CHUBB®

CLYDE&CO

Securities Class Actions

in Australia

Executive Summary

The landscape for securities class actions against corporates across Asia-Pacific and the Directors and Officers (**D&O**) insurance solutions that are available to companies is maturing. Given Australia has one of the most developed class action regimes in the world, and has seen the bulk of the class actions in the Asia-Pacific region, the majority of this summary is focused on developments in Australia.

Australia

It has been 27 years since the class action regime was introduced in Australia. The Australian class action regime is among the most plaintiff-friendly in the world. Companies are more likely to face class action litigation in Australia than anywhere in the world, outside of the United States (**US**).

Since the first securities class action was filed in 1999, there has been a rapid growth in securities class action suits in Australia, with at least 78 shareholder class actions filed in the Federal Court since 2002. Shareholder class actions are now the most commonly filed class actions in the Federal Court, with 34% of all class actions filed in the last 5 years being shareholder claims. The frequency of class actions filed in Australia shows no signs of slowing, aided by an increasingly entrepreneurial plaintiff bar, a burgeoning market with government-support for litigation funding, heightened scrutiny of corporate governance and continuous disclosure and relatively low thresholds for bringing a claim under the class action procedure.

On 24 January 2019 the Australian Law Reform Commission (**ALRC**) released its final report in its "Inquiry into Class Action Proceedings and Third-Party Litigation Funders" (**Inquiry**). The Inquiry focused on the impact that an increasing number of class actions and litigation funders have had on the class action regime. The ALRC has recommended several reforms that were the subject of public consultation, including a review of the legal and economic impact of the central causes of action in shareholder claims.[1]

A securities class action will typically be brought by a group of shareholders against a company and/or its directors and officers claiming damages for financial loss suffered as a result of the company's alleged failure to disclose material facts to the financial market, or based on alleged misleading or deceptive conduct by its statements to the market. These claims usually involve large overall losses, even where the loss suffered by each individual shareholder may be relatively small.

A current concern for the Australian D&O market is the significant and increasing number of securities class actions being filed against insured entities, in some cases without any claims being brought against the insured directors or officers themselves. This creates a risk of the D&O cover being fully eroded by a single class action (or multiple actions) against the entity alone, leaving no, or limited cover available for the insured directors and officers for the same or other claims, which is an unforeseen consequence of extending Side C cover to D&O policies.

The Insurance Council of Australia has reported that the average securities class action can cost between AUD 50 million – AUD 70 million (including settlement value and legal costs). In recent years the Australian D&O insurance market premium pool is around AUD 280 million annually. In 2017 there were 16 securities class actions filed and in 2018 there were at least 18 actions filed. The adverse impact of securities class actions on this market in particular has been recognised by the ALRC during the course of its Inquiry.

Any settlement must be approved by the Court as being fair and reasonable, and in the interests of class members. The highest settlement to date is the Black Saturday Bushfires for AUD 494 million in 2014, with Centro being the largest shareholder settlement for AUD 200 million in 2012. The exposure for defendants is potentially huge, with total settlements for shareholder and investor claims well exceeding AUD 1 billion.

Defence Costs

The costs of defending a securities class action claim are typically in the region of many millions of dollars. Recent studies suggest the average duration for shareholder claims to settle and obtain court approval is 962 days, or 2.7 years,[2] from commencement of the proceedings, though some actions can take much longer.

Recent reported Court settlement approvals have disclosed the plaintiff's costs of AUD 12.6 million in the OzMinerals class action, AUD 19.2 million in the AECOM/ Rivercity class action, AUD 5.7 million in the Billabong Class action, AUD 10.3 million in the Newcrest Mining class action and AUD 10.5 million in the Allco Finance class action. The defence costs incurred by a defendant are often commensurate with, or more than, the plaintiff's costs of pursuing claims.

In particular, the costs incurred in the discovery process are often substantial, the majority of which will fall on the defendant who will usually have voluminous internal documents needing to be reviewed and produced. Expert evidence costs can also be significant in defending these claims. Expert evidence is important to demonstrate the economic consequences (if any) of the alleged non-disclosure or misrepresentation, and to attack the quantum claimed.

Litigation Funding

The provision of litigation funding, being the financing by a third party not otherwise involved in the litigation, has been critical to the growth and development of class actions in Australia. It was one of the first jurisdictions in the world where litigation funding gained wide acceptance. Litigation funders supported 71% of shareholder class actions filed before mid-2017 in Australia.

The opportunities presented by Australia's class action regime have attracted an increasingly diverse range of funders, including those backed by institutional investors, hedge funds and even high net worth individuals. There are now around 25 Australian and international litigation funders currently active in Australia, with offshore funders comprising just over a third of the funding market.

1 For more information see www.clydeco.com/insight/article/alrc-class-actions-article and www.clydeco.com/insight/article/alrc-final-report-class-action-proceedings-and-third-party-litigation-funde

2 Prof Vince Morabito, 'An Empirical Study of Australia's Class Action Regimes', Fifth Report, July 2017

There is growing concern that the presence of less sophisticated litigation funders, who may be prepared to take on risks that more established funders will not, is leading to more speculative claims being announced and that there is increased competition among funders to be first off the rank in commencing a new claim.

Plaintiff Law Firms

While firms such as Maurice Blackburn and Slater & Gordon initially captured most of the market with specialist class action teams, there has been a recent trend of smaller and newer law firms entering the class action space in Australia. Studies show that there have been at least 22 new players as class action plaintiff firms in the past three years.

As with the growing litigation funding market, the increasing number of plaintiff law firms (with less experience) bringing class actions heightens the prospect of more speculative claims and the issues created by "race to file" scenarios.

The Future

Our predictions for shareholder class actions over the next 5 years are:

- The current trend of more than 10 new shareholder class actions being filed each year will continue, if not increase, unless and until such time as there is further law reform in connection with the central causes of action in shareholder claims.
- Law reform will follow the issue of the ALRC's Final Report. If its recommendations are accepted by the Australian Parliament, this will have an impact on the class action claims environment including in relation to:
  - A potential overhaul of the continuous disclosure regime (following Parliamentary review) which has driven shareholder claims. Although not going so far as watering down continuous disclosure obligations, we could see the introduction of a higher fault standard in respect of continuous disclosure and the laws relating to misleading or deceptive conduct. Additionally we may see changes to the laws around private enforcement of rights through the Courts with certain actions being reserved only to the corporate regulator, ASIC;
  - Exclusive jurisdiction may be conferred on the Federal Court of Australia for causes of action arising under specific Commonwealth legislation that are central to shareholder claims;
  - Explicit Court powers may be introduced to regulate and intervene in private contractual arrangements between litigation funders and group members in class action proceedings, rather than establishing a licencing regime administered by ASIC or otherwise imposing minimum capital adequacy requirements on funders;
  - The Court's powers will likely be enhanced to manage and dispose of competing class actions, which will help ameliorate current issues with multiple actions and return to the original objective that class actions proceed on an open rather than closed basis. This, in tandem with a possible prohibition on closed classes, would result in a reduction in competing class action proceedings; and
  - Changes may be introduced to the way costs are charged by solicitors in funded litigation, with the availability of contingency fee arrangements being permitted in class actions subject to a number of limitations.
- As the six year limitation period has expired for claims emanating from losses in financial services sustained from the 2009 global financial crisis, shareholder actions will continue to be pursued in connection with large scale corporate collapses, in respect of earnings guidance/forecasts and subsequent profit downgrades and based on any adverse findings which may arise from the Financial Services Royal Commission (with the final report delivered to the Australian Treasurer on 1 February 2019 and released publicly on 4 February 2019).
- We expect to see more jurisprudence, even before any recommendations from the ALRC are adopted by the Parliament, as to how Australian Courts are willing to intervene and case manage competing class actions irrespective of whatever private contractual arrangements have been entered into with group members and particular law firms/litigation funders.
- There will be increased involvement of institutional investors and trustees of superannuation funds as plaintiffs in class actions.
- We may see the first Australian shareholder class action based on data breaches, for example where a company's share price drops due to an undisclosed data breach or due to a company's inadequate cyber security protections.
- A superior Court in Australia will rule on whether a class can rely on indirect or market based causation in establishing reliance in a shareholder class action. The outcome of such a decision may impact the willingness of parties to run class actions to judgment, rather than settling in the future.
- We will see increased use of data analytics in class actions including by funders and law firms to identify potential class action claims, to narrow the scope and volume of discovery and to assess economic loss suffered by members of the class.
- There will be an increase in claims relating to financial disclosures with respect to the effects of climate change. In 2017 shareholder claims were instituted against the Commonwealth Bank raising allegations of inadequate financial reporting on the impact of climate change, but these were subsequently dropped. Our oil/energy sector may see claims similar to recent actions brought against major fossil fuel companies in the US, claiming they did not adequately or appropriately disclose risks posed to their businesses by climate change.
- D&O insurers are likely to adjust ways in which Side C cover is offered to the Australian market in the future, in an attempt to avoid limits of cover being fully eroded by actions against entities alone, leaving no or limited remaining cover to D&Os.

Chubb

Chubb is the world's largest publicly traded property and casualty insurer. With operations in 54 countries, Chubb provides commercial and personal property and casualty insurance, personal accident and supplemental health insurance, reinsurance and life insurance to a diverse group of clients. As an underwriting company, we assess, assume and manage risk with insight and discipline. We service and pay our claims fairly and promptly. The company is also defined by its extensive product and service off erings, broad distribution capabilities, exceptional financial strength and local operations globally.

658	31,500	54	190
Offices	Employees	Countries	Territories with policies issued

Clyde & Co

50+	3,800	415	1,800
Offices	Total staff	Partners	Lawyers

www.clydeco.com