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13 November 2018

The Hon Justice Sarah Derrington
President
Australian Law Reform Commission
GPO Box 3708
SYDNEY NSW 2001

via email to class-actions@alrc.gov.au

Dear Justice Derrington

Inquiry into Class Action Proceedings and Third-Party Litigation Funders

Thank you for the opportunity to provide a supplementary submission to the Australian Law Reform Commission (**ALRC**) Inquiry into Class Action Proceedings and Third-party Litigation Funders.

The Australian Institute of Company Directors (**AICD**) has a membership of more than 43,000 including directors and senior leaders from business, government and the not-for-profit sectors. The mission of the AICD is to be the independent and trusted voice of governance, building the capability of a community of leaders for the benefit of society.

We have confined our comments in this supplementary submission to the sections of the *Inquiry into class action proceedings and third-party litigation funders: Discussion Paper 85* (**Discussion Paper**) published by the ALRC relating to:

- the proposed review of the economic and legal impact of continuous disclosure obligations and misleading and deceptive conduct provisions (Proposal 1-1);
- additional regulation of litigation funders (Proposal 3-1 and 3-2); and
- a federal collective redress scheme (Proposal 8-1).

Review of the continuous disclosure obligations and misleading and deceptive conduct provisions (Proposal 1-1)

The AICD strongly supports robust continuous disclosure requirements for listed entities. Continuous disclosure is an essential component of a fair and efficient securities market. A fully-informed and well-functioning securities market promotes trust and confidence in the integrity of Australia's financial markets, and we do not support any dilution of the principles of continuous disclosure.

However, as stated in our submission dated 30 July 2018, the AICD strongly supports the proposed review of the legal and economic impact of continuous disclosure obligations and provisions relating to misleading or deceptive conduct on listed entities, particularly in the context of their interaction with Australia's class actions market.

The AICD is particularly concerned that the interaction between Australia's strict continuous disclosure laws and misleading or deceptive conduct obligations, combined with a well-developed and active class actions market, is driving unintended consequences, including:

- causing economic damage to long-term shareholders;
- distracting boards from their core duties;
- diverting company resources from investment opportunities to legal costs;
- driving overly conservative disclosure decisions by directors which would otherwise not be required by the relevant market operator's listing rules; and
- imposing high transaction costs on plaintiff class members.

The interaction between continuous disclosure and misleading or deceptive conduct laws, and the class actions market, must also be considered in light of the following factors:

In the context of an allegation of a breach of continuous disclosure laws, there is considerable uncertainty regarding the bounds of the law, and how any damages should be calculated. This is principally a result of the fact that no securities class actions are reaching final judgment. It is not helpful to anyone that the boundaries of continuous disclosure laws remain so unclear. The lack of any final judgments should also be understood in the context of the considerable incentive third party litigation funders have to settle securities class actions quickly and thereby reduce their costs and risk exposure.

Australia's continuous disclosure obligations are particularly strict, and provide no defence or carve out for the listed entity in the event it used all reasonable care and diligence in its efforts to comply with the relevant obligation, or deployed cautionary language in its projections. This is in contrast to comparable jurisdictions such as the United States, which provide for some measure of safe harbour or other protection is afforded the entity in the context of civil litigation. Nor does Australia provide any safe harbour exemption or defence for statements about future matters, in contrast to overseas jurisdictions, such as the United States and Canada, which provide protection for statements made with reasonable cautionary language.

Achieving compliance with continuous disclosure obligations is a particularly challenging exercise for company directors. Indeed, the challenges of achieving compliance were acknowledged by the Australian Securities and Investments Commission (**ASIC**) Commissioner John Price in a speech of 3 December 2012, where he stated that ASIC acknowledges the "delicate balancing act" that companies must undertake to comply with continuous disclosure obligations", and that ASIC "thinks very carefully before taking any action on continuous disclosure breaches under s 674".[1] The AICD understands that many company directors of listed entities are finding it very difficult, if not impossible, to ensure

[1] Speech by ASIC Commissioner, John Price, delivered at the Chartered Secretaries Australia, 2012 Annual Conference, 3 December 2012.

their entity is achieving ongoing comprehensive compliance with the continuous disclosure regime, despite their best intentions.

Continuous disclosure is critical to the functioning of equity markets. For these reason, a review presents a good opportunity for the government to examine whether the way in which Australia's continuous disclosure and misleading and deceptive conduct obligations, combined with our facilitative class actions market, are operating in the public interest. The AICD does not consider there to be any appreciable downsides to the review proposed by the ALRC. It provides an opportunity to ventilate the arguments being put forward by a number of parties in the context of the ALRC inquiry in a more fulsome manner. We particularly note the support for Proposal 1-1 of the Discussion Paper by the Australian Securities Exchange and the Corporations Law Committee of the Law Council of Australia.[2]

Against this backdrop, the AICD reiterates its strong support for Proposal 1-1, and we would be pleased to participate in such an inquiry, should the government agree to such a recommendation.

Additional regulation of litigation funders

The AICD reiterates its strong support for the introduction of appropriate licensing regime for litigation funders, which goes beyond the need to have conflicts of interest arrangements in place, as is presently the case under the *Corporations Regulations 2001* (Cth). Industry regulation alone will not adequately address the concerns already outlined by the AICD and other submitters relating to consumer protection, competition, conflicts, and prudential soundness associated with third party litigation funders.

In relation to the question of which regulatory model is ideal, the AICD's long-standing preference has been for the introduction of a customised licensing regime included within Chapter 7 of the Corporations Act. This enables the license to be crafted to meet the requirements of the industry in its particular circumstances. While this remains our preference, the AICD is supportive of any model which would ensure that the litigation funding market operates in the best interests of the public at large, with consideration given to the interests of class members in a class actions scenario, and with adequate prudential supervision. If leveraging off an existing licensing regime, such as the Australian Financial Services Licensing regime, would be effective, than that would be preferable to industry self-regulation.

A federal collective redress scheme

The AICD agrees with the ALRC that the establishment of an alternative to class action litigation for those who may be entitled to a remedy by reason of the conduct of a corporation has the potential to provide access to justice while reducing some of the downsides associated with litigation, and particularly class actions litigation.

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[2] Patrick Durkin and Michael Pelly, 'ASX backs continuous disclosure review', *Australian Financial Review,* 20 June 2018.

For this reason, the AICD supports, in principle, the proposal for the government to consider establishing a federal collective redress scheme. However, the AICD would need to see greater details of any proposal before providing its unqualified support.

In terms of the principles which should guide the design of a federal collective redress scheme, the AICD agrees with the suggestions of Law Firms Australia that a redress scheme should:[3]

(a) Provide finality and certainty for the potential defendant implementing the scheme;

(b) Be voluntary for the potential defendant;

(c) Not require the potential defendant to make an admission of liability (or any other admissions);

(d) Allow communications with the regulator to remain confidential; and

(e) Give rise to the potential for lower regulatory penalties in recognition of the potential defendant's willingness to voluntarily provide redress.

Next steps

We hope our comments will be of assistance. If you would like to discuss any aspect of this submission, please contact Matt McGirr, Policy Adviser, on (02) 8248 8431 or mmcgirr@aicd.com.au.

Yours sincerely,

LOUISE PETSCHLER
General Manager, Advocacy

[3] Law Firms Australia, Submission, *Inquiry into Class Action Proceedings and Third-Party Litigation Funders,* 6 August 2018.