CLASS ACTION RISK

There has been an increase in class action litigation in Australia in recent years, particularly class actions brought on behalf of shareholders against listed Australian entities. Since 2000 there have been over 20 shareholder class actions which have resulted in settlements ranging from $20 to $200 million.

Several factors have contributed to this trend:

- ASX listed companies are required to continuously report information to the market, which could reasonably be expected to have a material effect on the price or value of a company’s shares.

- There is a strict liability regime for misleading and deceptive conduct in Australia, meaning that there is no requirement that a director or company had an intention to mislead or deceive shareholders. This means a director can be held personally liable if market disclosures are found to be misleading and deceptive.

- The Australian Securities and Investors Commission’s (ASIC) support of shareholder class actions.

- The increased availability of funding by litigation funders, in a largely unregulated industry.

- A market based approach to causation. This hinges on the theory that the disclosure of information (and its accuracy), will be reflected in a listed company’s share price.
Litigation funders generally prefer to commence class actions against companies, however directors can still be joined to the proceedings. There is a greater risk that a director will be named as a party if the company is no longer trading, or is insolvent. Even if a director is not joined, they will inevitably be heavily involved in the litigation and may be required to give evidence. Directors may also need to appoint and personally pay for independent lawyers.

**WHAT THIS MEANS FOR DIRECTORS**

In this environment, directors should have strategies in place to avoid class actions. In the event one is commenced, it is vital that directors adopt a strategic approach in response, including seeking specialist legal advice.

**Avoiding a class action**

Most shareholder class actions commenced in Australia to date arise from public disclosures, their content and the way the disclosure was made. As such, directors need to carefully consider the implications of how a Board makes announcements, especially because claims usually implicate the highest levels of a company’s management and the Board.

- Companies should have a comprehensive process in place for deciding when and how information is disclosed.
- It is often better to disclose information to the market early and often - avoid 'bombshell' disclosures.
- Disclosures should, to the maximum extent possible, be contextualised and connected to previous announcements.
- If making forward-looking statements, ensure they are being made on reasonable grounds.
- Demonstrate transparency about the effects of events.

If a disclosure is likely to have a significant effect on the market, extraordinary care should be taken. Boards should seek advice from a class action specialist before making such a disclosure, who can assist with drafting the disclosure to limit the potential for scrutiny (and future litigation).

If ASIC commences an investigation prior to the commencement of a class action, the relationship between ASIC and the company should also be carefully managed, as the information disclosed to ASIC can have flow on effects to subsequent class action proceedings.
When a class action is commenced

Shareholder class actions are procedurally different from normal litigation: they are on a much larger scale and will usually attract media attention. It is important to engage a specialist with working knowledge and experience of the federal framework of class actions.

It is not uncommon for a shareholder class action to precede or follow an investigation by ASIC and the pressure of a class action coupled with an ASIC investigation and/or prosecution can often induce an entity into administration or liquidation. The risks for directors flow from here and directors should:

- engage specialist legal advice on the class action and any potential ASIC prosecutions,
- understand the allegations made, how the director is potentially involved and what evidence the director will need to adduce in the proceedings,
- establish a relationship with ASIC to determine what information it is seeking, and try to limit the scope, and
- ensure the company's insurance policy is comprehensive enough to cover a director embroiled in a dispute.

This article was written by Jason Betts, Partner, Sydney, Ante Golem, Partner, Emily Clarke, Senior Associate, and Emma Tormey Solicitor, Perth.

MORE INFORMATION

For information regarding possible implications for your business, contact Jason Betts or Ante Golem.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.
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