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Class actions in Australia

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Class actions are an established and important part of the Australian legal landscape. In recent years, Australia has become the most likely jurisdiction outside of the United States in which a corporation will face significant class action litigation.

Recent developments in the Australian legal landscape – including increasingly plaintiff-friendly class action laws, the acceptance of third party litigation funding and a growing number of plaintiff class action legal practices – have facilitated that evolution. At least in part, these developments are the direct result of support for class actions (and third party funding of class actions) as important means of facilitating access to the civil justice system. The checks and balances in the Australian system have, however, helped to prevent what was predicted in the mid-2000s to be an 'avalanche' of class action activity.

This paper outlines some of the key issues and trends in Australian class actions.

Contents

The Australian class action regime

Most class actions in Australia are commenced under the Federal Court of Australia's representative proceeding regime.[1]

The key features of that regime include:

- threshold requirements: the following requirements must be met to commence a class action:
  - there must be seven or more persons with claims against the same defendant;
  - the claims must be in respect of, or arise out of, the same, similar or related circumstances; and
  - the claims must give rise to at least one substantial common issue of law or fact;
- representative plaintiff(s): the claim is brought on behalf of all class members by one (or a small number of) representative plaintiff(s) – the representatives are the only class members to be parties to the proceedings;
- class definition: the class can be defined by a list of names or by a set of criteria (such as all persons who acquired shares in Company XYZ during a certain period) – it is not necessary to name members of the class nor to specify the number of people in the class or the total value of their claims;

1 Part IVA of the *Federal Court of Australia Act 1976* (Cth). There are also equivalent regimes for class actions in the Supreme Courts of Victoria, New South Wales and Queensland.

- opt-out regime: every potential claimant who falls within the class definition is a member of the class unless they opt-out of the proceedings. A class may, however, be defined in a way that effectively requires members to opt-in to the class (including by entering into a retainer with a particular law firm or an arrangement with a particular third party funder);
- settlement approval: once proceedings are commenced, any settlement must be approved by the court – this requires the court to be satisfied that the settlement is fair and reasonable and in the interest of class members.

How are the class actions regimes in Australia and the United States different?

Class actions in Australia are different to class actions in the United States in (at least) the significant ways outlined in the table below:

	United States	Australia
Class certification	The lead plaintiff bears the onus of satisfying the court that the case satisfies the threshold requirements for proceeding as a class action.	No certification process. The onus is on the defendant to establish that the threshold requirements referred to above have not been met.
Common issues	Common issues must predominate over individual issues.	There need only be one substantial common issue of law or fact.
Costs	Each party bears their own costs irrespective of the outcome.	The unsuccessful party will generally be ordered to pay the successful party's costs on a party/party basis.
Contingency Fees	Lawyers are permitted to charge based on a percentage of any amount recovered.	Contingency fee structures are generally prohibited for lawyers (but not for third party funders).

The absence of a class certification process and the low common issues threshold make it easier to commence and maintain a class action in Australia than in the United States. As a result, the Australian class action regime has been described as 'one of the most liberal class action rules in the entire world'.[2] The Australian position in respect of costs is, however, generally acknowledged as being a significant deterrent to speculative litigation.

Third party funding of class actions

After a rocky start, third party funding has become an accepted and entrenched feature of Australian class actions practice. At least in part this is because of the prohibition on lawyers taking a percentage of the proceeds of a class action creating both a need and an opportunity for third party funding.

Under the standard third party funding model, the funder agrees to pay the legal fees of the funded party (the representative plaintiff and class) and to provide an indemnity for any costs orders made against the representative plaintiff (costs orders cannot be made against other class members). Funding commissions have typically ranged from around 25% to 40% of the proceeds, plus reimbursement of costs. Although, as discussed below, there has been downward pressure on funding commissions in recent years.

While funding arrangements were traditionally the subject of individual contracts between the funder and class members, in recent years an alternative model known as 'common fund' has been accepted under which the court makes an order approving a funding arrangement which is binding on all participating class members. The legality of the 'common fund' method is, however, currently the subject of an appeal to the High Court of Australia.

Despite downward pressure on funding commissions, there have been sustained increases in recent years in both the number of class actions that are funded and also the number of local and offshore funders investing in Australian class actions. Accurate information about funding arrangements is not always publicly accessible, but by our reckoning:

- Roughly 80% of recently commenced class actions are third party funded, which is a material increase on prior periods. What's particularly notable about this trend is that the percentage of funded cases has grown at the same time as class action filings have materially increased. This suggests a very significant increase in funding dollars being invested in Australian class actions.
- There are approximately 20 funders active in the market as at 2018/2019. By comparison, less than 10 funders were active five years ago.
- Third party funders have a clear preference for certain types of class actions. In particular, they favour shareholder class actions. Other preferred claims are consumer and investor class actions – in short, class actions with a relatively large number of class members.

While there is no sign that third party funders' appetite for Australian class actions is diminishing, there are indicators of the market changing in a way that may mean that the enterprise may not continue to be as lucrative as it has been in recent years. These indications include the following:

- Courts are starting to take a more interventionist role in considering the appropriateness of funding commissions.
- There has been downward pressure on funding commissions, as a result of increased court scrutiny and increased competition among funders.
- We have also started to see novel funding models, such as a funder's return being calculated by reference to a multiple of costs expended rather than as a percentage of the amount recovered.

Moreover, the Australian Law Reform Commission has recently recommended that lawyers be permitted to charge contingency fees in class actions. If implemented, this would

2 Professor G Miller, 'Some Thoughts on Australian Class Actions in light of the American Experience' in the Hon Justice K E Lindgren (ed), *Investor Class Actions*, Ross Parsons Centre of Commercial, Corporate and Taxation Law (2009) 2 at 4.

likely result in reduced demand for third party funding as more lawyers are likely to be prepared to take on the funding risk themselves (because of the higher potential return on that risk).

One of the more controversial aspects of the third party funding industry is that, unlike other financial services providers, funders are not subject to any specific regulation beyond a basic requirement to have a policy in place for managing conflicts of interest. While a number of law reform bodies have recommended that funders should be regulated and have prudential adequacy requirements imposed on them, the Australian Law Reform Commission has recently recommended against such reform on the basis that it would create an unnecessary barrier to entry to the Australian funding market.

Other drivers

Aside from the entrenchment of third party funding, there have been a number of other sustained and long-term drivers for the growing significance of class actions in the Australian legal landscape, including the following:

- a broad range of law firms has seen the significant profit-making opportunities created by class actions and have developed plaintiff-focussed class action practices and relationships with third party funders;
- there has been (and continues to be) a growing focus on corporate governance and the role of private litigation in enforcement – indeed, the heads of some of Australia's peak regulators have openly endorsed the role that class actions play in enforcement and deterrence;
- the introduction of, and amendment to, court procedures, rules and regimes directed at facilitating the bringing of class actions; and
- the increasing number of plaintiff class action practices and the 'light touch' approach to regulation of third party funders has led to additional third party funders entering the Australian market.

The prohibition against misleading and deceptive conduct

Another important factor is Australia's statutory prohibition against misleading or deceptive conduct. In very general terms, in a commercial context, a person will have a statutory cause of action in respect of loss caused by the misleading or deceptive conduct of another. In establishing that cause of action, it is not necessary to prove that the conduct was fraudulent, intentional or negligent – simply that it was misleading or deceptive or likely to mislead or deceive. This enables many causes of action to be brought in Australia that could not be brought in other jurisdictions.

Misleading and deceptive conduct claims are usually the primary basis for shareholder/securities class actions in Australia. In proving those claims it is only necessary to prove that the company misled the market; whether or not the company intended to do so, or was negligent in doing so, is irrelevant. By way of contrast, most similar actions in the United States (including under SEC Rule 10b-5) require proof of scienter (intentional fraud or deceit).

Another telling example is that, in a class action focused on the rating of a structured financial product, the Federal Court of Australia held that Standard & Poor's had engaged in misleading and deceptive conduct in assigning a AAA rating to the product because it misrepresented the risk of default of the product. The Court also found that the arranging bank had engaged in misleading or deceptive conduct by marketing the product by reference to the rating. This was the first case in the world to find that a credit rating was misleading.

Trends in Australian class actions

Unprecedented filings, but not an avalanche

Class action filings have been steadily increasing over the last decade and have reached new heights in the last two to three years. This trend has been driven by new participants to the markets, more than one class action being filed in respect of the same issue and increased regulatory activity (including a Royal Commission into the financial services industry). That said, the level of activity is well short of the avalanche predicted in the mid to late 2000s.

Consuming-facing businesses at highest risk

Consumer class actions have recently overtaken securities class actions as the most common form of new filing. The major contributors to this trend are the post Royal Commission class actions relating to financial products and services; as well as product liability claims against manufacturers of cars and medical devices. Being a consumer-facing business is now the biggest indicator of class action risk in Australia. The banking/financial services and industrials sectors are the sectors most at risk.

Driven by entrepreneurialism

The defining feature of the current class action landscape is increasing entrepreneurialism. More than ever before, class actions are being seen as lucrative profit making enterprises for plaintiff lawyers and litigation funders.

There are, however, also indications that the courts are recognising this trend and taking steps to address some of the most concerning elements. In particular, there are increasing signs that the courts are recognising that class actions are being driven by promoter interests and are looking to restore the focus on class member interests. Generally speaking, we think this trend is also in the interests of class action defendants and will go some way to restoring an effective package of checks and balances.

Potential reform

In 2018, the Australian Law Reform Commission undertook a searching review of class actions and litigation funding practice, and raised some important proposals for consideration – many of which are directed at reining in the effects of entrepreneurialism.

The most important (and controversial) of the ALRC's reform proposals is for a review of continuous disclosure obligations in light of the evolving securities class action landscape.

Some high profile examples

Myer's expected profit growth	In September 2014, retailer Myer Ltd announced its FY2014 results and its CEO told analysts he anticipated profit growth in FY2015. In March 2015, Myer informed the market that its updated FY2015 expectations were well below prior year results. Myer's shareholders brought a securities class action alleging that the September 2014 statements about anticipated profit growth were misleading or deceptive, and a breach of Myer's disclosure obligations. In essence, class members claimed they suffered loss when they purchased shares at an allegedly inflated price caused by the allegedly misleading September disclosure. In October 2019, in the first ever judgment in a securities class action (all prior cases had settled), the Federal Court ruled that, while Myer had misled the market, its share price was not inflated (and therefore class members did not suffer a loss) because market expectations were generally aligned with the true position at all relevant times – to quote the judge 'the market had already deflated [the CEO's] inflated views'.
S&P's AAA rating	Investors in a complex structured financial product that had been assigned a 'AAA' rating by Standard & Poor's alleged that the rating misrepresented the risk of the product defaulting. This was the first case in the world to put a credit rating on final trial. It also raised the question of whether an arranging bank endorses a credit rating in passing it onto potential investors. Judgment was delivered against S&P and the arranging bank. In short, the court found that S&P's rating was 'unjustifiable, unreasonable and unreliable'. It also found that the arranging bank was 'knowingly involved' in procuring the erroneous rating.
Takata airbags	Separate class actions have been commenced against seven car manufacturers in relation to alleged financial losses associated with owning a vehicle that was recalled because it contained a Takata airbag. The cases are listed for hearing in the second half of 2020. The class actions are brought on behalf of all persons who owned recalled vehicles as at February 2018 and allege breaches of the acceptable/merchantable quality protections available to consumers, misleading or deceptive conduct and unconscionable conduct. The alleged losses are the out-of-pocket expenses associated with having the airbags replaced, and an alleged reduction in true value of the vehicle at the time of purchase said to arise from the presence of an airbag that would require replacement (albeit that the airbag would be replaced without charge).
FX (alleged) cartel	In 2019, a class action was commenced against five international investment banks in relation to alleged cartel conduct relating to the pricing of foreign exchange instruments. The claim draws heavily on similar class actions commenced in the United States. The case is still in the very early stages.
Bank fees	In a series of coordinated class actions, bank customers alleged that the exception fees charged by many of Australia's major retail banks were unlawful penalties. In September 2012, the High Court reversed the law of penalties in Australia by finding that the doctrine of penalties may apply outside the context of a breach of contract. In February 2014, the Federal Court decided (in the first of those class actions to go to trial) that only one of the challenged exception fees (late payment fees on credit cards) was a penalty. However, in July 2016, the High Court of Australia held that none of the fees in question were penalties and, as a result, the class actions were abandoned.

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