Senior Associate Jon Downes and Lawyer Matt Warburton review the position in relation to class actions.

Senior Associate Dirk Fairweather and Jonathan de Ridder consider the current status of litigation funding agreements.

Class actions – where are we now?

Class actions have become an established part of the Australian legal system. Indeed, Australia is now the most likely jurisdiction outside North America in which a corporation will face a class action. Whilst class actions have traditionally been commenced in respect of product liability matters, experienced plaintiff law firms are now using this procedure in many different areas. We have already seen claims commenced against major public utilities, financial institutions and government agencies.

Class actions have been brought in relation to products as diverse as weight loss drugs, aircraft fuel, heart pacemakers and oysters. More recently, we have seen class action-based shareholder litigation – something previously unheard of in Australia.

Further, the High Court of Australia has recently affirmed the constitutional validity of the Victorian ‘opt out’ class action regime (see Mobil Oil Limited v Victoria [2002] HCA 27). This may well result in other states implementing similar regimes.

What are class actions?

A class action is a mechanism by which a group of people, having the same interest, can secure a result in one set of proceedings, rather than having to commence separate individual actions. In effect, the claims of numerous individuals are consolidated so that common issues can be tried simultaneously.

There are essentially two class action regimes: the regime available under Part IVA of the Federal Court of Australia Act 1976 (Cth) and that available under Part 4A of the Supreme Court Act 1986 (Vic).

In order to commence a class action under these regimes, it is necessary that:
In cases where the representative of the class is a person or entity of limited resources, security for costs is unlikely to be granted. That said, an order for security for costs was recently made against an incorporated association that had been specifically established for the purpose of commencing a class action against a tobacco company.

A successful defendant may also be able to recover its costs from the plaintiffs’ solicitors. In *Cook v Pasminco Ltd (No 2)* [2000] FCA 1819, the plaintiffs’ solicitors were ordered to pay the defendant’s costs on an indemnity basis because they were found to have given no proper consideration to the question of whether the claim had any prospect of success.

**Challenges to the constitutional validity of class action regimes**

Recently there have been challenges to the constitutional validity of both the Victorian and Federal class action regimes.

In *Bright v Femcare Ltd*, the constitutional validity of the Federal regime was challenged on the basis that the provisions purported to authorise the court:

- To exercise its power in a manner not in accordance with ‘judicial process’.
- To determine issues or questions in circumstances where there is no ‘matter’ within the meaning of Chapter III of the Constitution.
- To exercise power in relation to hypothetical questions.

The Full Federal Court dismissed these arguments and upheld the constitutional validity of the Federal regime.

The constitutional validity of the Victorian regime was challenged in *Mobil Oil Australia Pty Ltd v Victoria*. Mobil put forward similar arguments to those raised in *Bright v Femcare*. The High Court, however, unanimously upheld the constitutional validity of the Victorian regime.

**An unsuccessful class action - Philip Morris (Australia) v Nixon**

The *Nixon* case ([1999] 165 ALR 515) was the first attempt at mass litigation against the Australian tobacco industry. The proceedings were initiated on behalf of some 60,000 people.
The applicants did not specify how each individual applicant had been affected by the tobacco manufacturers’ conduct, but instead looked at the overall effect of the conduct (the ‘broad canvas’ approach).

The Full Federal Court held that the broad canvas approach was confusing and inconsistent. It failed to meet a basic requirement of fairness that the applicants describe their case in sufficient detail to enable the respondents to understand the case made on behalf of the represented class and have a fair opportunity to meet the case.

The decision suggests that representative proceedings are best suited to cases that involve allegations arising out of a single event or a pattern of closely-related conduct occurring over a short period of time.

**A properly constituted class action - King v GIO Australia [2000] 100 FCR 209**

This action related to advice given to shareholders of GIO about a takeover offer by AMP Insurance (AMP). The advice given was that the AMP offer should be rejected. Soon after the close of the offer, GIO revised its loss provisions with the result that its share price fell from $5.35 per share to $2.50 per share. The plaintiffs alleged that GIO and the other defendants had breached s52 of the *Trade Practices Act 1974* (Cth).

The Full Federal Court, in refusing to grant leave to appeal from an interlocutory order dismissing the defendants’ application to strike out the pleadings and/or stay the proceedings, upheld the class action as valid. The Full Federal Court found, inter alia, that the issue of whether the conduct of which the group members complain constitutes misleading or deceptive conduct ‘raises substantial issues of law and fact that are common to the claims against all respondents, including the accessorial respondents’.

**Conclusion**

Whilst the number of class actions is increasing, there have been signs that the courts will limit the type of situations in which class actions will proceed. Furthermore, the courts have indicated their willingness to make adverse cost orders, particularly against plaintiffs’ solicitors, where such proceedings have little or no prospect of success.

However, class actions are still a growing source of exposure. All businesses should identify the areas of risk and assess whether they are appropriately minimising that risk.

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**Litigation funding agreements**

Despite the current debate regarding the increasingly litigious nature of Australian society, the Western Australian Supreme Court recently declined to stay an action brought pursuant to a litigation funding agreement.

**What are litigation funding agreements?**

There are a number of companies in Australia which offer to fund litigation in return for a share of the proceeds if the litigation is successful. Funding agreements with these companies typically provide that the plaintiff will pay nothing if it loses.

**Maintenance and champerty**

Litigation funding agreements may amount to maintenance and champerty. ‘Maintenance’ occurs where a party’s costs are paid by a stranger who has no interest in the litigation. ‘Champerty’ is a form of maintenance where the funder, in return for funding the litigation, is entitled to receive a share of the proceeds if the litigation is successful.

Historically, maintenance and champerty were torts and crimes at common law. However, they have been decriminalised in Western Australia. In New South Wales, Victoria and South Australia, maintenance and champerty are now neither crimes nor civil wrongs.

Nevertheless, a court may still refuse to allow litigation to proceed pursuant to a champertous agreement if it is perceived to be an abuse of the court’s process.

In recent years there have been a number of cases in which the courts have found that insolvency practitioners – administrators, receivers and liquidators – can validly enter into litigation funding agreements. In those cases the courts have had regard to the statutory power of sale given to those persons by the Corporations Act.

The recent decision in *Treacy v Rylestone Pty Ltd* [2002] WASC 178 is significant because it does not rely on what might previously have been described as the ‘insolvency exception’ to the rules against maintenance and champerty.
Treacy v Rylestone Pty Ltd

The Treacy case followed a royal commission into the WA finance broking industry. A group of plaintiff investors had entered into a funding arrangement with a private litigation lending company known as Insolvency Management Fund Limited (IMF). Following its own investigation of the plaintiffs’ claims, IMF retained lawyers to pursue claims against finance brokers and others. IMF agreed to fund the litigation in return for 35% of any favourable judgment plus reimbursement of its costs and disbursements. If the claim was unsuccessful, the plaintiffs would pay nothing.

One defendant applied to stay the proceeding as an abuse of process on the ground that the funding arrangement between the plaintiffs and IMF was tainted by maintenance and champerty.

The application was unsuccessful. Scott J refused to stay the proceeding because the defendant had not shown that IMF was inappropriately interfering in the proceeding (for example by influencing the plaintiffs and their lawyers regarding the prosecution of their case). Although Scott J thought the funding agreement left it open for such interference to occur, there was no proof of actual interference.

Scott J considered that the law relating to maintenance and champerty is informed by public policy and that this is a fluid concept. In his view, as a matter of public policy, the possibility of trafficking in litigation is outweighed by the need for people with valid causes of action to access the courts.

Costs against litigation funders

Moreover, if a plaintiff’s claim fails, the successful defendant may be able to recover its costs from the funder of the litigation. In the recent case of Gore (trading as Clayton Utz) v Justice Corp Pty Limited [2002] FCA 354, the Federal Court ordered the litigation funding company (Justice Corp) to pay the successful defendant’s (Clayton Utz’s) costs even though Justice Corp was not a party to the litigation.

In substance, the court in Gore held that, where a non-party to the litigation enters into a commercial arrangement whereby it stands to benefit from a favourable judgment, that non-party should be at risk of paying the defendant’s costs if the claim is unsuccessful.

Conclusion

Where a litigation funder is shown to be interfering in the prosecution of the case, it is more likely that the proceedings will be found to be an abuse of the court’s process, and be permanently stayed. However, it will generally not be easy for a defendant to lead evidence of actual interference by the funder, given that it will not have full details of the arrangements and dealings between a plaintiff, a funder and the plaintiff’s lawyers.

Scott J’s comments about the contemporary public policy considerations underlying maintenance and champerty have significance in all Australian jurisdictions.

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