Lawyer-driven class actions: When will the lawyer be compromised?

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Introduction

1. In recent years, class actions, which are often 'lawyer-driven' actions, have become "a prominent feature of the Australian litigation landscape."[1] While class actions have many advantages and benefits such as the provision of a cost effective means by which many individual claims against a defendant may be dealt with together and a multiplicity of actions avoided, there are also risks associated with them.[2]

2. Some of these risks were evident in the case of *Melbourne City Investments Pty Ltd v Treasury Wine Estates Limited (No 3)*[3] where Justice Ferguson of the Victorian Supreme Court found that a solicitor who was not independent of the lead plaintiff was compromised in his role as solicitor and should be restrained from acting for the plaintiff whilst it was the lead plaintiff and that the proceedings should not be permitted to continue as a class action whilst the plaintiff and the solicitor acted in tandem as plaintiff and solicitor.

Background

3. The plaintiff was Melbourne City Investments Pty Ltd ("**MCI**"), a Victorian investment company, whose sole director and sole shareholder was Mark Elliott, a Melbourne based solicitor.

4. On the day of its incorporation, MCI purchased small parcels of shares in 20 publicly listed companies including Treasury Wine Estates Limited ("**Treasury**"), Leighton Holdings Limited ("**Leighton**") and WorleyParsons Limited ("**WorleyParsons**"). Each parcel of shares cost a little under $700.

5. Subsequently, MCI commenced separate proceedings against Treasury, Leighton and WorleyParsons. Each proceeding was commenced under Pt 4A of the *Supreme Court Act 1986* (Vic) which contains a regime for the commencement and conduct of 'group proceedings'.[4] In general, group proceedings may be brought where 7 or more persons have

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[1] Grave D, Adams K & Betts J, *Class Actions in Australia*, 2nd ed (2012), Thomson Reuters, at [1.190]
[2] See, for example, *Giles v Commonwealth of Australia* [2014] NSWSC 83 at [81]-[83] for a list of the advantages and benefits and disadvantages of class actions
[3] [2014] VSC 340
[4] Substantially similar provisions exist in NSW where the proceedings are known as 'representative proceedings'. See Pt 10 of the *Civil Procedure Act 2005* (NSW)

claims against the same person, being claims which arise out of the same, similar or related circumstances and which give rise to a substantial common issue of law or fact.

6. In each of the group proceedings brought by MCI, Mr Elliott was the solicitor for MCI.

7. In the proceedings brought against Treasury and Leighton, the proceedings with which Justice Ferguson was concerned, MCI alleged breaches of the continuous disclosure obligations in s 674(2) of the *Corporations Act 2001* (Cth) and misleading or deceptive conduct in breach of s 1041H of the *Corporations Act*. The loss claimed was the difference between the prices at which MCI purchased the shares and the prices that would have prevailed had each company made what was alleged to be proper disclosure. This meant that the most that MCI could obtain by way of compensation if it were successful would be less than $700 in each of the proceedings.

8. Subsequently, MCI purchased similar small parcels of shares in another 145 publicly listed companies, together with further small parcels of shares in Treasury, Leighton and WorleyParsons.

9. Treasury and Leighton claimed:

    - that the proceedings brought against them were an abuse of process and should be stayed;
    - in the alternative, that orders should be made in the exercise of the inherent jurisdiction of the Court, restraining Mr Elliott from acting for MCI in the proceedings whilst MCI was the lead plaintiff;
    - in the alternative, that orders should be made under the group proceedings provisions in Pt 4A of the *Supreme Court Act* that the proceedings not continue as group proceedings whilst MCI was the lead plaintiff and Mr Elliott remained as its solicitor.

Were the proceedings an abuse of process?

10. Justice Ferguson found that it was probable that the reason for MCI's existence was to commence group proceedings so as to enable Mr Elliott to earn legal fees from acting as its solicitor. Her Honour further found that MCI commenced the proceedings against Treasury and Leighton for the predominant purpose of having Mr Elliott act as its solicitor so that he could earn legal fees given that the amount of any damages claim would be small.[5] Her Honour, however, was not satisfied that the proceedings were an abuse of process.

[5] Above, n 3, at [9], [11] and [29]

11. In reaching this conclusion, her Honour drew, in particular, on the principles governing abuse of process stated by the High Court in *Williams v Spautz*. [6] In summary, those principles were:

    - Court proceedings may not be used or threatened for the purpose of obtaining for the litigant some collateral advantage and not for the purpose for which such proceedings are properly designed and exist.
    - The criterion for abuse of process is whether the litigant's predominant purpose in bringing the proceedings is improper i.e. is to gain a collateral advantage.
    - The concept of abuse of process must be kept within reasonable bounds.
    - The power to stay a proceeding on such a ground will only be exercised in the most exceptional circumstances.
    - It is doubtful that a litigant with a genuine cause of action, which he or she would wish to pursue in any event, who can be shown to also have an ulterior purpose in view as a desired by-product of the litigation, can be debarred from proceeding.

12. To illustrate how it was important to keep the concept of abuse of process within reasonable bounds, the majority in *Williams v Spautz* had used the example of an alderman who prosecuted another alderman who was a political opponent for failure to disclose a relevant pecuniary interest when voting to approve a contract, intending to secure the opponent's conviction so that the opponent would then be disqualified from office as an alderman by reason of that conviction, pursuant to local government legislation regulating the holding of such offices. The immediate purpose of the prosecutor to secure conviction was within the scope of the criminal process instituted by the prosecutor but the ultimate purpose of bringing about disqualification was not. However, the majority said that the existence of the ultimate purpose could not constitute an abuse of process when that purpose was to bring about a result for which the law provided in the event that the proceedings ended in the prosecutor's favour. It would have been otherwise if the purpose of bringing the proceedings was not to prosecute them to a conclusion but to use them as a means of securing some advantage for which they were not designed or some collateral advantage beyond what the law offered.[7]

13. Justice Ferguson adapted the alderman example to the facts of the case before her Honour to demonstrate why there was no abuse of process. Her Honour said that MCI's ultimate purpose was for Mr Elliott to earn legal fees while MCI's immediate purpose was to obtain orders for compensation in the proceedings, which would naturally lead to an award of costs. Her Honour said that the ultimate purpose did not render the proceedings an abuse of process, the more so on the facts of the case before her Honour because, whereas the ultimate purpose of the alderman to obtain disqualification of the political opponent was

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[6] [1992] HCA 34; (1992) 174 CLR 509 per Mason CJ, Dawson, Toohey and McHugh JJ at 522, 526-530; Brennan J at 539

[7] Above, n 6, at 526-527

not something that could be achieved in the criminal process itself instituted by the prosecutor but was a consequence of it, an order for costs (were MCI to be successful in obtaining its principal relief) would form part of the relief sought in the proceedings or was a likely and natural consequence if MCI succeeded in its claim and was awarded damages. [8]

14. Justice Ferguson further said, relying on the reasoning of the majority of the High Court in *Campbells Cash and Carry Pty Ltd v Fostif Pty Ltd,*[9] that if there was a problem that needed to be addressed because of the relationship between Mr Elliott and MCI, then that was a problem that should be dealt with through the procedures that were employed in group proceedings, or through the Court's inherent powers to control the conduct of its officers.[10]

15. Finally, on the issue of whether the proceedings were an abuse of process, her Honour commented that Treasury and Leighton had not claimed that MCI was a sham plaintiff on the basis that it purchased the shares in publicly listed companies for the purpose of contriving a loss. Had that argument been put, her Honour said, it would have raised "some troubling issues."[11]

Should Mr Elliott be restrained from acting for MCI?

16. Her Honour then considered whether, in the exercise of the Court's inherent jurisdiction, Mr Elliott should be restrained from acting for MCI whilst it was the lead plaintiff.

17. Her Honour noted that the principles applicable to the Court's inherent jurisdiction to restrain a lawyer from acting in a particular case, as an incident of its inherent jurisdiction over its officers and to control its processes in aid of the administration of justice, had been summarised by Justice Brereton in *Kallinicos v Hunt* [12] as follows:

    - The test to be applied in the inherent jurisdiction was whether a fair-minded, reasonably informed member of the public would conclude that the proper administration of justice required that a lawyer should be prevented from acting, in the interests of the protection of the integrity of the judicial process and the due administration of justice, including the appearance of justice.

    - The jurisdiction was exceptional and was to be exercised with caution.

    - Due weight should be given to the public interest in a litigant not being deprived of the lawyer of his or her choice without due cause.

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[8] Above, n 3, at [33]
[9] [2006] HCA 41; (2006) 229 ALR 58; (2006) 80 ALJR 1441 per Gummow, Hayne and Crennan JJ at [95]
[10] Above, n 3, at [35]
[11] Above, n. 3, at [37]
[12] [2005] NSWSC 1181; (2005) 64 NSWLR 561 at [76]

- The timing of the application might be relevant because the cost, inconvenience and impracticality of requiring a lawyer to cease to act could provide a reason for refusing to grant relief.

18. Applying these principles to the facts of the case, her Honour considered that the 'hypothetical fairminded independent observer' would be reasonably informed:

    - of the shareholdings that MCI had in the various publicly listed companies;
    - that Mr Elliott had at all times been MCI's sole director and shareholder;
    - that MCI had commenced the three group proceedings;
    - that Mr Elliott was the solicitor on the record for MCI in each of those group proceedings;
    - that MCI did not stand to gain much in terms of compensation if the proceedings were successful but, in that case, the costs awarded in its favour and payable to Mr Elliott would be substantial;
    - that if MCI was unsuccessful in any of the proceedings, it would likely be exposed to a substantial adverse costs order; and
    - that liability would likely reduce the value of Mr Elliott's shareholding in MCI.[13]

19. Her Honour then said that, with knowledge of those matters, the hypothetical fair-minded independent observer would reach the following conclusions:

    - that Mr Elliott was the decision-maker in the conduct of the proceedings, both from the point of view of what was in MCI's commercial interests as plaintiff and also as its solicitor;
    - that Mr Elliott, through MCI, was in the business of purchasing small shareholdings in listed companies with the purpose of subsequently commencing group proceedings against some of them for alleged breaches of their continuous disclosure obligations;
    - that MCI's (and Mr Elliott's) business model was likely to depend upon the outcome of the three group proceedings;
    - that Mr Elliott was compromised in his role as a solicitor such that there would be a real risk that he could not give detached, independent and impartial advice taking into account both the interests of MCI (and its potential exposure to an adverse costs order) and the interests of group members who did not have control over the proceedings yet were bound by the judgment in the proceedings unless they opted out;
    - that it was important that the solicitor who was acting for the plaintiff be independent, so that forthright and strident advice could be given, untainted by the personal interest of the solicitor beyond his or her normal interest;
    - that Mr Elliott's interest went beyond that of other solicitors acting for plaintiffs in group proceedings because he not only had an interest in recovering his fees, but

[13] Above, n 3, at [48]

also an interest in ensuring that MCI did not suffer the consequences of adverse costs orders; and

- that if justice was to be seen to be done, MCI should be represented by a person without the vested interests that Mr Elliott had in the proceedings.[14]

20. Her Honour accordingly concluded that the proper administration of justice required that Mr Elliott be prevented from acting for MCI whilst the proceedings remained as group proceedings with MCI as the lead plaintiff.[15]

Should orders be made under the group proceedings provisions in Pt 4A?

21. Treasury and Leighton sought orders that the proceedings not continue as group proceedings whilst MCI was the lead plaintiff and Mr Elliott remained as its solicitor under the following group proceedings provisions in Pt 4A of the *Supreme Court Act*:

    - section 33N(1)(d), which permits the Court, on application by the defendant, to make a 'declassing order' if it is satisfied that it is in the interests of justice to do so because "it is otherwise inappropriate that the claims be pursued by means of a group proceeding";[16] and
    - section 33ZF, which enables the Court, in any proceeding conducted under Pt 4A, of its own motion or on application by a party, to "make any order the Court thinks appropriate or necessary to ensure that justice is done in the proceeding."[17]

22. Justice Ferguson declined to make orders under s 33N(1)(d) on the basis that the issues raised in the proceedings appeared to be amenable to group proceedings, with common questions able to be determined, and that MCI could continue on as the plaintiff (with other solicitors acting for it) and the issues raised in the proceedings determined in the usual way.[18]

23. However, her Honour considered that it would be in the interests of justice, in addition to orders restraining Mr Elliott from acting for MCI in the group proceedings, to make an order under s 33ZF to the effect that the proceedings ought not be allowed to continue as group proceedings under Pt 4A for so long as Mr Elliott was acting for MCI or, if Mr Elliott continued to represent MCI, for so long as MCI remained the lead plaintiff.[19]

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[14] Above, n 3, at [49]-[50]
[15] Above, n 3, at [51]
[16] Cf s 166(1)(e) of the *Civil Procedure Act 2005* (NSW)
[17] Cf s 183 of the *Civil Procedure Act 2005* (NSW)
[18] Above, n 3, at [61]
[19] Above, n 3, at [62]

24. In deciding that these orders should be made, her Honour had regard to comments made by Justice Finkelstein in *Kirby v Centro Properties Ltd*[20] about 'lawyer-driven litigation' being litigation in which the lawyer:

    - investigated the potential for a claim;
    - recruited the plaintiff who was sometimes a mere figurehead with little at stake and who was usually not well informed about the theories of their case; and
    - often recruited the group on whose behalf a class action was commenced.

25. Justice Finkelstein had said that solicitation of business by lawyers was not of itself improper and that, in fact, it could be a good thing that lawyers find clients who would not otherwise have sought redress for the wrongs that they had suffered or even realised that redress was available for such wrongs. However, his Honour had expressed concern about the risk that the entrepreneurial lawyer would not be adequately monitored by the client plaintiff and would largely operate according to his or her own self-interest, "subject only to the restrictions imposed by the ethical rules that govern the profession, some judicial oversight and their own sense of ethics and fiduciary responsibilities."[21]

26. With Justice Finkelstein's comments in mind, Justice Ferguson said:

> *"Whether it is good or bad, the reality is that group proceedings are lawyer driven... They will not, for that reason, be brought to a halt. Nevertheless, it does seem to me that the risks associated with entrepreneurial lawyers acting in group proceedings, as identified by Finkelstein J, are exacerbated here where the plaintiff and the solicitor are not independent of one another. I have a concern that, whilst MCI is the plaintiff and Mr Elliott its solicitor, despite their best intentions, there is a risk (which cannot be dismissed as remote) that selfinterest will dominate over the interests of group members. Ordinarily, lead plaintiffs have the benefit of independent advice about what they should or should not do taking into account the interests of group members. Ordinarily, the solicitor is not facing any possibility of adverse costs orders that will affect them if the plaintiff fails in expensive interlocutory disputes or does not succeed at trial. Mr Elliott is simply not in a position to give detached advice to MCI."* [22]

27. Her Honour added that, given that the group members would be bound by the decision of the Court unless they opted out, it was important that both the group members and the Court could have confidence that MCI was representing their interests as well as its own, having had the benefit of legal advice from a solicitor who did not have a vested interest in the outcome of the proceedings in the way that Mr Elliott did.[23]

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[20] [2008] FCA 1505; (2008) 253 ALR 65 at [4]
[21] Above, n 20, at [5]-[6]
[22] Above, n 3, at [63]
[23] Above, n 3, at [64]

28. Her Honour concluded by saying that the overarching purpose of the *Civil Procedure Act 2010* (Vic) to facilitate the "just, efficient, timely and cost effective resolution of the real issues in dispute"[24] would not be served if Mr Elliott and MCI continued as solicitor and lead plaintiff together. [25]

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[24] See s 7(1). Cf s 56 of the *Civil Procedure Act 2005* (NSW)
[25] Above, n 3, at [67]