



# THE SHAREHOLDER IMF'S QUARTERLY NEWSLETTER

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## “OPTING IN” TO REPRESENTATIVE PROCEEDINGS

Australia’s class action laws were drafted at a time when litigation funding for shareholders was unknown.

In two class actions being funded by IMF – the proceedings against *Aristocrat Leisure* and *Concept Sports* – changes to the original definition of the class have been made in response to the Federal Court’s interpretation of Part IVA of the *Federal Court Act*.

Both the Federal Court (Part IVA of the *Federal Court of Australia Act 1976*) and the Victorian Supreme Court (Part 4A of the *Supreme Court Act 1986*) have introduced class action regimes containing an opt out regime. All persons who fall within the description of a group represented by a representative plaintiff will be bound by the outcome of the

litigation, unless they take the active step to opt out of the proceedings.

In both the *Aristocrat* and *Concept Sports* cases, which are running in the Federal Court, the description of the group were those shareholders who had retained law firm Maurice Blackburn Cashman, had purchased shares at a certain time and suffered loss, and were being funded by IMF.

Section 33C of the *Federal Court of Australia Act* specifically provides that a proceeding may be commenced by one or more persons representing “some or all of them”, suggesting that the legislature anticipated a class could legitimately be defined to include some, rather than all potential members.

However, in the *Aristocrat*

case, Justice Stone said: “I find that the requirement that group members opt in to the proceeding to be inconsistent with the terms and policy of Part IVA.” (*Dorajay Pty Ltd v Aristocrat Leisure Limited* [2005] FCA 1483 at par 125.)

The practical effect of the decision in *Aristocrat* is that shareholders who obtain litigation funding and wish to take action against a company for misleading conduct will not be able to limit the class so as to exclude shareholders who have not obtained litigation funding.

The corollary is that IMF will be unlikely to offer funding for a class action if shareholders (who have not entered into a Funding Agreement) are able to “freeload” on the legal

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**For more information about IMF, visit [www.imf.com.au](http://www.imf.com.au) where you can request information about IMF-funded actions against :**

**Westpoint**

**ION**

**Sons of Gwalia**

**Village Life**

## IMF GRANTED ACCESS TO DOCUMENTS - BUT NOT USE OF SHARE REGISTERS

The analysis of information provided under discovery and the ability to make contact with potential members of a class action are important elements in IMF’s provision of litigation funding.

Access to documents is important because it allows IMF to monitor its investments and determine whether it will continue to provide funding as a matter is being prepared

for trial.

Contacting shareholders allows IMF to make shareholders aware of the action and facilitates communication with and between shareholders in relation to potential representative proceedings.

These issues have been the subject of recent decisions by the Federal Court.

In June, the Federal Court held that IMF is entitled to examine documents provided under discovery. However, the Federal Court last year held that IMF was not entitled to use the share register of a company to contact shareholders and inform them of a potential class action.

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## MORE INSTITUTIONAL INVESTORS FOCUSSING ON CLASS ACTIONS

Increasing numbers of institutional investors are recognising their fiduciary responsibilities to assess joining class actions, according to a 28 July 2006 front page story in *The Australian Financial Review*.

The topic of class actions has been on the agenda at a number of recent industry conferences, including the Australian Council of Super Investors conference in Melbourne in June, with delegates treated to a session on the Australian and US class action scenes.

IMF counts a number of Australia's largest institutional investors as clients and is continuing to work with the major superannuation trustees to ensure they are aware of the opportunity of litigation

funding to pursue losses sustained as a result of companies' breaches of the Corporations Act.

The AFR article quoted the president of the Australian Council of Super Investors, Michael O'Sullivan, on super funds' fiduciary duty to join class actions unless there is an overwhelming duty not to do so.

"Any kind of misleading or deceptive conduct or recklessness or negligence or malfeasance...trustees of super funds have a special responsibility to make sure they look at that very closely," Mr O'Sullivan told the AFR.

Mr O'Sullivan believes it is unlikely that Australia will see a proliferation of class actions akin to the US, but "I do think

we'll get to a stage where there will be more than there are now."

*Representatives from Institutional investors attend IMF seminar in Sydney*

Meanwhile, around 70 fund managers, superannuation trustees, insolvency practitioners and lawyers attended IMF's Sydney presentation on shareholder actions, held at the Jamison Rydges Hotel on 11 July 2006.

*A copy of the paper delivered at the seminar, titled "Shareholder Actions", can be downloaded from the Presentations section of the IMF website at [www.imf.com.au](http://www.imf.com.au)*

## SHAREHOLDERS PREVENT RIO TINTO FROM LIMITING CLASS ACTIONS

Companies should think twice before attempting to curb the rights of their shareholders to bring class actions against the company.

That is the clear message to corporate Australia following Rio Tinto's embarrassing defeat ahead of its annual meeting in May, when a number of the mining giant's shareholders forced it to withdraw a proposal to limit class action lawsuits to those from Victoria and the UK.

Following the recommendation of international shareholder activist group ISS, a number of institutional investors voiced their concerns about the proposal, forcing Rio Tinto to withdraw it from the annual meeting.

With the jurisdictions of Victoria and the UK seen as "corporate friendly", the proposal was an attempt by Rio Tinto to ensure it could shop jurisdictions if it ever faced shareholder litigation.

IMF welcomes the action, which illustrates that institutional investors are not willing to have their rights limited by corporate action. Rather, increasing numbers of large shareholders will seek to protect their rights. The action also illustrates that more institutional investors are recognising the importance of class actions to protect their statutory rights.

Impressively, Australian institutions have shown themselves to be more active than their UK counterparts.

Rio Tinto's proposal to limit class actions received the support of the UK's National Association of Pension Funds, which rejected ISS's advice. This meant that the motion was approved at Rio Tinto's UK meeting.

## STATES CONSIDER REGULATION OF LITIGATION FUNDING

The State Attorneys-General are considering whether to regulate the funding of litigation and the Standing Committee of Attorneys General (SCAG) released a discussion paper in May on the issue, titled "Litigation funding in Australia".

The paper notes that litigation funders bring a number of benefits to consumers of legal services by:

- ensuring access to justice for some meritorious claims which otherwise would be abandoned (particularly in class actions);
- creating a level playing-field by providing strategic and investigative expertise and funding to take on wealthy and insured defendants;

- providing cohesive direction in class actions;
- introducing budgeting for legal costs, for example, by ensuring solicitors adhere to budgets, thereby creating more competition for legal services; and
- providing confidence to defendants that their costs will be recovered.

The paper also raises a number of issues for discussion, including whether litigation funders should be subject to disclosure requirements and prudential regulation, and whether criteria for legally acceptable funding agreements should be formalized. IMF is not opposed to the regulation of litigation funding

and is the only funder which has obtained an Australian Financial Services Licence. But IMF believes that it should not be treated differently to insurance companies, who also fund and "maintain" litigation every day (typically on the defendant side).

Submissions or comments on the discussion paper are due to be submitted with the Standing Committee of Attorney's General by 14 September.

The discussion paper can be found on the AG website at [www.lawlink.nsw.gov.au](http://www.lawlink.nsw.gov.au)

*The next edition of The Shareholder will detail IMF's response to the discussion paper.*

## “OPTING IN” TO REPRESENTATIVE PROCEEDINGS - CONTINUED FROM PAGE 1

work being paid for by IMF.

Opt in proceedings have other benefits, many of which have been recognised by the Courts over the years when making orders “closing the class”, which effectively creates an opt in process. For defendants, when the class action is defined to a limited number of shareholders, it is easier to estimate the quantum of the claim and therefore the potential liability can be defined.

In response to Justice Stone’s decision, IMF has approached the NSW Supreme Court, suggesting that an amended version of Part IVA of the *Federal Court of Australia Act* be adopted in NSW to provide for both opt out and opt in proceedings.

The NSW Supreme Court does not currently contain a class action procedure akin to Part IVA, although class actions can be brought under the NSW Supreme Court Rules,

which do not contain extensive provisions relating to the procedural issues which are likely to arise in class actions.

Part IVA was introduced by the Federal Court of Australia fifteen years ago and facilitation of access to justice was its primary objective. Since its introduction, there have only been 156 completed Part IVA proceedings.

An amended version of Part IVA that permits a class to be

limited to those persons who agree to accept funding will recognise the commercial reality that without funding, the case might not get off the ground at all.

This outcome has been sought by IMF in an application to the Federal Court.

## ACCESS TO DOCUMENTS AND THE USE OF SHARE REGISTERS - CONTINUED FROM PAGE 1

### **Access to discovered documents granted**

In June, the Federal Court allowed IMF access to discovered documents in the context of the litigation against Concept Sports. The plaintiff in that action was not certain that discovered documents could be provided to IMF, so approached the Court for permission. Justice Finkelstein held the plaintiffs did not require permission before they give discovered documents to IMF.

Justice Finkelstein noted that IMF must keep funded cases constantly under review and it would not be possible for IMF to properly review cases unless it has access to discovered documents. “The question is whether the use of documents for that purpose is for a purpose that is foreign to the action,” His Honour said.

“IMF is not a stranger to the action; it has a sufficient interest to be provided with discovered documents, at least those documents it needs to assess the merits of the action.”

### **Use of the share register to contact shareholder denied**

Conversely, the Federal Court has prevented the shareholder register being used to inform shareholders about a potential action.

In an action against *Sons of Gwalia*, IMF sought to use the share register to contact shareholders to inform them of a potential claim against the failed miner. However, the Federal Court (at first instance, and by majority on appeal to the Full Court) last year found against the use of the register to contact members in relation to an action against the company for breaches of the continuous disclosure laws or for misleading statements made by the company.

Section 177 of the *Corporations Act 2001* (Cth) prohibits using information contained in a share register to contact or send material to a person, to protect shareholders’ privacy.

IMF sought to rely on an exception to the prohibition,

contained in section 177(1A), which says that information in a register can be used to contact persons if: (a) the use or disclosure of the information is “relevant to the holding” of the shares; or (b) such use is authorised by the company.

In the majority decision in the Full Court, Justice Emmett held: “It does not follow that a communication about the circumstances in which a person agreed to acquire shares in, or to become a member of, a company can be characterised as being connected with the fact that that person holds the shares.”

In contrast, the dissenting judge in the Full Court, Justice North, said: “Shareholders would likely have a real interest in receiving [the letter regarding the action], and would not regard the use of information from the register for this purpose as an undue intrusion into their privacy.”

IMF sought leave to appeal the decision of the Full Court to the High Court; leave was denied.

IMF has now approached the Commonwealth Department of The Treasury with a submission that the legislation be amended and clarified. The submission suggests that advising shareholders of the possibility of joining in a legal action to help them recover losses arising out of their acquisition, holding or disposal of shares is likely to be of sufficient interest to those shareholders to justify use of the register for that purpose.

Treasury is expected to provide advice to the Government on the issue and suggest options for reform.

Meanwhile, IMF has also provided a submission to the New South Wales Attorney General in relation to its Review of the Policy on Access to Court Information.

*Both submissions can be found in the “Legal consumer issues” section of the IMF website: [www.imf.com.au](http://www.imf.com.au).*

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## ACTION AROUND TOWN INSURANCE LAWYERS DISCUSS FUNDING

### ***Insurance layers talking litigation funding***

Barrister Mark McCulloch SC, of Wentworth Chambers, delivered a paper titled "Funding the fight: A look at recent developments in the law in relation to litigation funding" to the Insurance Law Association's Twilight Seminar Series in July.

The paper concluded that the thrust of recent cases in NSW was that litigation funding is permissible as long as safeguards are in place to ensure the Court's process is not abused. The paper noted the importance of the upcoming High Court decision in *Fostif*.

### ***IMF takes the floor at the Consumer Representatives Conference***

Clive Bowman of IMF delivered a paper at the recent Consumer Representatives Conference, held in Melbourne in June.

The paper examined the Westpoint debacle and the advantage of funded court proceedings as an alternative to the Financial Industry Complaints Service.

The next edition of *The Shareholder* will discuss the limitations of FICS dealing with class actions.

### ***IMF on the bill at D&O Insurance Symposium***

John Walker, IMF's managing director, will be appearing on a panel with Jan Redfern of ASIC at The Australian Directors & Officers Liability and Insurance Symposium, to be held on 28 and 29 August in Sydney. Ms Redfern will be addressing the regulators' views concerning D&O policies.

The conference also contains a session, titled "The rise of Securities Actions - are Directors and Officers More Exposed?", with panel members including Bernard Murphy of Maurice Blackburn Cashman, Ian Ramsay of the University of Melbourne, and John Walker.

### **OVERSEAS NEWS**

#### ***US class action filings fall***

The number of US class action filings in the first half of 2006 is at the lowest level for any six month period since 1996, and on an annualised basis is 36 percent below the 1996-2005 historical average of 194, according to a recent report by Stanford Law School and Cornerstone Research. The annualised number of

"traditional" securities fraud class actions filed from January through June 2006 decreased 31 percent compared to 2005 levels, falling from 179 filings to an annualised estimate of only 123, based on 61 filings through June 30, 2006.

"While we lack the data necessary to determine the precise cause of the slowdown, the most intriguing hypothesis is that extensive and expensive corporate efforts to improve governance and accounting have reduced plaintiffs' ability to allege fraud," said Stanford Law School Professor Joseph Grundfest.

#### ***French shareholders sue EADS***

A group of French shareholders have launched a class action against the majority owner of Airbus, EADS, following a 26% collapse in the company's share price on 13 June when it announced the latest delays to the A380 "superjumbo". The action has been filed in the Netherlands, and follows an investigation launched by AMF, the French financial regulator, which is investigating share trading in EADS just before the June announcement.