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Mr James Wood AO QC
Chairman
NSW Law Reform Commission
DX 1227 Sydney

Dear Chairman

Re: Inquiry into Security for Costs and Associated Costs Orders

We are pleased to provide the following preliminary submission in response to the NSW Law Reform Commission's Inquiry into Security for Costs and Associated Costs Orders ("the **Inquiry**").

The Inquiry seeks to gauge the opinion of practitioners as to whether the existing law and practice surrounding security for costs strikes an appropriate policy balance and provides adequate protection for all parties to litigation.

> The Court seeks to achieve a balance between ensuring that adequate and fair protection is provided to the defendant, and avoiding injustice to an impecunious plaintiff by unnecessarily shutting him out or prejudicing him in the proceedings.[1]

Under the present system, the court has a broad discretion when considering whether to order a corporate plaintiff to provide security for the legal costs incurred or to be incurred by a defendant to the proceedings. However, the court's jurisdiction to order a natural person to provide security for costs is limited to exceptional circumstances, reflecting the fundamental rule that "*poverty is no bar to a litigant.*"[2] Recently, the increasing prominence of commercial litigation funders, particularly in relation to representative proceedings, has raised questions concerning the adequacy of existing principles.

SUMMARY

In our submission, the existing law and practice in New South Wales provides a suitable balance between the interests of plaintiffs and defendants. The current system:

1. Promotes access to justice by limiting the circumstances in which an order can be made against an individual to those where the individual has sought to evade the consequences of the proceeding, is outside the jurisdiction, or is otherwise acting for the benefit of another person;

2. Provides for orders to be made against corporate plaintiffs where they are unable to establish that they have sufficient assets to meet the amount of a likely order; and

3. Provides judge's with a broad discretion concerning the appropriateness or amount of security for costs to be awarded, and recognizes that there are mitigating factors that

[1] *Idoport Pty Ltd v National Australia Bank Ltd* [2001] NSWSC 744 at [47]
[2] *Cowell v Taylor* (1885) 31 Ch D 34 at 38

would render a security for costs order to be inappropriate, even when against an impecunious corporate plaintiff.

Security for costs orders vs. associated orders

More generally, we believe that it is important to distinguish the role played by security for costs orders, from the policy objectives of the other costs orders that are the subject of the Inquiry, including public interest orders. The purpose of security for costs orders is to ensure that defendants do not unfairly bear a risk of non-recovery of legal costs that have been incurred in the successful defence of proceedings brought against them. The challenge faced by lawmakers is to ensure that the protection offered to defendants is balanced against the need to provide access to justice.

We would urge law reformers to resist any temptation to alter the policy balance, for instance by extending the availability of security for costs orders against natural persons even whilst also increasing a plaintiff's ability to access public interest or protective orders. Such a change would establish a higher hurdle to ordinary litigants and, accordingly, reduce access to justice. The legal system must enable individuals to pursue personal causes of action, without requiring them to establish some broader social benefit.

In our submission, an overarching policy imperative must be to ensure that plaintiffs are not prevented from pursuing legitimate causes of action merely because of their relative financial weakness. In our view, this objective is of social importance in its own right, and irrespective of whether a particular claim meets additional independent criteria, for example by raising issues that are considered to be of public interest.

SECURITY FOR COSTS

The Judicial College of New South Wales has outlined the circumstances in which each of the various courts in New South Wales will have jurisdiction to make security for costs orders against corporations (**corporate plaintiffs**) and individuals (**individual plaintiffs**), and summarized the various discretionary factors that are taken into consideration by courts in deciding whether security should be ordered and, if so, in what amount.[3] We refer generally to those principles, and do not propose to replicate them in this submission.

However, the following provide particular support for our submission that the existing law and practice results in an appropriate policy balance:

1. The threshold question for consideration by a court is whether there is credible testimony to establish that the plaintiff (corporate or individual) will be unable to meet the costs of a successful defendant.[4] However, balancing this is:

> The basic rule that a natural person who sues will not be ordered to give security for costs, however poor, is ancient and well established.[5]

In our submission, it is of paramount importance that individual plaintiffs are provided with this additional protection. They:

a. do not have the benefit of the corporate veil;
b. in commencing litigation, they necessarily expose their personal assets to an order for adverse costs. Rule 42.1 of the UCPR specifically contemplates security being ordered against individuals that take steps to avoid the potential negative consequences of litigation by avoiding service;

Ensuring that individual plaintiffs have access to the legal system is of primary importance. Given the ease with which "two-dollar" companies could otherwise be used

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[3] http://www.judcom.nsw.gov.au/publications/benchbks/civil/security_for_costs.html
[4] *Idoport Pty Ltd v National Australia Bank Ltd* [2001] NSWSC 744 at [47]; *Corporations Act* 2001 (Cth), s 1335.
[5] *Pearson v Naydler* [1977] 1 WLR 899 at 902

as nominal plaintiffs, it is appropriate that corporate plaintiffs be required to pay security for costs if they cannot provide evidence that they have sufficient assets within the jurisdiction to meet the potential costs of the defendant.

We believe that a court's observance of the "basic rule" provides sufficient protection to self-represented litigants and those funded by legal aid.

2. Where a plaintiff is unable to meet the costs of the defendant and security might otherwise be ordered, it is a mitigating factor if the contravening conduct alleged against the defendant itself caused or contributed to the plaintiff's impecuniosity.[6] In *Australian Quarry Holdings Pty Ltd (in liq) v Dougherty*, Ormiston J (as he then was) said:

> It might be said that this factor raises similar difficulties to that relating to the prospects of success but in my opinion the factor is ordinarily taken into account upon the assumption that it would be unfair to deny the plaintiff the right to sue where its impecuniosity may be said to result from the matters complained of, without great regard to the plaintiff's chances of success. In other words it is usually related to a similar factor, that an order for security may stultify the litigation or be otherwise oppressive. In the present case it is reasonably clear that the company was placed in liquidation after the events of which complaint is made in the proceeding.[7]

This rule avoids what would otherwise be a fundamental injustice; namely, a defendant being able to take the benefit of their own alleged wrongdoing in order to stultify legal proceedings.

Because of this discretionary principle, we believe that in the majority of circumstances, impecunious plaintiffs are adequately protected by existing law and practice.

3. The court will consider the bona fides of the plaintiff in bringing the claim, including their motivations (identifying potentially vexatious litigants), as well as considering at a preliminary level whether the claim discloses a cause of action, and is free from material defect or irregularity.[8]

The court has stated that any further assessment of the strengths of each parties' case, over and above considering whether a case discloses a cause of action, has any obvious flaws and is bona fide, is "highly imprudent" *Fiduciary Ltd v Morningstar Research Pty Ltd* at [39]. This is appropriate, as a defendant wishing to attack the plaintiff's pleadings (rather than its financial position) ought to do so via a strike out application.

The existing discretion protects defendants in those infrequent circumstances where a plaintiff might use litigation for a collateral purpose or is otherwise an abuse of process.

4. Courts will be less inclined to order security for costs if it would have the effect of unreasonably stultifying the plaintiff's claim.[9] It is recognized that, depending on the other factors involved, there are circumstances where an order will be appropriate even if a plaintiff's claim will effectively be stayed. This decision is made by a judge and is capable of being challenged by interlocutory appeal.

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[6] *Sir Lindsay Parkinson & co Ltd v Triplan Ltd* [1973] QB 609; *Lynnebury Pty Ltd v Farquhar Enterprises Pty Ltd* (1977) 3 ACLR 133; *Spiel v Commodity Brokers Australia Pty Ltd (in liq)* (1983) 8 ACLR 410; ; *Sydmar Pty Ltd v Statewise Developments Pty Ltd* (1987) 73 ALR 289; *Fiduciary Ltd v Morningstar Research Pty Ltd* (2004) 208 ALR 564 at [85]-[101])

[7] (1992) 8 ACSR 569. See also *Bufalo Corporation v PrimeLife Corporation* [2009] VSC 171.

[8] *Jodast Pty Ltd & Ors v A & J Blattner Pty Ltd & Ors* (1991) 104 ALR 248

[9] *Fiduciary Ltd v Morningstar Research Pty Ltd* at [72]-[74]; *Staff Development & Training Centre Pty Ltd v Commonwealth of Australia* [2005] FCA 1643)

In weighing this factor, a court will be more inclined to allow the case to proceed if it potentially benefits a group of affected persons that is wider than the plaintiff.[10]

5. Finally, there is a general principle that a security for costs application should be made by a defendant at an early stage in proceedings.[11] In Buckley, Moffitt P stated:

> The primary reason why the application should be brought promptly and pressed to determination promptly is that the company [plaintiff], which by assumption has financial problems, is entitled to know its position in relation to security at the outset, and before it embarks to any real extent on its litigation, and certainly before it is allowed to or commits substantial sums of money towards litigating its claim.[12]

This goes some way to ensuring that defendants apply for security out of a genuine concern about costs recovery, rather than strategically deploying an application in an effort to derail or halt the litigation, or otherwise force the plaintiff to bear additional legal costs.

In our view, the jurisdictional thresholds and fundamental discretionary principles applied by courts in New South Wales (and most Australian jurisdictions) work together to ensure that security for costs will be ordered against plaintiffs in appropriate circumstances, particularly when that plaintiff appears to have taken measures to avoid the consequences of the litigation that it has brought, or that a nominal plaintiff is being used by the true beneficiary of the litigation to shield themselves from the risk of adverse costs. The thresholds and principles otherwise preserve the right of individual plaintiffs to bring proceedings without fear that its claim will be stayed.

The existing framework provides an adequate policy balance and should not be the subject of any modification.

Litigation Funding

In addition to those outlined above, there is also a fundamental principle that a court is more likely to order security for costs when the plaintiff is suing for the benefit of other persons.[13] This has been adapted by the court to extend to third party litigation funders that have taken a material interest in a plaintiff's cause of action, in exchange for the payment of legal costs and the provision of an indemnity against adverse costs and security for costs orders.

In circumstances where the indemnified plaintiff is often without their own means to pay an adverse costs order (for instance, they are a representative party in a class action, or a company in liquidation) then the application of ordinary principles suggests that security be ordered and paid by the funder.

We believe that funded proceedings are adequately dealt with by existing principles.

Speculative Funding Arrangements

We are concerned by a recent decision of the Supreme Court of New South Wales which regarded as relevant to a security for costs application the fact that the plaintiff's solicitor was acting on a conditional fee basis.[14] Such "No Win-No Fee" agreements are designed to provide access to justice by making the payment of legal costs conditional on the plaintiff achieving a successful outcome in the litigation. Such agreements are highly regulated, and typically do not involve any agreement to indemnify the plaintiff against an adverse costs order.

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[10] *Tran v The Commonwealth* [2009] FCA 921

[11] *Staff Development & Training Centre Pty Ltd v Commonwealth of Australia*).

[12] *Buckley* v *Bennell Constructions Pty Ltd* (1974) 1 ACLR 301 at 309

[13] *Green (As Liquidator of Arimco Mining Pty Ltd) v CGU Insurance Ltd* [2008] NSWCA 148

[14] *Del Bosco v. Outtrim* [2008] NSWSC 105

To the extent that conditional fee agreements are aimed at plaintiffs who are otherwise unable to meet their *own* legal costs up-front, it is perverse for the court to regard this as a factor that speaks in favour of the plaintiff paying the defendant's legal costs up-front.

We regard the existence of a speculative fee arrangement as irrelevant to the exercise of judicial discretion in relation to security for costs.

Representative Proceedings

In the representative proceeding of *Bray v F Hoffman-La Roche Ltd* (2003) 130 FCR 317, in considering whether a security for costs order was justified, the court looked to the financial circumstances of each of the members of plaintiff group, the estimate of the legal costs in respect of which security was sought, and whether the order would stifle the proceedings.

In our view, the ordinary application of legal principles would speak against an order that a representative plaintiff pay security for costs in proceedings not involving a litigation funder. The purpose of the representative proceeding mechanism was to enable an individual plaintiff to represent a broader group of similarly situated group members, to determine the issues of law and fact that were common to all of them and, in so doing, achieve considerable public policy benefits by increasing access to justice whilst reducing both legal costs and the burden on the judicial system. The costs of the class action defendant may be higher than would otherwise be the case if defending a proceeding brought by a lone individual, but they would generally be far lower than if each or even a number of affected individuals instituted separate proceedings. Further, the defendant to a class action is likely to be in a strong financial position.

We believe that the application of existing principles will adequately balance the rights of defendants to representative proceedings against the public policy benefits that flow from allowing validly constituted representative proceedings to proceed, both in terms of access to justice and the effective administration of mass claims.

PUBLIC INTEREST AND PROTECTIVE COSTS ORDERS

Public interest or protective costs orders aim to shift or balance the threat of adverse costs orders with the public benefit to be obtained from the proceedings being brought by a plaintiff. Such an application could be made under Division 1 of Part 42 of the UCPR which enables the court to alter the general rule that costs follow the event. In particular, 42.4(4) provides that a court may specify at the outset of the proceeding, the maximum costs that can be ordered where there are special circumstances or it is in the interests of justice to do so.

Notwithstanding this, such orders have been sought and granted in very few instances. In our view, there should be a greater prominence given to the court's ability to order on the application of the plaintiff, that the costs of the unsuccessful plaintiff or for both parties to be capped at a fixed amount immediately following the commencement of the proceeding.

A number of past reviews into the law and practice relating to public interest and protective costs orders have recommended that greater clarity be given to the criteria against which an application for such orders will be assessed, and greater prominence given to their availability.[15] The reports note that, notwithstanding the technical availability of these orders, current practice usually results in the non-pursuit or abandonment of public interest cases, due to the threat of an adverse costs order against a plaintiff who was little or no financial incentive to bring the proceedings. In summary, these reports recommended:

- The establishment of definite public interest criteria for assisting and/or directing the court determining whether a proceeding should be granted relief; and

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[15] Australian Law Reform Commission, "*Costs Shifting – Who Pays for Litigation*" (October 1995); Department of Environment, Water, Heritage and the Arts, "*The Australian Environment Act: Report of the Independent Review of the Environment Protection and Biodiversity Conservation Act 1999*" (October 2009) and the Victorian Law Reform Commission's "*Civil Justice Review*" (2008)

- Where a proceeding is deemed to be in the public interest, specifying the range of available costs orders to allow a plaintiff to apply for particular relief and provide both parties with a predictable range of outcomes.

The current state of confusion is exemplified by McHugh J's obiter dictum in *Oschlak v Richmond River Council*,[16] in which it was said that displacing the normal costs rule with reference to a non-specific 'public interest' criterion is problematic. In His Honour's opinion, most litigation concerns a matter of public interest, and that judicially-determining distinguishing principles would be "probably impossible".[17]

The legislature should provide criteria to assist the court's in determining what matters are considered to be in the public interest

Where the courts have found a proceeding to be in the public interest or have an element of public interest, the effect of such a finding on the courts determination of the appropriate costs order to be made is unpredictable.

The variety of costs orders recently made in proceedings that have been found as being as in the public interest show an inconsistency in the application of public interest or protective costs orders. We note that in three recent cases, the plaintiff was found to have raised novel questions concerning the construction of the *Environmental Protection and Biodiversity Conservation Act* 1999 (Cth), but that different costs orders were made in each.[18]

In our view, uncertainty for the plaintiff about their adverse costs exposure is a deterrent to public interest litigation, as well as creating another layer of uncertainty and therefore risk for defendants.

The legislature should identify the costs orders that are available to the plaintiff in a public interest proceeding.

Conclusion

The principles that are applied when ordering security for costs strike the right balance between ensuring access to justice and protecting defendants. We believe that the common law is an adequate and appropriate mechanism for the determination and weighing of these principles; providing parties with certainty about the factors to be applied in a proceeding, and enabling judges to develop the law and the application of principles to meet new challenges.

Public interest and protective costs orders require the same level of certainty that has developed with security for costs orders. However, in our submission, it is clear from cases cited that legislature needs to define what it regards to meet the public interest requirement, and to articulate the range of costs orders that could follow the making of such a determination.

Yours faithfully

Andrew Grech
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[16] (1998) 193 CLR 72

[17] See also, VLRC report at 15 above, and *Save the Ridge Inc v Commonwealth* [2006] FCAFC 51

[18] *Blue Wedges Inc v Minister for Environment, Heritage and the Arts* [2008] FCA 1106; Wilderness Society v the Hon Malcolm Turnbull [2008] FCAFA 19; and *Lawyers for Forests Inc v Minister for Environment, Heritage and the Arts* [2009] FCAFA 114