australia. It is based only partially on the measures that have been announced this month with respect to yet another inquiry into class actions and litigation funding; the licensing of litigation funders; and a greater level of “protection” from shareholder class actions over the next six months. What concerns me even more than these developments are the process that has been followed to arrive at these decisions and the evidence that has been relied on to introduce these changes.

Benefits do not outweigh the costs

In December 2018 the Australian Law Reform Commission provided the Commonwealth Attorney-General with its final report in relation to its 12-month study of class actions and litigation funding. The ALRC is widely recognised as one of the world’s finest law reform commissions. Its President, the Honourable Justice Sarah Derrington, has had a stellar career as an academic and barrister. She had not, to my knowledge, previously written on class actions and/or commercial litigation funders or been briefed to appear for parties in class action litigation. In other words, she had no pre-conceived views about class actions and the litigation funding industry.

In its May 2018 discussion paper, the ALRC revealed its intention to recommend that the Corporations Act 2001 be amended to require litigation funders to obtain and maintain a “litigation funding licence” to operate in Australia.

In its submission to the ALRC the Australian Securities and Investments Commission provided the following analysis: A requirement that a litigation funder obtain an AFS [Australian Financial Services] licence will not, without significant changes to other aspects of the Corporations Act, necessarily mean that the litigation funder will be adequately capitalised to ensure that it can meet adverse costs orders, continue to fund litigation or distribute funds to shareholders.

The ASIC was also of the view that: “The existing mechanism for the court to order security for costs is a more targeted and effective way to address the risk that a litigation funder will not have adequate resources to meet an adverse cost order. ... By contrast, ... the AFS licensing requirements are not designed to act as security to meet a particular liability, nor are they intended to protect against credit risk more generally.”

Similarly, the ALRC noted that it “is not satisfied that the benefits of a licensing regime ... outweighs the regulatory costs of imposing a licensing regime with minimum capital adequacy requirements on litigation funders”.

The ALRC’s conclusion was that “a licence is unlikely to improve regulatory compliance in the third-party litigation funding industry in the short to medium term”.

No evidence in support of change

What has been the response by the Federal Government to this objective and balanced analysis undertaken by the ALRC and the ASIC? We are still waiting for it but in the meantime we have been told, through media releases: (a) that the Federal Parliamentary Joint Committee on Corporations and Financial Services will be asked to cover essentially the same areas covered by the ALRC and in a shorter period than what was available to the ALRC; and (b) that litigation funders will be subject to, not only the AFS licensing requirements, but also the requirements that apply to managed investment schemes.

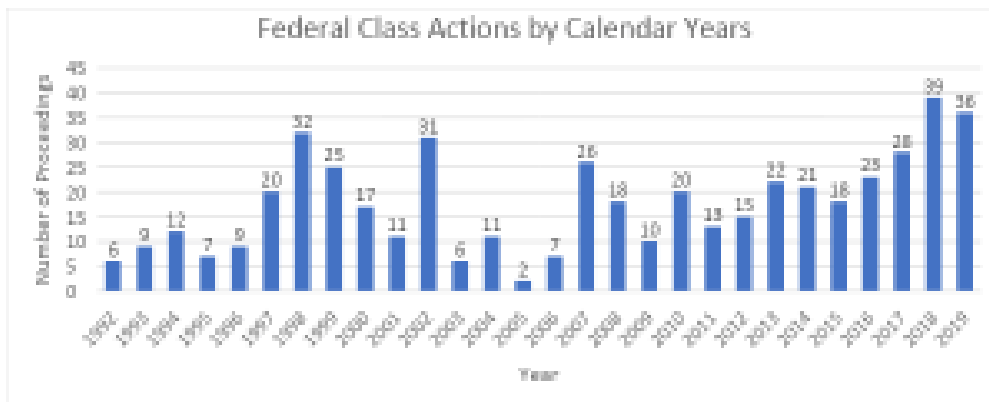
In light of the careful analysis of this area undertaken by ASIC and the ALRC, one would have reasonably expected, at the very least, a detailed explanation as to what was incorrect in the reasoning adopted by the ALRC and ASIC. Instead, we have been told by the Treasurer, through the media, that there has been a 325 per cent increase in the number of class actions filed in the Federal Court of Australia over the past ten years.

Before considering the accuracy of this statistic, a preliminary but crucial question needs to be asked: how does this statistic, standing on its own, justify the introduction of licensing requirements for commercial litigation funders? It is like saying that the arrest powers of police should be drastically reduced because the number of arrests in Australia more than tripled over the past ten years. This statistic would provide no evidence in support of a change in this area unless it was demonstrated that a majority (or at the very least a substantial number) of these arrests were unjustified. A similar finding would need to be made with respect to class actions. Furthermore, it would need to be demonstrated that the meritless litigation was “instigated” by litigation funders.

Before considering this issue though, it is necessary to go back to the issue of placing the funding of class actions by commercial litigation funding under the requirements of the regime regulating managed investment schemes. In 2009 a majority of the Full Federal Court held that the funding of class actions satisfied the definition of a managed investment scheme under the relevant statutory regime. Shortly after this judicial pronouncement the Federal Treasury organised a roundtable of experts to canvass what regulatory action (if any) may be necessary to deal with its consequences. No politicians participated at this roundtable. A clear majority of the participants at this roundtable concluded that placing class actions funded by litigation funders (and plaintiff solicitors) under this regime would be inappropriate and undesirable in light of the simple fact that its drafters did not envisage or intend that this regime would be applicable to funded class actions. To my knowledge, this conclusion is as valid in 2020 as it was in 2010.

No class action flood

This graph captures my data with respect to the volume of federal class action litigation up to the end of 2019:



In the ten-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. Over the next 10 years, a total of 235 federal class actions were filed. This represents a 69 per cent increase. At first glance that may seem a significant increase. But what does this data mean in terms of annual averages of federal class actions? In the first period there was an annual average of 13.9 federal class actions. In the next ten years, the annual average went up to 23.5. Does this latter annual average evince an opening of the floodgates or a class action regime that is out of control in our “national” court? No objective or balanced assessment of this question could possibly lead to an affirmative answer.

Furthermore, 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. We also see that the upward trend that occurred in the period from 2015 to 2018 came to an end in 2019. This was despite the fact that in 2019 we saw the filing of a number of federal class actions stemming from the Hayne Royal Commission. It is also crucial to remember that, as I revealed in my most recent empirical report, exactly one-third of all class actions filed in Australia as at 30 June 2019 were “duplicates”, that is, they concerned 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).

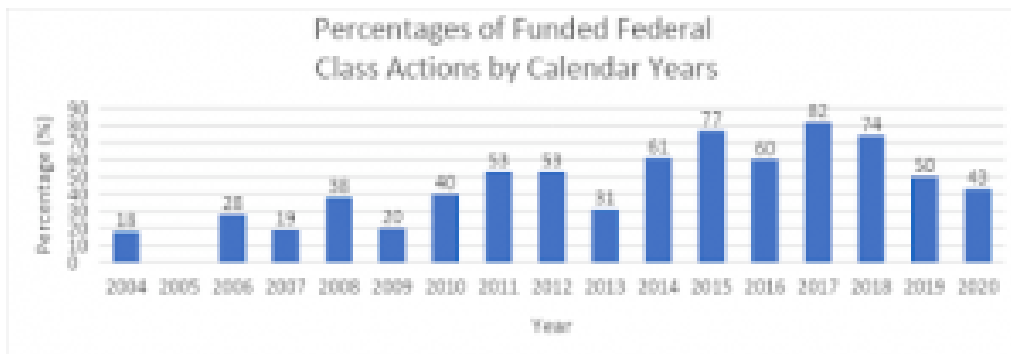
What if the Treasurer was referring to the increase in all Australian class actions? A comparison of the country’s overall volume of class action litigation over the two periods in question would be inappropriate for a simple but crucial reason. In the first period class actions were available in only two Australian courts: the Federal Court and the Supreme Court of Victoria. In the last ten years, three more State courts joined the class actions market: the Supreme Courts of Queensland and Tasmania and, most importantly, the Supreme Court of New South Wales. Thus, comparing the two periods would be as inappropriate and unhelpful as comparing the total number of products coming out of a factory during two periods of equal duration if, in the first period, only two employees were employed at this factory whilst in the second period three extra employees were employed.

A meaningful comparison would instead entail a consideration of the changes in the volume of class action litigation when these three regimes - as well as Australia’s fourth most important class action regime, in the Supreme Court of Queensland - were all operating at the same time. Given that the NSW regime came into operation in March 2011 and that the Queensland regime came into operation in March 2017, the appropriate review period starts in 2017.

In the 2017 calendar year I identified the filing of 49 class actions in Australia. In 2018, 66 class actions were filed, to my knowledge, marking a 34 per cent increase. In 2019, there was an 18 per cent decrease as I identified a total of 54 class actions. Again, hardly evidence of an “explosion” of class actions.

Downward trend in third-party funded class actions

What about the involvement of third-party litigation funders? The graph below provides data on the percentages of federal class actions supported by funders since 2004.



A significant downward trend is evident. The existence of a similar scenario at the national level is provided by the following data. 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.

Finally, looking at the outcomes of funded class actions, I found that over 64 per cent of resolved funded class actions were ultimately resolved through judicially-approved settlement agreements. This finding is clearly not consistent with the claim that commercial litigation funders have supported meritless class action litigation.

I hope the analysis and data set out above shows why I am genuinely concerned that in a couple of years from now scholars will look back at 2020 as the year that marked the beginning of the demise of Australia’s class action regimes. Should this occur it would be a very sad, indeed tragic, event for Australia when one considers that thousands of ordinary Australians have been able to secure monetary compensation only because of class action litigation. I will provide comprehensive data on the compensation received by class members in my next empirical report, which will hopefully be released in June or July.

About the author

Vince Morabito is a Professor of Law at the Monash Business School and has conducted empirical work on class actions and litigation funders for over 12 years.