

A common fund order, or is it?

The Full Court of the Federal Court of Australia in *Money Max Int Pty Limited (Trustee) v QBE Insurance Group Limited*¹ has proposed a "Common Fund" order in relation to the funding commission payable from recoveries by group members in a shareholder class action. However, questions remain about whether the order is quite the win for litigation funders that it may initially appear to be.

Funding of class actions

Class actions in Australia are increasingly supported by litigation funders, but generally only if they consider it is commercially viable to do so – the return must exceed the risk.

To achieve a return, the funders enter into agreements with individual group members whereby the funder agrees to meet the costs of the litigation and the group member agrees to pay a funding commission (being a percentage of any recovery they obtain).

Class actions are commenced on either:

- a closed basis – where all group members have entered into funding agreements (**funded group members**); or
- an open basis – where there are some funded group members and also some group members who have not entered into funding agreements with the funder (**unfunded group members**).

Unfunded group members are entitled to the fruits of the open class action, but do not have any obligation to pay commission to the funder. It is only

the funded group members which have that obligation.

To achieve equality between funded group members and unfunded group members, the Courts have previously made "funding equalisation" orders as part of a settlement of a class action. The effect of such orders is to redistribute an amount equivalent to the commissions that would have been payable by unfunded group members (had they entered into funding agreements) between all group members.² The total commission payable to the funder does not change, but effectively all group members proportionately contribute towards its payment.

"Common fund" orders

Common fund orders, in essence, have the effect of applying litigation funding terms to all group members in a class action, including unfunded group members.

Common fund orders of this kind would have particular advantages to a funder if sought early in a class action (rather than at the time of settlement) as:

- the litigation funding terms apply to all group members without the funder needing to reach

Key issues

- the Full Court of the Federal Court has approved a "common fund" approach to the funding of open class actions.
- the "common fund" approach is a significant development in class actions and was expected to increase the number of class actions in Australia.
- the form of orders proposed by the Full Court does not provide many of the advantages previously expected from a "common fund" approach and, once considered further, may not be pursued by funders as much as expected.

individual agreements with all of group members;

- the total commission payable to the funder is increased, as all group members are bound to pay a percentage of recoveries as commission;
- the percentage commission payable by group members is approved by the Court early in the proceedings; and

- the funder has certainty early in the proceedings as to its likely return in the event of a settlement or judgment.

Common fund orders of this kind are not however to the benefit of unfunded group members, and do not have a significant benefit to the funded group members. That is because whilst the order does achieve equality, it does so by increasing the total amount payable to the funder.

A common fund order of this kind was sought in *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed)(In Liq)*.³ Justice Wigney declined to make the order, finding that the order sought would not be in the best interests of the group members and that the motivation for seeking the order was the commercial interests of the funder.

QBE proceedings

Money Max Int Pty Ltd v QBE Insurance Group Limited is a class action in which shareholders of QBE allege that in connection with the performance of its North American business QBE engaged in misleading and deceptive conduct and breached its continuous disclosure obligations. The proceedings are brought on an open class basis - there are both funded and unfunded group members.

The Applicant (which is funded) filed an application seeking the making of a common fund order which was opposed by QBE. The Chief Justice of the Federal Court referred the application to the Full Court for hearing and determination.

By the time of the hearing, the Applicant sought:

- as its preferred position, an order that all group members be

required to pay the funder a funding commission of 30% of their recoveries (which was a reduction of in the commission agreed with funded group members, which was 32.5% or 35% depending on how many QBE shares were acquired in the relevant period); and

- as a fallback position, an additional order that the amount payable by group members pursuant to the first order could not exceed what would otherwise be payable had the order not been made.

The additional order was to act as a cap on the amount payable pursuant to the common fund order, and required a comparison between what was payable by group members under the common fund order and what would be payable by group members had no common fund order been made.

It appears that if there was no common fund order, only the funded group members who had entered into agreements with the funder are required to pay a funding commission. In those circumstances, the common fund order would be capped at the commission payable under those existing agreements.

The Full Court (Murphy, Gleeson and Beach JJ) considered the merits of a common fund order in detail and have indicated that they propose to make orders (subject to the funder giving an undertaking to meet funding obligations):

- requiring all group members to pay a funding commission at a percentage of recoveries to be determined by the Court (at a later stage, probably at

settlement approval or distribution of damages); and

- that the amount payable by group members cannot exceed what would otherwise be payable had the order not been made (providing the cap).

The Full Court has invited the parties to file and serve proposed forms of these orders.

Whilst the final orders have not yet been made, the form of orders proposed by the Full Court would not appear to provide the funder with the benefits ordinarily associated with a common fund order. In particular:

- the percentage commission payable by group members is not certain, even in respect of funded group members who have already entered into agreements with the funder at specified percentages;
- the total commission payable to the funder has not increased, and in fact may decrease, as the funding commission is capped at the amount payable had the order not be made;
- the funder may still need to attempt to reach individual agreements with all group members as that is the only way to increase its funding fee, in circumstances where those unfunded group members may have little incentive to enter into those agreements; and
- the funder does not have certainty as to its likely return in the event of a settlement or judgment.

As such, the benefit, if any, to the funder from the orders proposed by the Full Court appears to be questionable.

The primary beneficiary of the proposed orders are the funded group members who have certainty, at an early stage, that the funding fees payable pursuant to their contractual arrangements will in effect be paid proportionately amongst group members and may in aggregate be reduced by the cap.

Implications

The orders proposed by the Full Court are not, in substance, a common fund order of the kind previously sought by parties to class actions (and indeed, no parties to *QBE* sought the orders proposed by the Full Court).

Whilst the proposed orders do require all class members to pay a funding commission unless they opt out, the funding commission will be at a reasonable rate determined by the Court. This approach shows that the Court will clearly take a more interventionist approach to funding agreements.

The Court has also indicated that it is unlikely that the funding commission approved by the Court will be at the level originally agreed with funded group members. The funding commission also cannot in aggregate exceed the amounts that would have been payable by funded group members pursuant to their funding agreements.

In this sense, the proposed orders are more akin to a funding equalisation order, but with the added element of the Court determining (rather than just approving) the funding commission rate.

The Full Court appears to have acknowledged in its judgment that the orders it proposes do not provide the funder with the benefits it might have wished to obtain, and it is possible the funder will not give the undertaking that is required by the Court for the proposed orders to operate.

Common fund orders have previously been considered to be in the interests

of funders and likely to encourage funders to commence class actions on an open basis (as opposed to closed class actions). This has in turn given rise to concerns of a flood of additional class actions as funders seek the commercial benefits of the common fund order.

In what may be viewed as an ironic outcome, if the orders proposed by the Full Court in *QBE* are made, the decision may well discourage funders from seeking common fund orders and may also discourage open class actions.

¹ *Money Max Int Pty Limited (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148

² *P Dawson Nominees Pty Limited v Brookfield Multiplex Limited (No 4)* [2010] FCA 1029

³ *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed)(In Liq)* [2015] FCA 811

Contacts

Diana Chang
Partner
T: +612 8922 8003
E: diana.chang@cliffordchance.com

Kate Godhard
Counsel
T: +612 8922 8021
E: kate.godhard@cliffordchance.com

Tim Grave
Partner
T: +612 8922 8028
E: tim.grave@cliffordchance.com

Daniel Moloney
Senior Associate
T: +612 8922 8006
E: daniel.moloney@cliffordchance.com

Angela Pearsall
Partner
T: +612 8922 8007
E: angela.pearsall@cliffordchance.com

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www.cliffordchance.com

Clifford Chance, Level 16, No. 1 O'Connell Street,
Sydney, NSW 2000, Australia

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