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The Price of Access to the Civil Courts in Australia: Old Problems and New Solutions - A Commercial Litigation Funding Case Study

Camille Cameron

Chapter 2
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2.1 Introduction

Like many of the jurisdictions considered in this volume, Australia struggles with how best to manage and control the cost of civil litigation. The purpose of this chapter is to explore the connections between the cost of litigation and Australia's cost and fee allocation rules. Section 2.2 provides a broad overview of those rules and related practices. Only the key features are mentioned; readers can refer to the "Country Report" for additional details.[1] In Section 2.3 the rise of commercial litigation funding in Australia is discussed. The prominent place it has assumed in the litigation landscape in a relatively short period of time is attributable to key features of Australia's cost and fee allocation rules. It is therefore a window through which we can get a clear view of those rules. Section 2.4 offers some final analysis and conclusions.

[1] *See* http://www-personal.umich.edu/~purzel/national_reports/. The focus in this chapter is on litigation in the superior courts. There are small claims courts and tribunals that deal with minor civil disputes. Some features of those tribunals include restrictions on legal representation and rules that the parties should bear their own costs. Many of the costs and funding issues considered in this paper would therefore not be relevant in those courts and tribunals.

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2.2 Overview of Litigation Funding and Costs in Australia[2]

The costs-shifting ("loser pays") rule applies in Australia. Successful litigants can expect an order for reasonable costs, called party and party costs.[3] This is not, however, a complete recovery. There will in most cases be a substantial gap between the costs expended by successful parties and the costs they can recover. The irrecoverable portion of the successful party's costs is estimated to be in the range of 40–50%. Anecdotal evidence suggests that this figure may vary depending on whether a particular jurisdiction has prescribed scales of costs.[4]

It is possible in some cases to get an order that costs will be paid on an indemnity basis. This is virtually a full recovery, but such orders are not easy to obtain. There must be some special or unusual feature in a case to justify an order for indemnity costs, such as delay or non-compliance on the part of the losing party. There are also provisions in the procedural rules relating to formal settlement offers that provide for an indemnity costs order where a defendant refused a reasonable settlement offer.[5]

There is a particular view of fairness informing some of the justifications for the loser pays rule – it would be unfair for a successful plaintiff whose claims have been vindicated or for a successful defendant who had no real choice but to incur the cost of defending the claim, to have to absorb the litigation costs. But of course the fairness arguments cut both ways. Costs shifting has also been described as "a crude exclusion device the burden of which falls disproportionately on individuals and community groups which do not have the same deep pockets as governments and corporations."[6] In its 1995 report on costs shifting the Australian Law Reform Commission

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[2] Some of the content in this Section is adapted from Camille Cameron, ch 6, *Australia*, in C. Hodges et al, eds, *The Costs and Funding of Civil Litigation, A Comparative Perspective*, Hart, November 2010.

[3] Exceptions to the loser pays rule include costs penalties for refusing a reasonable settlement offer, tribunals and small claims jurisdictions in which the norm is no costs shifting, costs orders where a party has had mixed success, and the willingness of courts in an appropriate case to exercise their costs discretion in favour of an unsuccessful public interest litigant.

[4] Scales of costs are prescribed amounts for court fees and other expenditures, usually contained in schedules or appendices to Rules of Court. In the State of New South Wales, where there are no such scale costs, estimates are that successful parties will recover 65–85% of their actual costs: Lord Justice Jackson, *Review of Civil Litigation Costs, Preliminary Report*, May 2009.

[5] In the State of Victoria, for example, if a defendant in a personal injury case rejects the plaintiff's settlement offer, and the plaintiff does as well or better at trial than the offer, the usual order will be for costs to the plaintiff on an indemnity basis. *Supreme Court General Civil Procedure Rules 2005*, Rule 26.08(2).

[6] Victorian Environmental Defender's Office, quoted in Victorian Law Reform Commission, *Civil Justice Review, Report, 2008* (VLRC Civil Justice Review 2008).

stated that submissions made during the consultation process indicated that the costs shifting rule is most likely to deter "people who may suffer substantial hardship, such as the loss of their home, car or livelihood, if required to pay the other party's costs, and people or organisations involved in public interest litigation who have little or no personal interest in the matter."[7] This view is shaped less by ideas of adversarial contest, reward and vindication and more by ideas of access to justice and to the courts. Whatever its justifications, the cost shifting rule is an entrenched feature of civil procedure in Australia and not likely to be easily displaced. Almost all major reviews of civil justice in Australia have favoured its retention.[8]

All Australian courts charge fees prescribed by statute.[9] Typical charges are for filing documents in court, issuing a subpoena, using court mediation services, and daily fees for court hearings. Australia does not have a true user pays system. The fees charged for these and similar services fall well below the actual cost of maintaining courts. For example, the Commonwealth of Australia reported in 2009[10] that court fees charged by the Federal Court amounted to 9.3% of total Commonwealth expenditure on that court.[11]

The costs between lawyers and their clients consist of the lawyers' fees and disbursements. The primary method of charging clients is by time billing based on an hourly rate. There are some exceptions to the hourly rate approach, however, and these may be increasing. Fixed fee agreements for specific services or discrete tasks, such as preparing a will or a contract, are common. Some commercial clients use their market power to demand alternatives to hourly billing, and law firms have responded to this market demand by bidding for legal services. This can be in the form of an agreed amount for a project or for parts of (or events within) a project.

Another common billing arrangement is the conditional fee (also called "no win-no fee"). Lawyers using this model agree not to bill the client until the case is resolved. If the client is successful, then the lawyer will be paid his fees, either calculated on an hourly basis or at an amount agreed

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[7] Australian Law Reform Commission, *Cost Shifting – Who Pays for Litigation in Australia?* 1995 (*Cost Shifting 1995*) at [4.14].

[8] In *ALRC Cost Shifting 1995*, the Australian Law Reform Commission endorsed the loser pays rule but recommended that courts should be able to depart from the rule if "a party's ability to present his or her case properly or to negotiate a fair settlement is materially and adversely affected by the risk of an adverse costs order." [12.40] This proposal has not been adopted.

[9] See for example *Federal Court of Australia Act 1976 (Cth)*, s. 60 and *Federal Court of Australia Regulations 2004 (Cth)*, Schedule 1.

[10] *Commonwealth Access to Justice Report 2009*.

[11] *Commonwealth Access to Justice Report 2009*, ch 3, p 45, quoting the Productivity Commission, *Report on Government Services*, 2009. The percentage of recovery varies across federal courts.

in advance between the lawyer and the client (but not as a percentage of the damages awarded). If the client is unsuccessful, the lawyer will not be paid. The risk of an adverse costs order, always a factor in a system with costs shifting, remains with the client.[12] These conditional fee agreements often include a term that the lawyer will in the event of a successful outcome charge a premium, also known as an uplift (success fee). This fee is a matter between the lawyer and her own client; it is not recoverable from the opposing party. The maximum uplift fee permitted in Victoria and New South Wales is 25%.[13] There is some evidence to indicate that in personal injury cases in Victoria, claimants receive 80–85% of their damages, after deduction of the success fee.[14]

2.3 Commercial Litigation Funding

Commercial litigation funders have a significant and growing presence in Australia. The need for commercial litigation funders exists primarily because of gaps in the market created by the costs shifting rule and the prohibition against lawyers charging contingency fees.

The role of litigation funding companies in Australia in litigation other than insolvency cases was, until recently, uncertain. Their legitimacy was challenged on the basis of maintenance (improperly encouraging litigation), champerty (funding a third party's litigation for profit) and abuse of process, and there were conflicting judicial decisions.[15] In 2006 the High Court of Australia resolved the conflict by endorsing the role of institutional litigation funders.[16] The trial judge had accepted arguments that the litigation funding agreement was invalid because it amounted to "trafficking in litigation". The Court of Appeal reversed the trial judge's decision and described a need for a change in attitudes about litigation funding. In the Court of Appeal, Mason P stated:

> These changes in attitude to funders have been influenced by concerns about access to justice and heightened awareness of the costs of litigation. Governments have promoted the legislative changes in response to the spiralling costs of legal aid. Courts have recognised these trends and the matters driving them. 'Ambulance chasing' still has negative connotations in many quarters, but it is now

[12] Unlike England, there is no market for "After the Event (ATE)" insurance in Australia to cover the adverse costs risk.

[13] State practice varies. Recovering a success fee under a conditional fee arrangement is more common in Victoria than in New South Wales.

[14] Lord Justice Jackson, *Preliminary Report*, 2009 (n 28), ch 58, p 588.

[15] The key cases are discussed in *Fostif v. Campbells Cash and Carry Pty Ltd* [2005] NSWCA 83, [2005] 63 NSWLR 203.

[16] *Campbells Cash and Carry v. Fostif* [2006] HCA 41.

> widely recognised that there are some types of claims that will simply never get off the ground unless traditional attitudes are modified. These include cases involving complex scientific and legal issues. The largely factual account in the book and film *A Civil Action* has demonstrated the social utility of funded proceedings, the financial risks assumed by funders, and the potential conflicts of interest as between group members in mass tort claims propounding difficult actions against deep-pocketed and determined defendants.[17]

The High Court, without responding specifically to these comments, endorsed the legitimacy of the commercial litigation funding arrangement. The *Fostif* decision gave an already emerging litigation funding market a substantial boost.[18]

There are at least six litigation funding companies operating in Australia. Two of these companies, IMF (Australia) Ltd and Hillcrest Litigation Services Ltd are listed on the Australian Securities Exchange. Of these, IMF is the most visible. It began its litigation funding activities in insolvency cases, but has assumed a growing presence in large commercial cases and in securities class actions. When IMF expanded its litigation funding activities beyond insolvency cases to other commercial litigation and securities class actions, it was gambling that traditional views about maintenance and champerty would be displaced by acceptance of "the social utility of litigation funding."[19] Subsequent jurisprudence, culminating with the 2006 High Court decision in *Fostif*,[20] has vindicated this view. A review of IMF's business model and practices offers some insight into how the litigation funding market in Australia operates.

When it listed on the Australian Stock Exchange in 2001, IMF included in its investment protocol a minimum case size restriction of $2 million. It takes the view that funding smaller claims is commercially unviable. This decision was a response to its previous experience of cases in which too much of the settlement or judgment sum was taken by legal costs and the fees of lawyers and IMF.[21] It makes an exception for small claims that can be prosecuted as a group action; aggregation of many small claims converts single unviable claims into a commercially viable group action.

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[17] *Fostif v. Campbells Cash and Carry* [2005] 63 NSWLR 203.

[18] Another factor contributing to the growth of commercial litigation funding has been the effort of plaintiff lawyers to prosecute class actions.

[19] John Walker, *Litigation Funding*, presentation to the AILA (Australian Insurance Law Association) National Conference, 2006, available at http://www.aila.com.au/speakersPapers/downloads/2006_Conference/06-11-01_John_Walker.pdf last accessed on 26 April 2011. These words were also used in 2005 by Mason P in *Fostif v. Campbells Cash and Carry*: see above note 16.

[20] *Campbells Cash and Carry Pty Limited v. Fostif Pty Ltd* [2006] HCA 41; (2006) 229 CLR 386.

[21] Ibid, and information provided by IMF to the author.

Other factors determining IMF's case choice, in addition to claim size, are:

- the likely investment is less than 10% of IMF's current assets or facilities;
- net return to the plaintiff must be greater than 60%;
- IMF's return on investment must be at least 300%; and
- cases must rely mainly on documentary rather than oral evidence.[22]

Assuming the case meets the factors listed above, IMF then conducts a rigorous analysis of the claim, defence, parties, and costs. The analysis includes estimates of the likely duration and cost of the entire litigation and of separate components of the case. The risks assumed by a litigation funder in exchange for a percentage of the settlement or judgment sum include paying any order for security for costs and paying the defendant's costs if the claim fails.

If a case passes these tests, the funded parties sign a funding agreement in which they agree that IMF will take a percentage of the settlement or judgment sum, in the range of 20–40%.[23] In return, IMF agrees to pay the claimant's legal fees and disbursements, to assume the risk of and to pay any adverse costs order, to pay security for costs if ordered, and generally to assist with project management. Information this author has obtained in connection with a related research project indicates that some funders take an active role in the management of cases but that this can vary as between funders, and even between claims managers working for the same funder.[24]

As few cases will meet IMF's investment protocols, it follows that commercial litigation funding will not provide access to justice for most claims. This is left to lawyers who are willing to take smaller or riskier cases on a no win, no fee basis. There is some anecdotal evidence, however, that the entry of commercial litigation funders into the civil litigation landscape has had a detrimental effect on the willingness of lawyers to run cases on a no win, no fee basis. If lawyers can choose cases that funders are willing to underwrite, they may be inclined to reduce their portfolio of no win, no fee cases.[25]

Commercial litigation funding exists and thrives in Australia because of certain conditions in the market for legal services. One of these is that

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[22] Ibid.

[23] Hillcrest Litigation Services Limited declares a range of 25–45% in its 2010 *Annual Report*.

[24] *The Role of Institutional Litigation Funders in Australia*, made possible with funding provided by the Melbourne Law School. This variation among claims managers is one example of how the practice of litigation funders is akin to that of insurers.

[25] One experienced litigation solicitor interviewed in relation to other research the author is conducting (see above note 24) expressed the view that this shift is occurring.

Australian lawyers are prohibited from charging contingency fees. If that restriction were removed, plaintiff lawyers who presently depend on litigation funders might be more willing to accept the risk themselves. This is, however, subject to a substantial caveat. As long as costs shifting remains – and it will – there will be relatively few law firms with the resources to take on the added risk of an adverse costs order, at least in large commercial litigation and in many class actions. This may create a market for litigation insurance that caters for the risk of adverse costs. Unlike some of the other jurisdictions considered in this book, after-the-event and before-the-event litigation insurance have not yet flourished in Australia.

Commercial litigation funding is attractive for other reasons as well. The priority it accords to realistic case budgets appeals to many commercially-minded litigants intent on managing the risks created by the unpredictability of fees and costs. This feature of litigation funding has also been commented on favourably by Australian judges. In *QPSX*, for example, French J stated:

> Where [litigation funding agreements] involve the creation of budgets by funders knowledgeable in the costs of litigation it may inject a welcome element of commercial objectivity into the way in which such budgets are framed and the efficiency with which the litigation is conducted.[26]

A recent procedural reform in the State of Victoria picks up on this sentiment. Section 50 of the *Civil Procedure Act 2010* gives a court the power to order a lawyer to prepare a budget that states the estimated duration of a trial, the estimated costs and disbursements, and the estimated amount of any adverse costs order.

Canadian, American and European funders are becoming interested in the Australian market.[27] For example, International Litigation Funding Partners Pte Ltd, a Singapore-based company in which a Canadian law firm has a substantial interest, funded the *Multiplex* securities class action.[28] That case became the vehicle, over several years, for some major judicial

[26] *Civil Procedure Act 2010 (Vic)*.

[27] In 2006, it was estimated that 95% of the litigation funding business in Australia was done by 6 or 7 Australian litigation funding entities then operating. The gradual entry of non-Australian funders into the market in the intervening 4–5 years will have altered this estimate. The interest in foreign markets works both ways. In its *Annual Report* for 2010, at p 4, IMF refers to its "entry into offshore markets, including the United States and United Kingdom markets" (see also p 58). The report is available at http://www.imf.com.au/pdf/AnnualReport2010.pdf, last viewed on 26 April 2011.

[28] This was a class action by shareholders against Multiplex for damages for losses allegedly caused by the company's belated disclosure of cost problems related to the construction of the Wembley Stadium.

and policy clarifications of the proper role and limits of commercial litigation funding. Two outcomes of that case with significance for litigation funding deserve brief mention.[29]

Any expectation that it would be smooth sailing for litigation funders post-*Fostif* were dashed when the Full Court of the Federal Court ruled (2-1) in *Brookfield Multiplex*[30] that the arrangement in that case between the commercial litigation funder, the law firm representing the class, and the members of the class was a managed investment scheme as defined in the *Corporations Act*.[31] One ramification of that decision was that the arrangement should have been registered under the relevant provisions of the *Corporations Act*. Another was that the impact of the decision extended beyond the boundaries of the particular case. There were other funded class action proceedings underway that had not been registered as managed investment schemes. The Australian Securities and Investments Commission intervened to grant a temporary exemption for the class actions affected.[32] Discussions then began about how best to respond to the decision. One possible outcome was that the matter would go to the High Court of Australia. A more expeditious outcome was realized when the Federal Government introduced a regulation to reverse the effects of *Brookfield Multiplex* by excluding funded class actions from the definition of a managed investment scheme. This was the best outcome. The cost of a further appeal to the High Court was averted, and the new regulation clarified the confusion that *Brookfield Multiplex* had created. Most knowledgeable observers thought that classifying the funder/lawyer/class arrangement as a managed investment scheme was akin to trying to put a square peg into a round hole.[33]

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[29] It is beyond the space constraints of this chapter to do anything other than a cursory overview of the case and its consequences. For additional information see: *Multiplex Funds Management Ltd. v P Dawson Nominees Pty Ltd* [2007] FCAFC 200 (appeal dismissed, *P Dawson Nominees Pty Ltd v. Multiplex Ltd* [2007] HCA 1); *Brookfield Multiplex Limited v. International Litigation Funding Partners Pte Ltd* (2009) 180 FCR 11; *Brookfield Multiplex Limited v. International Litigation Funding Partners Pte Ltd (No 2)* [2009] FCAFC 147.

[30] *Brookfield Multiplex Limited v. International Litigation Funding Partners Pte Ltd (No 2)* [2009] FCAFC 147. This is a representative proceeding (i.e., a class action) by shareholders against Brookfield Multiplex for damages for losses allegedly caused by the company's belated disclosure of cost problems related to the construction of the Wembley Stadium.

[31] *Corporations Act 2001* (*Cth*).

[32] See ASIC media release, November 2009, 09-218MR, *ASIC grants transitional relief from regulation for funded class action*, available at http://www.asic.gov.au/ (under Publications – Media Centre), last viewed on 26 April 2011.

[33] Information obtained by author in connection with research project referred to in note 24, above.

A second, very significant contribution of the *Multiplex* securities class action came with the decision of the Federal Court in *Multiplex Funds Management Ltd v. P. Dawson Nominees Pty Ltd.*[34] As a result of that decision, it is possible to have as one element of the definition of a class the requirement "and have signed a funding agreement with [Funder X]". The validity of this approach was challenged on the basis that it created an impermissible opt in requirement in what is an opt out system, because people were being asked to take the specific step of signing the funding agreement as a condition of being in the class. Initial judicial decisions in the Federal Court and the Supreme Court of Victoria were to the effect that these clauses were inconsistent with the opt out nature of the class action legislation. In this *Multipex* decision, however, the validity of such clauses was endorsed. The court found that the language of the legislation did not prohibit such an arrangement. It was relevant that people signed the funding agreement before the class action was commenced, which meant that when they signed there was not yet any class action into which a person could opt (thus avoiding the opt in criticism).

One result of this decision is that closed classes are permissible. There are good reasons for commercial litigation funders to prefer this approach. They take on a substantial risk when they fund a class action, including the obligation to pay the defendant's costs if the class action fails. The signed agreements with class members provide certainty and give them the assurance that they will be paid in the event of success.

Whatever one's view of these *Multiplex* decisions, they highlight the ad hoc way in which commercial litigation funding has been developing in Australia. In 2006, regulation of commercial litigation funders was explored by the Standing Committee of Attorneys General,[35] with no specific regulatory outcomes. Nothing has been done since that time to put in place any regulatory framework. It has been left primarily to the courts to define the proper scope and boundaries of commercial litigation funding. This is how regulation is happening, and views vary about whether this is sufficient. Some lawyers are of the view that no additional regulation is needed; where conflicts between lawyers and funders emerge, they say, lawyers will be robust enough to behave in the interests of their clients and, where necessary to stand up to the funders. Others decry the incongruous, or perverse, situation in which lawyers, who have a duty to the court, are prevented by law from charging contingency fees while litigation funders, who have no such duty, are able to do so. But apart from intervening to remedy the *Brookfield Multiplex* problem, it appears there is nothing, yet, about the

[34] [2007] FCAFC 200.

[35] *Litigation Funding in Australia*, Discussion Paper, Standing Committee of Attorneys General (SCAG Report 2006).

way litigation funding is operating to convince regulators that any further public regulatory intervention is required.

In addition to their role as key players in the "extraordinary" jurisprudential developments that occurred in *Multiplex*, litigation funders are increasingly prominent in more ordinary, run-of-the-mill decisions. This reflects the degree of control litigation funders have assumed in litigation – control made possible by the imprimatur given by the High Court in *Fostif* to their robust participation in the cases they fund. In *Pharm-a-Care Laboratories*,[36] for example, court approval of a class action included consideration of the fairness and reasonableness of the percentage of the settlement amount that would go to the litigation funder. And it is increasingly common to see discussions in cases about how much of the information disclosed by the defendant to the plaintiff will be available to the litigation funder.[37]

Civil justice reforms are reflecting the new reality of litigation funders who like the degree of control approved in *Fostif*, and who use it. In the State of Victoria, for example, new statutory obligations aimed at improving the conduct of civil litigation apply not only to parties and their lawyers but also to litigation funders and insurers.[38]

2.4 Conclusion

The rise of commercial litigation funding in Australia is a predictable result of the interaction of a variety of factors, including costs shifting, the prohibition on lawyers charging contingency fees, the hourly billing practices of lawyers, and the open-ended and unpredictable nature of civil litigation. Litigation is expensive, especially complex commercial litigation and class actions, and few Australian law firms have the resources to finance such cases themselves. Commercial litigation funders saw an opportunity to use the expertise they obtained in insolvency litigation in new categories of cases. Their efforts have been greatly assisted by favourable court decisions and the maturing of Australia's class action regimes.

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[36] *Pharm-a-Care Laboratories Pty Ltd v. Commonwealth of Australia* (No 6) [2011] FCA 277.

[37] See for example *Cadence Asset Management Pty Ltd v. Concept Store Ltd* [2006] FCA 711; *QPSX Limited v. Ericsson Australia Ltd (No 5)* [2007] FCA 244; and *Kirby v. Centro Properties Limited* [2009] FCA 695.

[38] See for example s. 10, *Civil Procedure Act 2010 (Vic)*. This was one of the reforms that the Executive Director of IMF called for in his 2006 AILA presentation: see above note 19.