Class actions

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In the United States, the class action is a well established feature of litigation. In New Zealand, however, representative or class actions are a rarity. In this paper, Justin Emerson considers the potential for the class action as a mode of dispute resolution.

I. INTRODUCTION

Class action procedure is a mechanism which enables a single or "representative" plaintiff individually to bring an action in which his or her claim is resolved along with the claims of others who have a similar cause of action against the defendant. Class action procedures exist in varying forms in most legal jurisdictions. In New Zealand such procedure is accommodated in rule 78 of the High Court Rules.

The underlying concept of the class action - a single individual acting as the representative of many - raises unique issues in legal systems which are founded on the notion of individuals facing each other with each ultimately rewarded by, and accountable for, his or her actions. This uniqueness combined with the reluctance of legislatures to provide guidance on the substantive issues abounding in this area has subjected the rules to the fluctuating development of case law.

This paper suggests that the case law developments in New Zealand have not advanced the rule to a form which maximises the benefits that such procedure can offer. It is suggested that the merits of a widely accessible and expanded procedure outweigh the possible costs of such a development, and that legislative reform of rule 78 and other obstructive elements is necessary. The paper examines the issues central to the class action question, and suggests solutions appropriate to the New Zealand context.

The question of reform will be addressed with close reference to procedures used overseas and to recent developments and proposals in both Canada and Australia.

While it is possible to have class defendants as well as plaintiffs, the device is most frequently used by plaintiffs and this paper focuses only on that aspect of the law.

II. WHAT IS A CLASS ACTION?

The class action has its origins in the courts of equity. Equity saw the need for a process which avoided large numbers of persons having similar claims from pursuing separate actions against the same defendant. An earlier rule of compulsory joinder which forced all persons interested in the subject matter of the suit to become parties proved

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difficult to manage in practice. Equity thus responded with the class action. This course of development occurred in both England and America.[1]

The class action was developed as a device by which a single plaintiff could pursue an action on behalf of all persons with a common interest in the subject matter of the suit. The ruling of the court would bind all class members. This was perceived as a means of fostering both judicial economy and social utility - the courts would no longer be inundated with numerous claims relating to a common subject matter, and individual plaintiffs with claims too small for individual pursuit were provided access to the courts. In the United States the class action also served an effective enforcement function, especially in the areas of civil rights, anti-trust and securities law violations.

It has often been mistakenly asserted that class actions and representative actions are different devices. New Zealand and England have rules known as "representative", whereas the United States rules are known as "class". Although different in form, these rules are of identical nature, and are merely specialised developments of the more general class action concept. Thus although the New Zealand rule has special characteristics which appear to distinguish it from the American "class" description, essentially it remains a class action device.

Further confusion of terminology occurs with the distinction between class and derivative actions. The shareholders' derivative action is a device which arises out of the exceptions to the rule in *Foss* v *Harbottle*.[2] In a derivative action, the plaintiff brings the action on behalf of the company to remedy a wrong done to the company. The confusion in terminology arises because the plaintiff must frame his or her action as representative of all the *members* of the company rather than the company itself. The action is thus representative in nature but derivative in form. A more typical representative action involving a non-derivative claim on behalf of the shareholders could occur, for example, where the company proposes to act *ultra vires*.

III. CLASS ACTION PROCEDURE IN NEW ZEALAND

Class action procedure in New Zealand is more familiarly known as representative procedure. Rule 78 of the High Court Rules provides:[3]

> Where two or more persons have the same interest in the subject-matter of a proceeding, one or more of them may, with the consent of the other or others, or by direction of the Court on the application of any party or intending party to the proceeding, sue or be sued in such proceeding on the behalf of or for the benefit of all persons so interest.

1 Ontario Law Reform Commission *Report on Class Actions* (1982) 5-9.
2 (1843) 2 Hare 461.
3 Judicature Amendment Act 1985 (No 2), First Schedule.

The interpretation of rule 78 is largely governed by the case law on its precursor.[4] Rule 78 is little different to rule 79, and significantly it repeats those characteristics which have seriously detracted from the use of the procedure. English case law has played a substantial part in the shaping of the New Zealand procedure, based on the interpretation of these characteristics in the inherently similar English rule.[5]

The major difficulties with the rule stem from the judicial interpretation of the term "same interest".

The leading case which forms the basis of "same interest" analysis in England and New Zealand is *Duke of Bedford* v *Ellis*.[6] In that case, a group of stall holders in a market sued on behalf of themselves and "all other growers of fruit, flowers, vegetables, roots and herbs." The action was intended to enforce various preferential rights the stall holders contended were owed to them. The case resulted in the seminal statement of Lord Macnaghten:[7]

> Given a common interest and a common grievance, a representative suit was in order if the relief sought was in its nature beneficial to all whom the plaintiff proposed to represent.

Lord Macnaghten's formula was not further expanded in the case, but it is clear there is considerable overlap between the three elements in the test.

The number of actions bought under the procedure in New Zealand have been few. The paucity of case law in the area has meant an accurate assessment of when an action is appropriate or is likely to succeed cannot be made, and this acts as a considerable deterrent to the utilisation of the procedure. Many other factors, though, have acted as a disincentive to the bringing of actions in class form. These factors and possible solutions are outlined below.[8]

The foremost disincentive has been the limitations on the pursuit of damage claims. New Zealand cases have duplicated English restrictions in their interpretation of the requirement of "same interest". This interpretation initially imposed a blanket restriction on the use of the procedure for damage claims, thereby reducing the economic feasibility of the procedure. Although recent case law has somewhat pierced the restriction, the area is still very uncertain and remains far behind the level of utility that has been achieved in the United States with a more liberal approach.

Another factor which acts as a limitation on the use of the procedure is the financial costs involved in bringing an action. The problem arises not so much from the actual

4 Rule 79 of the Code of Civil Procedure:
Where there are numerous persons having the same interest in an action, one or more of them may sue or be sued, or may be authorised by the Court or a Judge to defend in such action on behalf of or for the benefit of all persons so interested.

5 Supreme Court 1965 Ord 15, r 12.

6 [1901] AC 1.

7 Ibid 8.

8 Below, Part V et seq.

expense of the action, but from the "free-rider" notion. The free-rider effect concerns the unjust enrichment of non-contributory class members. Class actions are brought by a representative plaintiff on behalf of the class. The members of the class, although they may benefit from the action, are under no obligation to contribute in any manner to the litigation. This financial burden on the representative plaintiff exists as a serious disincentive to class actions.

Three main areas of cost are pertinent to the problem: legal costs, party and party costs, and the costs of notice. The New Zealand legal system offers very little to soften these blows to the representative plaintiff. Although many options exist to overcome these cost barriers to litigation, each raises significant questions about who should most appropriately finance an action.

IV. THE QUESTION OF REFORM

Any question of altering the existing rule 78 class action procedure must carefully address what such changes will achieve, and at what cost. In the international context the pace of class action reform is rapid.

In 1982, the Ontario Law Reform Commission ("OLRC") produced a comprehensive report on class actions.[9] Although the report has not yet been legislatively acted upon in Ontario, the legislative proposal of the Commission remains an intelligent initial source of reference for an examination of this topic.[10]

The Australian Law Reform Commission has been working on a document proposing reform since first issuing a discussion paper on the topic in 1979.[11] More immediate changes in Australia include a recent legislative reform of the Victorian and South Australian class action procedures.[12]

The general focus of these international reforms has been to overcome the restrictiveness of the case law by recognizing the procedure as a more flexible device, to remove some of the extra-judicial obstacles to the use of the procedure (such as the costs factor), and to make the rules more procedurally express so as to eliminate uncertainty as to the appropriateness of the procedure.

Whether an expansion of the procedure to increase its utility is appropriate in New Zealand involves a weighing of the benefits and costs of the use of class action procedure. The benefits and costs will be discussed in turn.

9 Above n1.
10 Ontario Law Reform Commission Draft Bill Proposal, 861-878.
11 Law Reform Commission of Australia *Access to the Courts-II Class Actions* (Discussion Paper No 11, 1979).
12 Below n 31.

A. *The Benefits of Expansion*

1. *Access to the courts*

Court actions by individual persons on behalf of themselves are often rendered impracticable because the potential costs far outweigh the returns. By combining many of these individually untenable complaints the cost of litigation is dramatically decreased for the plaintiffs, and a realistic access to the courts is created.

It is often argued that increased access to the courts will lead to litigation which ought not to have been brought at all. In other words, the cost system serves the useful and desirable function of weeding out actions which do not deserve judicial attention. Opponents thus contend that class actions should be restricted only to an amalgamation of existing viable individual claims.

The weakness of this argument is the assumption that the viability of an individual claim gives an accurate assessment of its legitimacy and importance. Indeed, providing access for untenable claims has been described judicially as one of the most important goals of class actions. In *Naken* v *General Motors of Canada Ltd*, Arnup J stated:[13]

> [when consumers purchase a defective article]... in many instances the pecuniary damages suffered by any one purchaser may be small, even if the article is useless. It is not practical for any one purchaser to sue a huge manufacturer for his individual damages, but the sum of the damages suffered by each individual purchaser may be very large indeed. In such cases it would clearly be convenient and in the public interest if some mechanism or procedure existed whereby the purchasers could sue as a class.

Thus the vindication of the rights of groups of people without effective strength to litigate is seen as a meritorious step even at the cost of an increase in volume of litigation.

2. *Judicial economy*

There is no disagreement that class actions can achieve judicial economy where numerous individually recoverable claims exist. By litigating multiple small claims as a single action economies can be achieved both administratively and in terms of efficacious use of court time.

This benefit, however, must be viewed as more theoretical than real. The number of cases in which many individually practicable claims exist will be few. The real effect of an expansion will be to stimulate the condensing of many individual claims which would not be individually pursued. In all likelihood, this would lead to an *increase* in the amount of litigation.

13 (1978) 21 OR (2d) 780, 784.

3. *Behaviour modification*

An extended class action procedure can play an important role in the behaviour modification functions of justice. The potential for large judgments against the defendant acts as a disincentive to the defendant or other potential defendants from risking or attempting further wrongs. Without this disincentive the wrongdoer can proceed in his or her activities without fear of any judicial recourse.

Some commentators argue that the only proper function of civil litigation is to redress conflicts between parties, and not to discourage future conduct.[14] These opponents argue that the objective of deterrence should be pursued through criminal or quasi-criminal sanctions. However, law is often recognised as having a behavioural responsibility in a much broader capacity:[15]

> The function of a legal system is not limited to its role in providing individuals with a mechanism by which to resolve disputes and redress grievances. Law also serves as a standard of the conduct which the community or the society expects from its members and by the same token, the judicial system should provide realistic sanctions which the community can invoke in order to enforce obedience to its prescribed values and rules of conduct. It seems clear, therefore, that if sellers and manufacturers are, for whatever reason, in practical effect immune from the sanctions of the present legal structure with respect to some claims which might be brought against them, the community has to that extent lost its ability to compel obedience to the standards of conduct it has established.

Any restriction on the degree to which class actions may operate has a commensurate effect on social control through the law. An extension of the class action procedure would both serve as a means of encouraging compliance with the law, and halt the feeling of impotence and dependence on government intervention which many small claimants suffer.

4. *Resource effectiveness*

Closely associated with the behaviour modification benefit are the benefits accruing from a more efficient use of resources. Present sanctions for improper actions in company management may be inadequate deterrents in many situations.[16] Penalties are often token in relation to the extent of the improper gains made.

14 Scott "Two Models of the Civil Process" (1975) 27 Stan L Rev 937.

15 Jones and Boyer "Improving the Quality of Justice in the Market Place: The Need for Better Consumer Remedies" (1971-72) 40 Geo Wash L Rev 357, 367.

16 For example, the minor fines in ss 58 and 60(2) of the Securities Act 1978.

The reality of the situation is that with fixed sanctions of fines or imprisonment, an opportunity is provided for a wrongdoer to weigh the costs of his or her actions. As the OLRC concluded:[17]

> Even where a criminal sanction is available, and a conviction is obtained, there is evidence to the effect that the fines levied in criminal proceedings do not serve to deprive defendants of the fruits of their wrongful conduct or to require them to internalize the costs of the injuries imposed upon individual victims; accordingly, in many cases a conviction may do no more than impose a "licence fee" upon wrongful conduct, which remains sufficiently profitable to justify continued wrongdoing.

If the benefits of the wrong exceed the sanctions then the deterrent and prevention resources of the legal system are being ineffectively utilised. By providing the responsibility of redress to the individuals harmed through a damage claim process, the potential cost of wrongful conduct becomes greater, and resources are being more effectively utilised.

5. *Prevention of unjust enrichment*

Equity has continually devised mechanisms by which to prohibit unjust enrichment, viewing the creation of wrongful windfalls as an action worthy of redress. Without an extended class action procedure, wrongfully obtained profits remain in the possession of the wrongdoer.

The process by which unjust enrichments are extracted from wrongdoers is known as *"cost internalisation"*, and involves forcing the defendant to compensate the victims in regard to the degree of damage caused. This redistribution of the enrichment is seen without disagreement as an equitable and fair action. Thus by extending the class action procedure a more equitable system of redress is created.

B. *The Costs of Expansion*

1. *Strike suits*

Class action procedure has sometimes been described as a process for "legalised blackmail".[18] These criticisms stem from the perceived potential for class actions to be used as a means of exploitation.

A "strike suit" describes the process where frivolous or unmeritorious actions are brought with the singular intention of inducing the defendant to settle the claim. The calculation by a defendant to settle for such insubstantive actions is based on a number of coercive circumstantial factors.

First, the large outlay of both time and cost required to defend an action can be a deterrent even when there is a good prospect of a successful defence. This problem is

17 Above n1, 144.
18 Above n1, 146.

exacerbated in jurisdictions where costs are not awarded to successful litigants. Second, the sheer size of the claims often involved encourages defendants to settle. Even if the defendant is reasonably certain of a favourable outcome, a small degree of doubt can often lead to a settlement when in the context of a multi-million dollar claim. Third, a defendant may be offered the prospect of settling for a very small amount, often with only the class plaintiff in an individual capacity. The small price of this compromise often takes precedence over a formal resolution of the issue. Fourth, even if the defendant is sure of a favourable outcome, there is an extensive risk of adverse publicity. The propensity for newspapers to engage in witch-hunting escalates the potential cost of an action so as to render settlement more favourable. Finally, the defendant must also be concerned with balance sheet implications. The detrimental effect of a large damages claim appearing in the balance sheet discourages defendants from letting the plaintiffs file an action.

Despite these indications of the potential for exploitation by the class, empirical evidence indicates there is "no basis for concluding that class actions are yielding disproportionate numbers of early settlements that might reflect a pattern of 'legalized blackmail'".[19] Part of the explanation for this lack of exploitation are the mechanisms which can be used to weed frivolous and meritless claims from the procedure. The first is a procedural requirement that the action satisfy certain tests before it can be certified as appropriate for class form. In the United States, a complicated certification process locates the weakness of frivolous claims and prevents them from proceeding into litigation.[20] Second, all civil actions before the courts must satisfy the natural safeguard of being able to state a cause of action. If no reasonable cause of action can be illustrated by the representative plaintiff, then the action can be frozen at an early stage, eliminating most of the financial outlay that the defendant would have been required to make in defence.

The problem of potential defence costs acting as an incentive to settle is often met by the general rule that costs will be awarded to a successful litigant. This means any outlay the defendant makes in defending the action will be ordered to be compensated by the plaintiff. Even where rules prohibiting costs prevent this type of compensation, a more flexible approach could permit such recovery only in exceptional circumstances, such as where a claim is frivolous.

In summary, an expanded class action procedure will not necessarily create a strike action problem if the procedure is drafted appropriately.

2. *Unfair settlements*

Because of the peculiar representative nature of a class action there exists the possibility of unfair or abusive settlements. These involve settlements made entirely for the benefit of the class plaintiff, and/or the class lawyers.

19 Above n1, 163.

20 Federal Rules of Civil Procedure for the United States District Courts, r 23(a).

As the class plaintiff is representative of the interests of the whole class, any settlement the plaintiff reaches should encompass the interests of the class. But often a representative plaintiff may bring a meritorious action in class form, not to benefit the class, but solely to inflate the possible settlement value of the plaintiff's individual claim. Alternatively, the intentions of the plaintiff may be good but the defendant may make a generous offer to induce a rapid settlement with the individual.

This abuse of the class action procedure is unfair not only to the defendant, who may settle for more than the individual claim of the representative plaintiff, but to class members, whose claims are exploited for the personal gain of the representative plaintiff. Although the action could be continued by a new representative plaintiff, this often proves difficult if the representative was so selected for his or her financial or other capabilities.

Settlements favourable to class lawyers can often be more damaging because the whole class is bound by the settlement and cannot pursue the action in court. Solicitors can engage in damaging settlements when their form of payment is by way of contingency fees. This takes the form of a payment of the solicitor *only* on the result of a successful litigation. To avoid the risk of non-payment, solicitors can be induced to settle the claim for substantially less than could have been awarded through litigation.

This guarantee of payment benefits the solicitor, but is often not in the best interests of the class. The exploitation is often possible due to the misinformed state of most classes.

The problems of unfair settlements are not without remedy, however. A convenient device to overcome this exploitation is to require an informed consent to the settlement before it can be regarded as valid or binding. This informed consent could be either judicial, or from a body such as the law society, and would effectively eliminate this potential problem.

3. *Floodgates fear*

Another significant concern of extending class action procedures is that existing judicial and administrative resources will be flooded by a large quantity of new class actions. This may overload the legal system. Many arguments exist to dispute this concern.

First, it is a sound argument that legitimate legal claims should not be sacrificed in order to meet the existing capabilities of the legal system. Thus even if a flood of litigation was imminent, resources should be expanded accordingly, rather than questioning the merits of potential claims in law.

Second, the floodgates concern fails to recognise the many other elements which detract from litigation. Questions of litigiousness, costs, other changes to the form of the procedure, the extent of civil rights provisions in the legal system, and social behaviour trends, all influence the quantity of litigation. The extension of the class

action procedure is but one variable in a multi-variable equation and will not necessarily cause any substantial change.

Finally, there is empirical evidence from the extension of the United States class action procedure in 1966.[21] This major revamping of the Federal Rule was predicted to involve a drastic flood of existing legal resources. The flood never eventuated however, and the system quite comfortably accommodated a gentle increase.

Any extension of the class action procedure does raise the possibility of increasing the volume of litigation. But due to the number of variables involved no absolute determination of volume can be made. Although a flood of overloading proportions is not a serious likelihood, this area is still worthy of further investigation in an attempt to determine some indication of possible effects.

4. *Manageability*

Opponents of an extension of class action procedure also contend that such an extension will encourage unmanageable claims, and will result in procedural innovations of an undesirable character in the process of accommodating difficult damage claims. It is submitted that this is an unlikely consequence due to the strong indications from United States case law as to what procedural innovations are appropriate, and the consequences which follow from them.

5. *Conclusion*

Although there are many problems stemming from an expanded class action procedure, closer examination reveals that many of the costs are more severe in theory than in reality, and that most of the costs can be controlled or mitigated through carefully drafted provisions within the rule itself. It is submitted that the significant benefits that can be achieved from a limited and cautious expansion of the procedure outweigh any remaining cost residue.

V. THE NATURE OF THE EXPANSION

The nature of any reform must be carefully assessed. It must take into account the benefits sought to be achieved, the nature and philosophy of the New Zealand legal system, and avoid the pitfalls found in the procedures of other jurisdictions.

The OLRC proposal provides a useful starting point for consideration of the substantive aspects of the rule because of the comprehensive examination of the issues which accompanies the proposal.[22] In addition, comity suggests that any proposals which come from the Australian Law Reform Commission should also be considered. The appropriateness of these proposals to the New Zealand context will be evaluated.

21 Above n1, 170-182.
22 Above n10.

Five main issues require specific analysis in respect of the nature and extent of the reforms. They are: damages and common interest; certification; notice; exclusion from the class; and costs. These issues are discussed below.

VI. DAMAGES AND COMMON INTEREST

The damages and common interest issues are closely connected to each other. The common interest issue involves the degree of common interest that must exist between class members for the procedure to be used. More specifically, it considers whether the presence of questions of law or fact unique to individual class members prevents the use of the procedure to resolve questions common to the class. The damages issue involves case law which has suggested that a class action is never appropriate in a claim for damages because questions unique to each individual class member would always have to be resolved. Whether such a blanket prohibition on damage claims is justifiable has been discussed at length in recent case law developments in both New Zealand and overseas.

1. *England*

The damages and common interest issues in New Zealand, Canada and Australia have largely been governed by the seminal English case *Markt & Co* v *Knight Steamship Co Ltd*.[23] The case involved a class action for damages by all the owners of cargo on a ship that was lost at sea.

The court held that a class action for damages was inappropriate for two reasons. First, each of the members of the alleged class had separate contracts with the owner of the vessel and therefore did not have a "common interest". If issues specific to individual claimants were likely to arise in the proceedings, then an action in class form was inappropriate. Second, the court held that where the remedy sought by the class is damages:

> ... the machinery of a representative suit is absolutely inapplicable. The relief which [the plaintiff] is seeking is a personal relief, applicable to him alone, and does not benefit in any way the class from whom he purports to be bringing the action.

This decision has a profound effect on class actions in England, restricting classes to non-monetary remedies, and thereby limiting the economic feasibility of instigating an action in class form.

However, recent case law suggests that the courts are viewing a blanket restriction as inappropriate. In the case of *Prudential Life Assurance Co Ltd* v *Newman Industries Ltd*[24] the representative plaintiff instigated a class action on behalf of all the shareholders in Newman Industries Limited for a declaration of entitlement to damages for fraud and breach of duty. Vinelott J at first instance adopted a two stage approach of resolving the common issues in the class proceeding, and leaving the individual issues for secondary

23 [1910] 2 KB 1021.
24 [1979] 3 All ER 507.

individual proceedings. In respect of the damages question, the court sought to overcome the *Markt* conjecture that damages were of a personal nature inappropriate to class treatment by holding that no order would be made in favour of a representative plaintiff if the order could have the effect of conferring on a member of the class a right he or she could not have asserted in individual proceedings. Vinelott J thus maintained the restriction on the award of the damages due to the requirement of individual proof for its determination.

The next notable advance towards damage recovery was in the 1981 case of *EMI Records Ltd* v *Riley*.[25] In *EMI*, the two stage process adopted by Vinelott J was side-stepped, the court instead favouring the possibility of a direct award of damages. The case involved a representative action for an inquiry as to damages by members of the recording industry over breaches of copyright by a cassette pirate. Dillon J distinguished the restriction *Prudential* had maintained on the awarding of damages by contending in the circumstances the two stage process would be redundant. Individual proof by members of the industry would be extremely difficult, and as all members belonged to the representative body, the British Phonographic Industry, an award to this body in a representative capacity (rather than a class of individuals) would be most practicable.

This is a strong, if somewhat amorphous, recognition that in some instances a class action for damages may be resolved in a single class proceeding. As with *Prudential*, however, *EMI* is only a first instance decision, and does not necessarily reflect the future of the case law. Another first instance case marginally preceding *EMI* adhered to the *Markt* approach.[26] This leaves the area still considerably uncertain, and ripe for legislative clarification.

2. *Canada*

Class action procedure in the various Canadian provinces has followed a path of development similar to that in England. Canadian courts were for many years burdened by the restrictive *Markt* decision. But in the 1970s, social pressures impressed the judiciary with the necessity to develop a representative procedure.[27]

In *Farnham* v *Fingold*[28] the Ontario Court of Appeal pierced the blanket restriction on damages claims and allowed a class action because the assessment of damages to the class was not dependent upon the need to resolve individual issues, but was based simply upon common issues and a pro rata mathematical calculation.

Five years later further restrictions on damages claims were temporarily swept away by the Ontario Court of Appeal. In *Naken* v *General Motors of Canada Ltd*[29] a group of representative plaintiffs pursued an action for damages on behalf of every purchaser of

25 [1981] 2 All ER 838.
26 *EETPU* v *Times Newspaper* [1980] 1 All ER 1097, 1104.
27 J K Bankier "The Future of Class Actions in Canada: Cases, Courts, and Confusion" (1984) 9 Can Bus LJ 260, 269.
28 (1972) 32 DLR (3d) 433.
29 (1978) 21 OR (2d) 780.

a certain model of a General Motors car. The Plaintiff attempted to bring the case within the *Farnham* decision by claiming that all class members had suffered identical damages of $1,000. The Court of Appeal accepted this contention, but held that individual proof would still be necessary for each member to establish reliance.

In an innovative solution to the problem, the court held that if there was a favourable determination of common questions of liability for the plaintiff, the individual issues could then be examined by a court appointed referee. This had the dual effect of permitting class actions even where individual issues were present, and providing a means for resolution of individual issues that avoided the impracticability of additional individual claims.

This development was short-lived. The decision of the Court of Appeal was overruled by the Supreme Court of Canada. The court held that class actions for the award of damages would not be permitted where individual proceedings were necessary to establish the total liability of the defendant. Although this limited the potential for the pursuit of damages, the restriction was not a total prohibition. If the total amount of the defendants liability to the class could be established through common proof, then the action may proceed by way of class action. This decision draws the Canadian case law to a position similar to that established by the *Prudential* decision in England.

3. *Australia*

The early case law developments in England again provided the basis for interpretation of the class action rules in the different Australian States.

In 1977 the Australian Law Reform Commission released a discussion paper[30] proposing reform of class action procedure which resulted in reforms in both Victoria and South Australia.[31] The reforms of both states provide that class proceedings will not be inappropriate for the resolution of common issues merely because the actions arise out of separate transactions, or that there is a claim for damages that would require individual issues to be resolved. The South Australian reform also expressly recognises a two stage resolution process whereby common issues would be resolved in class proceedings, and individual issues would be resolved in separate actions or separate trials within the actions.

In respect of the damages issue, the most significant part of the reforms is the high degree of procedural flexibility given to the courts. Both states allow the courts to fully determine the conduct of the action. This could be a device by which the courts open up the procedure to allow resolution of damage claims containing individual issues in single proceedings.

It is also important to note that without some form of commensurate changes to other factors which deter the use of the procedure (such as the costs problem), the

30 Above n 11.

31 Supreme Court Act 1958 (Victoria), s 62(IC); Ord 6 r 2 Federal Court Rules; Supreme Court Rules (South Australia), r 34.

reforms may only be of limited effectiveness in achieving the benefits that can accrue from an expanded procedure.

4. *United States*

Class actions are frequently (some would say too frequently) utilised in the United States. Although many varying forms of class actions exist at the state level, rule 23 of the Federal Rules of Civil Procedure has been the source of the major case law developments.

The United States attitude towards damages claims has been significantly more flexible than the English model. First, rule 23 expressly recognises that the presence of individual issues within the class claim does not restrict the use of class procedure.[32] Secondly, the courts have made efforts to expand the utility of the procedure to cover claims even where individual issues would need to be resolved in order to determine the total extent of the defendant's liability. In other words, courts have not been overly concerned with the notion of conferring on the defendant a liability he or she may not have incurred if individual actions were bought.

When faced with actions involving individual issues essential to the liability determination the courts have adopted some unique and controversial solutions. Among them include the idea of conducting mini individual trials within the body of the class action and the possible use of a referee or similar impartial adjudicator to resolve those issues. This process is known as the split trial, and was a development which was rejected by the *Naken*[33] case in Canada. This technique, however, is subject to its own manageability limitations, and is often ineffective where the class is very large, where the identity of all the class members is not known, and where the split would cause the action to be unduly protracted.

Perhaps the most graphic example of the United States attitude towards damage recovery and the courts' flexibility towards the issue, is the concept of punitive estimated awards. Where it would be impracticable or impossible to resolve in separate actions those questions unique to individuals, the courts have approved the use of computers and survey techniques supported by expert evidence to compute the loss suffered by the class.[34]

One of the most controversial estimation methods has been the "fluid recovery" approach. In *Daar* v *Yellow Cab Co*[35] an action was bought on behalf of all the passengers of a taxi company to have used the service over a specified period during which the Cab Company was unlawfully overcharging. The court recognised the overcharge was incapable of individual assessment, and indeed the class members were incapable of identification. However, the court was concerned with the punitive notion

32 Rule 23(c)(4).
33 Above n 31.
34 *In re Co-ordinated Pretrial Proceedings in Antibiotics Antitrust Actions* 333 F Supp 278, 289 (1971).
35 63 Ca R 724 (1967).

of the action, and ordered the company to reduce its fares by the overcharge amount over an equivalent time period. This resulted in many persons who were not members of the class recovering under the action, but had the desired punitive effect on the company. The case was quite exceptional, however, and has met with little judicial acceptance.

In summary, case law treatment of claims for damages where individual issues are involved has been innovative as the courts have sought to give the procedure an extensive ambit of utility. The concept of punitive estimated damages has gained much case law support, though some aberrant decisions have taken the concept of unfavourable extremes.

5. *New Zealand*

In the case of *Take Kerekere* v *Cameron*[36] two tenants seeking to represent many other tenants sued for damages for trespass. Chapman J rapidly dealt a severe blow to the future of class actions in New Zealand by adopting without analysis the reasoning of Moulton LJ *Markt Fletcher & Co* v *Knight Steamship Co Ltd.*[37] He held: "A representative action is moreover inappropriate to the settlement of numerous claims for damages".[38]

In *Morgan* v *Taranaki Farmers Meat Co Ltd*,[39] 112 shareholders attempted to bring a representative action claiming damages for rescission of a contract to take up shares and other relief. The action was struck out by Ostler J on the basis of unspecified authorities.

This ended the early history of the representative action for damages in New Zealand. The renewed activity in the field of class actions in the overseas context has sparked a new judicial approach to the device in recent years however.

In the case of *The Auckland Paraplegic and Physically Disabled Association Incorporated* v *South British Insurance Co Ltd and Others*,[40] the damages issue was discussed by Barker J. In an earlier application the applicant had claimed to be entitled to sue the defendant as representative of all the creditors of the Securitibank group. Motions were filed by the defendants seeking orders that the reference to the representatives capacity in the pleadings be struck out. The applicant subsequently consented to such motions. The defendants, however, went on to claim costs in relation to the class procedure application. This involved Barker J having to determine the propriety of bringing the action in class form in the course of making a judgment on the costs question.

Although indicating that in the circumstances the multiple and diverse interests of the "class" members were too wide to constitute a single class, Barker J recognised the

36 [1920] NZLR 302.
37 [1910] 2 KB 1021.
38 Ibid 303.
39 [1925] NZLR 513.
40 Unreported, 28 July 1980, Auckland High Court, A1367/78, Barker J.

developments in *Prudential Life Assurance Co Ltd* v *Newman Industries Ltd*[41] without deciding the question. He said:[42]

> It seems that, as the law is developing as shown by the *Prudential* case, representative action can be brought for a declaration that a tort has been committed in given and typical circumstances. However, ... the Court will need to ensure that every claimant, with facts peculiar to him, must prove his cause of action, even though he may obtain some advantage from a declaration made in a representative capacity.

The issue was not discussed again until 1986, by which time there had been further progress in England in the form of *EMI Records Ltd* v *Riley*.[43] In the case of *R J Flowers Ltd* v *Burns*[44] McGechan J decisively broke new ground in the use of the device in New Zealand.

The case involved the cool storage of quantities of kiwifruit. The defendant had contracts with many growers of fruit. The action arose from an allegation that the defendant negligently allowed the temperature of the store to fall to a damaging level. The plaintiffs applied to the court for an order that each plaintiff may take representative proceedings.

In determining how the new rule 78 should be interpreted, McGechan J made express reference to the High Court rule 4 requirement that all rules be interpreted to secure the "just, speedy, and inexpensive determination of a proceeding". Focusing on the need to fashion the rule to meet modern requirements, he said:[45]

> the approach to this application should be liberal ... if *in*justice can be avoided the rule can and should be applied to serve the interests of expedition and economy, both indeed the underlying reason for its existence.

The conclusion to which McGechan J came on the basis of the English developments was that a class action was appropriate if:

1 Members of the class had a common interest in the proceedings, and each was able to claim as plaintiffs in separate actions in respect of the event concerned.

2 The action was beneficial to the whole class.

3 The action covered virtually the whole of the class of potential plaintiffs.

4 Where a claim for damages was concerned a class action was appropriate if:

(a) The global loss of all represented members could be established.

41 [1979] 3 All ER 507.
42 Ibid 48.
43 [1981] 2 All ER 838.
44 [1987] 1 NZLR 260.
45 Ibid 271.

(b) The consent (or implied consent) of all represented members to the payment of global damages was established.

It is submitted that the result of his analysis is that where individual issues are present (thus necessitating individual proof) an action for damages can only be resolved in respect of those individual issues where the need for that individual proof can be made superfluous by the provision of global proof. A judgment based on global proof must not impose any unjustified burden on the defendant. Indeed, McGechan J expressly commented: "The traditional concern to ensure that representative actions are not to be allowed to work injustice must be constantly kept in mind".[46]

Where individual issues cannot be resolved by global proof, it is submitted the McGechan analysis would allow the action to proceed in respect of those common elements only. The res judicata established could then aid the rapid resolution of the individual issues in separate actions.

Concerning the question of whether the existence of separate contracts prevented the use of class proceedings, McGechan J did not treat the presence of separate individual contracts with the defendant as an impediment in itself. The court was only concerned with the presence or not of common questions of law or fact for every member of the class.

The decision of McGechan J is first instance only and there exists a recent English case inconsistent with his findings.[47] The future of this current development is uncertain. It is submitted that some form of legislative action is necessary to bring a degree of certainty into the area.

In conclusion of this Part, it is submitted that the following should form the basis of a new provision in New Zealand.

First, class actions should not confer on a class member any right or remedy he or she would not have had if an individual action had been brought. This reflects the basic precept that no person should benefit from or impose a penalty on another without an appropriate cause of action. To this extent, class actions should be considered inappropriate in any instance where the ruling of the court is on any issue where common interest does not exist.

Second, despite the existence of individual issues or parties affected by issues not common to the representative plaintiffs, a class action should still be able to be brought in relation to only those common elements of the claims. This allows the advantages of class actions to accrue to the plaintiffs in the form of a res judicata on the common issues.

46 Above n44, 282.
47 *EETPU* v *Times Newspapers* [1980] 1 All ER 1097.

If individual issues are present in a damages claim it is necessary that the whole action be resolved as a two stage process, with separate actions brought to resolve the individual issues. If, however:

1. The total liability of the defendant can be determined without the need for reference to individual issues, and the group structure of the class makes a class award appropriate; or

2. The individual liability to each member of the class can be determined also without the need to resolve individual issues (and hence without the need for individual proof);

then a class procedure would be appropriate and could resolve the action in a single stage.

The United States case law, however, goes significantly further than this and has expanded the ambit of the rule to accommodate damage claims of amorphous classes even where global liability could not possibly be assessed by normal methods. This has been achieved through a willingness of the courts to estimate damages.

The OLRC also recognised the need for a large degree of procedural flexibility, and proposed a procedural discretion that would allow the courts to adopt the split trial approach developed in the United States, whereby the courts can determine individual issues within the body of the class action.[48] The proposal suggests the courts may conduct such proceedings alone or with other judges of the court, or appoint one or more persons to resolve the issues by way of inquiry and report.

It is submitted that this proposal is a meritorious compromise between the excesses of the United States expansion and procedural innovations, and the restrictiveness and limited utility of the present New Zealand rule and case law. The emphasis of the discretion is revealed in section 31(2), which states:[49]

> ... in giving such directions [as to the individual proceedings] the court shall order the simplest, least expensive and most expeditious method of determining the issues that is consistent with justice to the members of the class, the defendant and the representative plaintiff, including dispensing with any procedure that it considers unnecessary and directing special procedures regarding such matters as discovery, admission of evidence and means of proof.

It is submitted that the movement towards the split trial concept is desirable in respect of the need to maximise the benefits which the procedure can nurture. However, it must be recognised that the breadth of the discretion given to the courts to conduct the proceedings may be a Pandora's Box in respect of the questionable procedural innovations which were spurned from the United States obsession with widening the rule and using it as a punitive device. If such was the case, then the legislature should

48 Above n10, s 31.
49 Above n10, s 31(2).

be prepared to partake in further reforms to control the extent of the discretion, perhaps at the cost of the accessibility of the procedure.

VII. CERTIFICATION

The process of certification is the means by which the courts determine at a preliminary stage whether an action should be brought as a class action. It exists as a safeguard against the unnecessary and often exploitative costs of unmeritorious actions, and allows the procedural issues to be resolved before the action is actually commenced. It is submitted that this safeguard is appropriate, as the certification test can examine not only questions related to the "same interest" issue, but other factors that may indicate an action is not suitable for the class procedure. In this respect, the OLRC proposal provides a suitable structural framework for a certification test. Much of the content of the proposal, however, is of questionable suitability to New Zealand. Each of the five requirements of the proposal will be discussed in turn.

1 "The action is brought in good faith and there is a reasonable possibility that material questions of fact and law common to the class will be resolved at trial in favour of the class".[50]

It is submitted that the first part of the rule is justified because it prevents unmeritorious strike actions and helps to control the increased pressure on the administration of justice. It would be hoped, however that most actions brought without good faith would be weeded out before this stage through a lack of a cause of action.

The criticism of this provision is in respect of the second part. Although it reflects the need to protect the defendant from the considerable consequences of even an unsuccessful action, it imposes an additional burden on the plaintiff and requires the courts to hold a "mini-trial" of sorts in advance of the main action. It is submitted this element is undesirable in that the cost to the plaintiff betrays the precept that a plaintiff need only establish a cause of action before the merits of the case are examined by the courts.

2 "The class is numerous".[51]

This requirement contains all the ambiguities contained in the United States rule, offering no guidance as to how big the class must be. The existing New Zealand rule requires only "two or more persons", achieving certainty with a minimum requirement. It is submitted this certainty provides the better option, and if a process of joinder would be more efficient for small classes, this can be caught by that part of the OLRC proposal which requires the class action to be superior to other methods of resolution.[52]

50 Above n10, s 3(3)(a).
51 Above n10, s 3(3)(b).
52 Above n10, s 3(3)(d).

3 "There are questions of fact or law common to the class".[53]

This requirement is carried over from the United States provision requiring some commonality of issues which warrants pursuing the action in class form. This would replace the "same interest" requirement in the New Zealand rule which generated the difficulty in regard to the pursuit of damages.

The major problem with this provision is its failure to define the *number* of common issues that must exist. It is submitted that there need only be one issue common to the class for the social benefits of a class action to accrue. However, it is suggested that in the interests of pragmatism and efficiency there should be included a test that the issue be one of "significance".

4 "A class action would be superior to other available methods for the fair and efficient resolution of the controversy".[54]

This superiority evaluation focuses directly on the comparative merits of pursuing the action in class form. Such a test has numerous justifications and is essential in the certification process. First, the greater administrative burden imposed by widening the class action ambit warrants that the pursuit of the claim in class action form is truly superior. Second, any innovations to the cost system resulting in substantial benefits to those pursuing class actions would warrant the procedure being restricted to the most suitable claims. Third, class actions involve a determination of issues on behalf of unrepresented parties. Because they involve this added responsibility, class actions should afford the absent members greater security by requiring certification that a class action is the superior method.

5 "The representative plaintiff would fairly and adequately protect the interests of the class".[55]

This requirement comes directly from federal rule 23. The OLRC viewed an adequacy requirement as an essential component of the certification stage. A basic tenet of the New Zealand system of justice is that no person should have his or her rights determined without being afforded an opportunity to be heard. Because class actions may involve decisions being made for absent or unascertained class members which will bind them, it is an essential safeguard that the representation of the class is adequate.

Fundamental to this protection are the factors the courts must address to decide the adequacy of the representation. Important issues which any New Zealand proposal should aim to cover would be: whether the plaintiff should be a member of the class; whether adequacy considerations should be influenced by the adequacy of the class solicitor (and, if so, how is that measured); whether the financial position of the plaintiff should have any effect; and the degree of difference in interest there can be between the class and the representative. The failure to address these questions in the

53 Above n10, s 3(3)(c).
54 Above n10, s 3(3)(d).
55 Above n10, s 3(3)(e).

United States provision has resulted in a degree of case law uncertainty that should be avoided.

One of the more contentious aspects of the OLRC proposal was the inclusion of a cost-benefit analysis. This comes as a second stage to the certification test, and provides the courts with a device to deny certification where the detriment of bringing the action in class form outweighs the benefit. The provision reads:[56]

> Where the court finds that the conditions set out in subsection 3(3) have been satisfied, it may nevertheless refuse to certify the action as a class action if, in the opinion of the court, the adverse effects of the proceedings upon the class, the courts or the public would outweigh the benefits to the class, the courts of the public that might be secured if the action were certified.

This provision thus permits exclusion even when no alternative access to the courts exists for the individuals.

Certain criticisms can be levelled, however, in response to the vagueness of the considerations that the courts must take into account. It has been argued that the test requires "a measurement and then a weighing of factors that are enormously difficult to measure and virtually impossible to compare".[57] In practice, such difficulties may lead to a vein of uncertainty within the rule. The pragmatism of the provision is also open to criticism. Even if a claim is administratively unworkable by present standards, if it is a meritorious claim there is a sound argument for adapting or remoulding the legal system to accomodate it. The courts should not be given licence to avoid administrative inefficiencies.

On balance, however, it is submitted that this is a pragmatic test which must be accepted in a legal system with finite resources. If the courts are deprived of the power to exclude administratively unmanageable claims there will be a constant struggle to arrive at methods of accommodation. Such efforts may result in bizarre and undesirable procedural innovations. This is one of the failings of the United States provisions, where the absence of such provision has forced both procedural innovation and a misshaping of the literal construction of the rule to facilitate exclusion.

VIII. NOTICE

The question of notice refers to the process by which members of the class receive advice that an action is being pursued on their behalf. The need for notice derives from the fact that once decided, the ruling of the court binds the whole class. Thus if a class representative could bring an action without the knowledge of the class members, and achieve a result which would prohibit individual pursuit of the action, a fundamental injustice could occur. For this reason a suitable notice provision is essential to provide the class members an opportunity of deciding loyalties to the class.

56 Above n10, s 6.

57 JRS Prichard "Class Action Reform: Some General Comments" (1984) 9 Can Bus LJ 309, 316.

In New Zealand, rule 78 provides little guidance. If the action proceeds on the basis of the consent of the class members, then, by definition, notice has been given. However, where the plaintiff seeks to bring the action by the judicial consent option, notice is not explicitly required. One assumes the rules of natural justice extend to notice in such situations but no standards are provided for how notice should be given.

In the United States, the case law has established strict requirements in respect of the unspecific Federal Rule requirement of "the best notice practicable".[58] In *Eisen* v *Carlisle and Jacquelin*[59] the Supreme Court held that if individual class members were identifiable, notice must be given to each individual irrespective of other impracticabilities such as cost.

The OLRC proposal involves a more flexible requirement.[60] Both the giving of notice and the form it takes are a discretionary option that the courts must examine. The courts may take into account such factors as the cost of giving notice, the nature of the relief sought and the total amount of monetary relief claimed.

The primary concern with the creation of such a discretionary notice provision is the vast area of uncertainty for the plaintiff in terms of the potential cost of the action.

Some advantages over a mandatory provision do exist, however. The mandatory notice provision in the United States is a cumbersome problem which has deterred many claimants. Because the courts cannot determine the appropriateness or form of notice in regard to the circumstances of each case, the burden of notice is often inflated and unnecessary. The factors the courts may take into account in the ORLC proposal are designed to require individual notification only in cases where the seriousness or importance of the action warrant it. Thus although the Canadian approach may somewhat compromise the right to be informed of the action, it is submitted it is beneficial in its pragmatic facilitation of access to justice.

IX. EXCLUSION FROM THE CLASS

Part of the function of providing notice to the potential class members is to enable them to decide whether or not to participate. As any class action ruling will bind all the class members, they must make a decision whether they wish to be part of such an action. The notification provision can be drafted in two ways. It can automatically include the member unless he or she expressly opts out. Or alternatively, it can automatically exclude the member unless he or she expressly opts in.

The existing New Zealand provision is silent on this point, and the issue has not been discussed in case law.

The issue of which is the superior alternative is difficult to resolve. Opting in is criticized for its exclusive effect on apathetic or silent parties. Where damages will be

58 Above n20, r 23(c)(2).
59 417 US 156 (1974).
60 Above n10, s 16.

small, this will have a positive effect of reducing the administrative burden caused by an expanded class action procedure, and of weeding out frivolous claims. However it also damages the behaviour modification goal by substantially reducing the size of the class or number of actions, and establishes an exclusion clause which effectively sanctions the unjust enrichment of the defendant.

Opting out, by contrast, has the opposite effect, and is the option used in federal rule 23.[61] Apathetic or silent parties will be automatically included, thus artificially increasing the magnitude of the class beyond the actual level of interest. This has the effect of inflating the level of damages the defendant would otherwise be faced with, perhaps forcing behaviour modification beyond the real social requirements. It may also compound or contribute to the administrative stress faced by the courts by bringing inflated actions beyond their realistic size. However, access to justice is greatly facilitated for persons who avoid interaction with the legal system, and most importantly, a more equitable proportion of the unjust enrichment would be extracted.

The OLRC solution to the option problem was to create a form of opt out scheme.[62] This is distinct from the traditional opt out concept, however, in that the right to exclusion from the class is within the discretion of the courts. This means, that irrespective of the members' individual desires, they may be bound by the action.

The factors the courts must take into account reflect this concern. They must consider all relevant matters, including: whether members of the class who exclude themselves would be affected by the judgment; whether the claims of the members of the class are so substantial as to justify independent litigation; and whether there is a likelihood that a significant number of members of the class would desire to exclude themselves.[63]

The proposal is of a pragmatic nature in that it seeks to avoid class members opting out and jeopardising the benefits than can be gained by bringing the action in class form. However, it is submitted that the proposal should not be followed in New Zealand. It promotes the punitive aspects of the procedure which, in the United States, has resulted in the class action being used somewhat as an oppressive device.

The foremost function of the procedure should be to provide a means by which parties can receive compensation for wrongs committed against them. The magnitude of the penalty brought against the defendant should reflect the actual degree of harm that individuals feel so motivated to act upon. This means that only an opt in proposal is capable of satisfying both parties' perceptions of justice, and should be the option that is followed.

61 Above n20, r 23(c)(2)(A).
62 Above n10, s 20.
63 Above n10, s 20(2)(a)-(e).

X. COSTS

The cost of litigating a class action claim can be a major deterrent to the pursuit of any such action. Costs to the representative plaintiff are almost invariably out of proportion to any potential benefit that may individually accrue from the action. This means that the potential benefits of the class action procedure will be eliminated unless there is some mechanism by which representative costs can be controlled. Three types of costs are pertinent to the discussion: legal costs; party and party costs; and the cost of notice.

A. *Legal Costs*

Legal costs are those costs incurred by the representative plaintiff for the services of legal representation. Due to the size and complexity of class actions, legal expenses tend to be very high. If the representative plaintiff is seeking only a small amount of damages, or is seeking non-monetary relief, it is often not economically sound to pursue the action. Most class actions will be impracticable if plaintiffs must bear their own legal costs.

However, certain solutions exist to overcome this cost burden, one of which operates in the United States and is responsible for inducing many court actions there. The potential solutions are: a form of legal aid; class contributions; and contingency fees. Each will be discussed below in turn.

In New Zealand, the Legal Aid Act 1969 restricts the granting the legal aid to "any person", but excludes "any other body of persons" from this term.[64] By definition, this would exclude a "class" from any aid. This has also been the opinion of the English case law, which has precluded classes from an English equivalent of this provision.[65]

Even if legal aid could be granted to a body of persons the strict financial tests imposed by the Legal Aid 1969 would preclude all but the most destitute plaintiffs.[66] Particularly in the context of securities laws, it is suggested that plaintiffs having shares in listed companies are unlikely to meet the tests for legal aid, yet the costs are such that even the most affluent shareholders would be reluctant to bring an action.

In Quebec, the legislature took the view that representative actions bring relief to a large number of people for whom the costs of bringing the action would outweigh the benefits.[67] Even though collectively a class could afford to pursue the action, the purpose of the class action reforms is to encourage litigation, a goal which would not be achieved purely through compulsory class contributions. The resulting system was one that provided a form of legal aid to the class, and extracted the value of the aid from any award subsequently made in its favour.

64 Legal Aid Act 1969, s 2.
65 *Wallersteiner* v *Moir (No 2)* [1975] 1 All ER 849, 866.
66 Above n64, s 17(1).
67 Above n1, 711.

It is submitted, however, that despite the need to facilitate access to justice, legal aid is never appropriate where the cumulative financial means of the body in question is sufficient to bear the cost burden. The use of the state to support actions in these circumstances involves an extensive free-rider effect at the cost of the taxpayer, and would also act as an incentive for classes to pursue unmeritorious claims. If classes with genuine claims wish to pursue the claims through class procedure, it would seem appropriate that the risk of financial investment in the action should fall on those parties who would receive the direct benefit of an award. Although there is an inherent social benefit that stems from the use of the procedure, it is submitted that this is a secondary benefit and should not be seen as a reason for the taxpayer to subsidise the direct beneficiaries.

The free-rider basis on which class members benefit without contribution to the costs of litigation is, it is submitted, a form of unjust enrichment inconsistent with principles of fairness. The most appropriate solution would be to extract the costs of the action *from the individual class members*. Although this would accord nicely with prevailing social notions of user pays, in practical terms it would have the effect of scaring off class members from participation in the action due to the potentially high costs involved in bringing an action in class form. However, this effect can also be seen as a benefit in that it acts as a mechanism to weed out non-viable claims and safeguards the defendant.

It is submitted that class contributions are the most equitable means of financing class actions, but they could also operate in conjunction with a form of limited contingency fee arrangement.

Contingency fees in the United States are a tool through which access to the courts is increased. Contingency fees involve a system of conditional payment. Lawyers conduct cases on the understanding that legal fees will be awarded *only* on the successful outcome of an action. However, many potential detriments and dangers are associated with their operation.

One significant problem was aptly stated by Buckley LJ in *Wallersteiner* v *Moir (No2)*:[68]

> Under a contingency fee agreement the remuneration payable by the client to his lawyer in the event of his success must be higher than it would be if the lawyer were entitled to be remunerated, win or lose; the contingency fee must contain an element of compensation for the risk of having done the work for nothing. It would, it seems to me, be unfair to the opponent of the contingency fee litigant if he were at risk of being ordered to pay higher costs to his opponent in the event of the latter's success in the action would be the case if there were no contingency fee agreement.

Contingency fees have also been criticized as encouraging a winning attitude to the sacrifice of legal ethics; promoting a conflict of interest between solicitor and client; and encouraging the solicitation of clients and stirring of litigation by solicitors. These

68 Above n65, 859.

undesirable outcomes were the reason for the laws of champerty and maintenance in England, which effectively prohibited contingent fees. Such fees are still not sanctioned by the New Zealand Law Society's Code of Ethics.[69]

The question now to be answered is whether the need for access to representative procedure outweighs the potential abuses of contingency fees. This was the question indirectly faced by the Court in *Wallersteiner*, a case involving a derivative claim. A majority of the Court held that in the case of a minority shareholders action, a contingency fee arrangement could not be justified. However, it was held that the plaintiff would be entitled to full indemnity for his costs from the company. Lord Denning, however, went on to exclude the possibility of a contingency fee system in a wider context on the basis of questionable public considerations.

This was not the view taken by the OLRC, which concluded that a representative plaintiff should have a right to enter into a contingency fee arrangement, and the amount of the fee would be a matter for determination by the courts. The agreement would be subject to strict statutory conditions:[70]

> (3) An agreement ... shall not stipulate the amount of the payment either by a gross sum, commission, percentage, salary or otherwise, and any such stipulation is void.
>
> (4) Where the representative plaintiff and his solicitor have made an agreement ... the court that has given judgment on the common questions or has approved a settlement shall ....
>
> (a) determine the amount of the solicitor's fees and, in addition thereto, an amount that is fair and reasonable compensation to the solicitor for the risk incurred by him in undertaking the action on a basis of payment only in the event of success ....

This proposal would effectively control the problem of excessive fee setting by solicitors (such as a percentage of the award), but does not expressly deal with other problems such as solicitation of clients and conflicts of interest. It is submitted, however, that the benefits of contingency fee arrangements far outweigh these more minor problems. They not only facilitate greater access to justice, but they do so by levying the cost of such access on the parties to whom the benefits of a successful action will accrue (that is, the solicitor and the class). They also provide an effective device to ensure only viable claims are pursued, due to the potential cost detriment to the solicitor for a loss in the courtroom. The remaining ethical complications of contingency fees are questions which the legal profession itself should turn its mind to, and should not stand in the way of increased access to justice.

B. *Party and Party Costs*

Party and party costs ("party costs") refer to the legal fees and other costs of the successful party. The award of party costs against an unsuccessful litigant reflects the

69 New Zealand Law Society *Code of Ethics* para 6.21.
70 Above n10, s 43.

need to compensate the successful litigant for the burden of bringing or defending an action.

In New Zealand, the awarding of party costs is totally within the discretion of the courts.[71] As a general rule, costs will follow the event, meaning an award for the costs of the successful party will be made against the unsuccessful party.[72]

As with legal costs, this potential consequence has a weeding out effect on actions. As the class is not bound to contribute to any party cost award against the representative plaintiff (as they are not parties to the action), it is unlikely that many representative plaintiffs could be found to bring anything but the most cut-and-dry actions. This raises the question of whether some form of control on party costs is appropriate in order to greater promote the use of the procedure.

The OLRC favoured the United States practice of not awarding party costs.[73] The proposal varied from the United States model though by giving the courts a discretion to award costs when it would be unjust not to, and in the event of vexatious, frivolous or abusive conduct.

It is submitted that neither the United States rule nor the OLRC proposal is desirable for a New Zealand proposal. The concept behind party costs is that if a disputant chooses to test the claim or defence of another disputant, then he or she must accept the cost of forcing that other party to prove the correctness of his or her assertion. This concept is equally valid in the context of class actions, perhaps even more so considering the large costs required to contest such claims.

It is suggested that the existing New Zealand party costs provision is suitable for a New Zealand class action proposal. Under the present rules, if it appeared that justice would not be well served by the award of party costs a court could simply decline to make any award. This flexibility allows both the underlying concept and the interests of justice to be served.

By avoiding any sheltering of the representative plaintiff from the burden of costs the class is also forced to confront the question of whether to make an undertaking to protect the plaintiff against any award. In reality, such an undertaking would necessarily be required before an action could proceed. By forcing the class to make such a commitment, the potential costs of the action is appropriately spread over all those who seek to benefit from its success.

C. *Costs of Notice*

Although, like legal costs, a successful party can have the cost of providing notice to class members awarded in his or her favour, difficulty arises from the enormous

71 Rule 46.

72 Rule 47; *Poverty Bay Electric Power Board* v *Attorney-General* unreported, 5 November 1987, Wellington High Court, CP552/87, Davison C J.

73 Above n10, s 41.

initial outlay that may be required by the representative plaintiff. The problem is somewhat lessened if the class has undertaken to bear the cost of the action. The question remains, however, whether there should be provision to defer or avoid the enormity of the outlay that may be required of the class (or alternatively, the plaintiff) until the action has been resolved.

The OLRC met part of the cost problem by giving the courts a discretion as to the means of notification. This means the courts may, in certain circumstances, approve a form of notice less expensive than individual communication.[74] The OLRC did not, however, address the more fundamental question of who is to meet the initial outlay of the notice expense, whatever form the notice may take. The presumption would be that this initial cost falls on the plaintiff.[75]

A possible solution would be to give the courts power to apportion the cost of notice between the parties. This was adopted by the OLRC in its proposal on the cost of general notice.[76] The discretion would be likely to take the form of the preliminary test that was first suggested by United States case law, involving an examination of the merits of the case and an order favouring the class plaintiff if it appeared there was a reasonable likelihood that the issues would be resolved in favour of the class.[77]

It is submitted that this does not serve the interests of fairness. The defendant should not be burdened with any costs of the other party until the case has been fully heard and the defendant has had his or her opportunity to test the claims of the class. As with other costs questions, the immediate onus connected to the specific use of class action procedure should fall on the party seeking to gain the benefit from the use of the procedure.

XI. CONCLUSION

The current class action procedure available in New Zealand is in need of legislative reform. Considerable benefits can be achieved from a widely accessible procedure, one of the more important being the vindication of the rights of large groups of wronged individuals whose individual claims are untenable. Such a vindication creates accountability for wrongdoers, and forces the cost internalisation of unjust enrichments. Such benefits could be more readily achieved through a redrafting of rule 78 to eliminate some of the disincentives to bringing actions in class form.

A New Zealand provision should attempt to crystallise the developments in the damages and common interest area which have been recognised in the recent *R J Flowers*

74 Above n10, s 16(3).

75 This presumption is based on the OLRC proposal that the cost of "general" notice (see above n10, s 18(4)) may be apportioned between the parties at the discretion of the court. Without such a specific indication to the contrary it can be presumed the cost of other forms of notice would naturally lie only with the plaintiff.

76 Above n10, s 18(4).

77 It should be noted, however, that this test was rejected by the United States Supreme Court in *Eisen* v *Carlisle and Jacquelin*, above n59.

case,[78] and which reflect the current trend of authorities emerging from England and Canada. The United States practice of estimated damages should be followed to the limited extent approved by the OLRC by giving the courts liberal control over the conduct of the action. A cautious eye would have to be kept on the development of the estimated damage concept to avoid an insidious slide towards some of the United States excesses.

The OLRC proposals on the other major issues provide an appropriate structure from within which to work reforms appropriate to the New Zealand context. A general theme running through the proposals seems to be to avoid placing any financial responsibility on the class in respect of the costs faced by the plaintiff. This theme should be rejected in favour of a self help or user pays ethic, which would ensure that those who were to receive the benefit of an action fully contributed to any gains that were to be made.

Class action procedure will increase in significance in New Zealand in the next few years as reforms continue overseas and New Zealanders become more aware of the possible ways to enforce their rights. The attempted use of the device is likely to become more prevalent, especially in the context of creditors and shareholders' actions where the economic downturn of the past year has created much corporate instability. This change in social need for a representative device should be taken as an incentive to precipitate movements towards legislative reform in this country.

78 Above n44.

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