

OPENING OF LAW TERM DINNER, 2009
THE LAW SOCIETY OF NEW SOUTH WALES
ADDRESS BY THE HONOURABLE J J SPIGELMAN AC
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In August last year, the third Corporations Law Conference organised jointly by the Supreme Court and the Law Society was held on the topic of “The Credit Crunch and the Law”. It is difficult to imagine a conference theme that was more timely. As the universal response to the quality of the papers presented at that conference attests, the Conference made a significant contribution to the understanding of the profession in this State, and beyond, to the range of important corporations law issues that have arisen as a result of the global economic downturn.

In April last, the Supreme Court initiated the first Asian Judicial Seminar on Commercial Litigation. It was attended by senior commercial judges from China, India, Japan, South Korea, Singapore, Hong Kong, The Philippines, Malaysia and Papua New Guinea. I am pleased to say that the Seminar was such a success that it will be repeated in Hong Kong next year, again to be jointly

organised by the High Court of Hong Kong and the Supreme Court of New South Wales.

I circulated the published papers of our Credit Crunch Conference to the attendees at that Commercial Seminar. They universally expressed their admiration for the publication. We have begun planning for next year's joint Supreme Court/Law Society Conference and I have no doubt it will be equally well received, both in Australia and beyond.

This downturn of the economic cycle is of such prospective severity that, on this annual occasion, I wish to address my remarks to the implications of this global development for the legal profession.

Our focus must be on the quality and efficacy of the services that the legal profession will be called upon to provide for the resolution of the disputes that necessarily arise in such a context. The downturn is already having an effect on the flow of litigation.

Proceedings instituted in the Supreme Court to enforce obligations under mortgages reflect the economic stress of the

times. Our monthly figures for matters entered into the Court's Possession List are sought as an economic indicator by the Reserve Bank of Australia. The Governor of the Bank has told me that the Bank appreciates our cooperation in this regard.

The major increase in Possession List filings occurred in 2005 and 2006 i.e. before the current nationwide downturn. In 2007 and 2008 they plateaued. (See Annexure.) Analysis of the figures indicates that in the first six months of 2008 there was a decline of some 11 percent in Possession List filings (2519), when compared with filings for the first six months of 2007 (2834). However, the second six months of 2008 were completely different: filings (2953) were up by 13 percent on the previous corresponding period (2620). Although overall, on an annual basis, there was no increase, it does appear from the figures for the second six months that difficulties are emerging and they are emerging notwithstanding the substantial decline in interest rates that occurred during that period.

One of the reasons why what has come to be known as sub prime mortgages – which we used to call “low-doc loans” – never reached the dimensions that they have overseas is because of the

particular legal regulation available in this State. The Supreme Court of New South Wales has on numerous occasions exercised the powers conferred upon it under the *Contracts Review Act* to set aside as “unjust” aspects of low-doc loans where a mortgage, often by an elderly person over the family home, had been advanced without any consideration of the capacity of the borrower to repay.

One of the foundational judgments of this character,¹ frequently applied subsequently, led to significant change in the practice of lenders with respect to controlling their brokers who originated such loans. As the *Financial Review* reported under the heading “Court ruling forces overhaul of low-doc lending”, the judgment led to warnings to members by the Mortgage Industry Association of Australia and to a change of practice by what was described as a \$5 billion mortgage finance company owned by major banks with respect to its brokers, leading to some 20% of the brokers being removed from their panel.²

This line of authority has received considerable publicity in the financial media leading to another article in the *Australian Financial Review* which said:

“Public awareness about the plight of families caught in the debt trap through low-doc lenders is only starting to emerge as consumer groups raise their concerns. But judges in NSW have been on to it for several years. As the number of mortgage defaults escalates, courts have closely examined the conduct of loan intermediaries in the low-doc industry – solicitors, accountants and brokers – and made a number of critical findings. Judges are increasingly prepared to look at the circumstances behind the loan documentation ...”³

I think it likely that the regulatory regime as enforced in this State has played a role in limiting the exposure of Australian banks and other lenders in the manner which has proven to be so disastrous elsewhere.

The second area of the Court’s jurisdiction which will reflect economic conditions to a significant degree are filings for insolvency. Statistics on these matters are kept for Australia by ASIC and reveal an interesting comparison between this State and other States.

In New South Wales the number of companies entering external administration for the first time were up by 11 percent from 2007. However, the national average was up by 21 percent. This was because of a 27 percent increase in Victoria, a 40 percent increase in Queensland, a 20 percent increase in South Australia and a 43 percent increase in Western Australia.

It does appear that in 2008 stress in the corporate community was greater in other States than in New South Wales. This State may have been affected by adverse conditions before other States, but the effects of last year's global credit crunch has not yet impacted quite as significantly here as in other States.

I wish to emphasise the long-term significance of the global shift in the economic tectonic plates which will lead inexorably to social tremors and quakes. These effects will test many aspects of our social infrastructure, including our legal infrastructure.

As many of you are aware, from the time of my swearing-in speech in May 1998, I have consistently emphasised the significance of the professional dimension of legal practice and, in

particular, the need to resist recasting the profession solely in terms of its commercial dimension. My swearing-in speech has recently been reprinted as the opening chapter of the collection of my speeches, of which the Law Society sponsored the launch by the recently retired Senior Law Lord, Lord Bingham. Please accept my gratitude for the support the Society gave on that occasion.

It is appropriate to reiterate some of the themes I raised at my swearing-in and which I have consistently repeated in the decade since. The salience of commercial values in discourse about legal practice, which threatened to overwhelm all other values, is now in secular retreat. We will, I believe, as a direct result of the extraordinary events we are now experiencing, re-emphasise the central significance of the professional dimension of legal practice.

Permit me to commit the sin of self-quotation and repeat some observations from my swearing-in speech:

“The independence and integrity of the legal profession, with professional standards and

professional means of enforcement, is of institutional significance in our society. ...

The ideology of the free market forces, which I do not doubt has a significant and appropriate role in many spheres of discourse, has been elevated by some to a universally applicable orthodoxy. It should not be accepted to be such.

Economic rationalism has its place. In the administration of justice that place is a limited and subsidiary one. A plurality of organising principles for our social institutions is as important to the health of our society as biodiversity is to our ecology.”⁴

In subsequent addresses I elaborated on that last proposition by emphasising that a society which adopts a single organising principle for its basic institutions is inherently unstable. That is why I adopted the analogy of biological diversity.

In every sphere of discourse, including the law, the end of an era which treated commercial values as of overriding significance will lead to the reassertion of more traditional values.

It is a tribute to the strength of the traditions of our profession that so few chose to abandon, or to significantly qualify, those traditions in accordance with the values of the era that has now passed. Multi-disciplinary partnerships have not become significant. Incorporation has not become the norm. Only one or two firms have taken the ultimate step of listing on the Stock Exchange. Furthermore, the large firms definitively asserted their connection with the profession. A special constitutional provision was adopted at the level of the Law Council of Australia and those firms continued their involvement with the State Law Societies. This is symbolised notably by you, Mr Cantanzariti, in your many years of involvement on the Executive culminating in your ascendancy to the presidency of this Society.

As many of you will recall, a few years ago, in an insightful address on the subject of “Lawyers and Money”,⁵ Brett Walker SC raised the possibility that the major commercial law firms should, in effect, leave the profession and join their business clients. Now, of

course, the idea that law firms should reinvent themselves as merchant banks would not be high on anyone's agenda.

At the time of the last recession, following the economic boom of the 1980s, my corporate law practice turned into a criminal practice. I was briefed by the Australian Securities Commission, as ASIC then was, and the Commonwealth Director of Public Prosecutions, to pursue criminal charges against a number of accused, including Laurie Connell in Western Australia. I remember a delightful exhibit that had been tendered at the Royal Commission into what became known as "WA Inc". It was a tombstone ad that read:

"ROTHWELLS LIMITED

ONE DAY ALL MERCHANT BANKS WILL BE LIKE OURS."

And so it has proved.

Reassertion of the conduct of a profession as the basic paradigm for the practice of law, rather than the adoption of a business paradigm, will be an important structural effect of the present crisis.⁶ The business paradigm regards the lawyer/client relationship as primarily a commercial relationship. The

professional paradigm emphasises that the lawyer/client relationship is a personal bond created in the context of a high degree of personal responsibility, with an overriding ethic of service to clients and to the public. There will now be renewed emphasis on the moral code that underpins the traditional authority of our profession, so that that ethic of service, which emphasises honesty, fidelity, diligence and professional self-restraint, will now resume its salience over the pursuit of commercial gain at the core of legal practice. In this our profession will reflect changes that affect all other professions.

The second matter to which I wish to refer this evening is closely related to the reassertion of professional values. As this audience is well aware, I have over a number of years emphasised the need to control legal costs. As I have said on previous occasions, the legal profession is in danger of killing the goose.

Economic adversity will increase cost consciousness at all levels and the profession must be prepared to respond to the demands of its clients and of the public at large in this respect. Unless the profession recognises that the period of economic

adversity we are entering requires a significant reduction in the cost of legal services it will be marginalised.

When, five years ago, major reforms were instituted to change the culture of personal injury litigation, they were driven to a substantial degree by the significant proportion of damages awards that were taken up by the costs of administering the system. No one should assume that there is any sphere of legal practice that is immune from similar intervention.

There are signs that other areas of practice are already being affected by the need to minimise costs. Even one of the few growth areas – corporate insolvency – will be more cost conscious. It is noticeable that in the case of some of the biggest examples of corporate stress – Centro, Allco, Babcock and Brown – major creditors who trust the existing management are letting them liquidate the assets rather than appointing receivers or liquidators with the additional level of costs and delays, including legal costs, that appear to be endemic with external administration.

The warning signs are clear.

Over the last decade or two substantial progress has been made in reducing delays in the courts and some progress has been made in controlling costs. However, we must continually re-engineer the process of dispute resolution because the pressures on the process are in a continual state of flux. The scope and speed of changes in the economy and in society, which the law is designed to serve, will never permit us to declare victory and sit back content. We must proceed on the basis that there is always scope for improvement. The period of economic adversity which we are entering makes this constant endeavour more pressing than it has been in recent decades.

Judges are able to contribute to the process of controlling legal costs, especially in terms of delay and length of trial. However, there are limits to the degree of supervision and intervention which are consistent with the continuation of an adversary system. Although that system has been modified in many respects, it remains the case that the principal role in controlling costs lies with the profession.

I recognise of course that there may be a perception of a conflict of interest in this respect. What a client regards as costs, a

lawyer, in large measure, regards as income. It is here that the re-emergence of a professional paradigm over a business paradigm for legal practice is of potentially great significance. Recognition of the centrality of the ethic of service for our profession is the most effective means to ensure that this conflict of interest is satisfactorily resolved.

The judiciary and the profession have to co-operate to ensure that all of the areas in which costs can escalate unreasonably, areas that have been well identified over the years, are controlled even more strictly than we have come to do in the past.⁷ That is not only in the public interest, it is in the enlightened self-interest of all legal practitioners. If the profession is too greedy it will end up with less and, in some fields, with nothing.

This requires careful attention to the matters of which we are all aware such as:

- Minimising the number of times matters are brought before the Court by maximising agreement on procedural and evidentiary matters that would otherwise involve interlocutory motions and attendances, together with the more extensive use of telephone and electronic directions hearings;

- Minimising the length of trials by exercising professional judgment as to what the chances of success on particular points of evidence and law are, and abandoning those in which the chances are low;
- Maximising co-operation on expert evidence to reduce the scope of disputation, recognising that a biased expert does your client harm.
- Further and more extensive use of the Supreme Court's practice in commercial disputes of a chess clock or stopwatch system for trials so that litigants have a higher degree of certainty about their costs exposure;
- Focussing the issues so that extensive discovery is not required and recognising that the faint hope that a smoking gun may exist to revive a weak case is simply not worth the costs involved;
- Applying with renewed vigour the test of proportionality, expressed in s60 of the *Civil Procedure Act* 2005, to the

effect that costs to the parties of dispute resolution must be proportionate to the importance and complexity of the subject matter in dispute.

Primarily through its series of committees involving the profession, on which the representatives of the Law Society serve, the Court has well-established mechanisms for ensuring that its practices remain responsive to the changing needs and concerns of legal practice. The Court remains open to changing its structures and practices in accordance with the ideas thrown up in these consultations.

The Court has a range of powers that are now almost a decade old and which more recent legislative reform in other jurisdictions has by and large replicated. Similarly, we have a series of specialist lists which ensure judges of particular skill and experience deal with particular cases, including in commercial matters for the best part of three decades and in corporations matters for about a decade. The use of ADR has long been encouraged, and for over two decades, we have successfully operated a system of external referees.

The Court is determined to ensure that the costs of legal proceedings are minimised. It remains ready and willing to continue to pursue changes in our practices in consultation with the profession.

In one area, in my opinion, legislation is required. The focus on commercial arbitration as a form of commercial dispute resolution has always offered, but rarely delivered, a more cost effective mode of resolution of disputes. Our uniform legislative scheme for domestic arbitration is now hopelessly out of date and requires a complete rewrite. The national scheme implemented in 1984 has not been adjusted in accordance with changes in international best practice. Of course, in our federation, agreement on technical matters such as this in multiple jurisdictions is always subject to delay. The delay with respect to the reform of the Commercial Arbitration Acts is now embarrassing. This is not an area in which harmonisation based on the lowest common denominator principle is appropriate.

In my opinion, the way out of the impasse is to adopt the UNCITRAL Model Law as the domestic Australian arbitration law. It is a workable regime, itself now subject to review at the

Commonwealth level. Its adoption as the domestic Australian arbitration law would send a clear signal to the international commercial arbitration community that Australia is serious about a role as a centre for international arbitration. Our competitors in this regard, such as Hong Kong or Singapore, do not create a rigid barrier between their domestic and international arbitration systems. Nor should we.

It is of course difficult to predict the future development of the current economic crisis. Nevertheless its implications will clearly be profound. In the short term one can expect a significant increase in commercial litigation, but the scope and intensity of the current downturn is such that this may prove to be short-lived, as more and more parties realise they are in no position to undertake the costs and risks of full litigation. As a profession it is our collective duty to minimise this barrier to access to justice. Lawyers are not immune to the effects of such a development. Many of you will already be feeling the pain. All of you will be apprehensive. The ethic of service obliges us to respond despite the commercial pain that practitioners will inevitably suffer during this period.

The one thing we cannot do is to rely on the traditional lawyer's instinct that nothing must ever be done for the first time.

Giuseppe di Lampedusa, in his great novel, *The Leopard*, crafted these words for a perceptive aristocrat facing the oblivion of the Sicilian aristocracy: "If you want things to stay the same, you have to change."

Not all societies or social groups prove capable of changing their practices, often with disastrous results. As Jared Diamond noted in his book *Collapse: How Societies Choose to Fail or Succeed*,⁸ a form of intellectual paralysis may emerge which leads to doom. What, he legitimately asked, was in the mind of the Easter Islander, when he chopped down the last tree on that island upon which the whole society had long depended? A similar question could be asked of some legal practitioners. It is our mutual task to ensure that we avoid this state.

¹ *Perpetual Trustee Co Limited v Khoshaba* [2006] NSWCA 41.

² See "Court ruling forces overhaul of low-doc lending" *Australian Financial Review* 20 December 2006 p 1.

³ See "Buyer beware: Home truths about low-doc loans" *Australian Financial Review*, 10 August 2007 pp84-85; see also "Buyer beware? Now its seller play fair" *Australian Financial Review*, 20 December 2006 p4.

⁴ See (1998) 44 NSWLR xxvii, reprinted in Tim D Castle *Speeches of a Chief Justice: James Spigelman 1998-2008*, Sydney, 2008 p 3.

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- ⁵ See “Lawyers and Money” (2005) *Lawyers Lectures*, St James Ethics Centre, 24 October 2005 accessible at www.ethics.org.au.
- ⁶ For discussion of these matters see my address “Are Lawyers Lemons? Competition Principles and Professional Regulation” (2003) 77 *Australian Law Journal* 44 reprinted in Tim D Castle (ed) *Speeches of a Chief Justice: James Spigelman 1998-2008*, Sydney, 2008 at p138.
- ⁷ See generally my address “Access to Justice and Access to Lawyers” (2007) 29 *Australian Bar Review* 136; (2007) 14 *Australian Journal of Admin Law* 158.
- ⁸ Diamond J, *Collapse: How Societies Choose to Fail or Succeed* (Viking, New York, 2004).

Companies entering external administration – number and per cent from each state and territory

	NSW	Vic	Qld	SA	WA	Tas	NT	ACT	Total
2007	3764	1945	1103	269	275	43	15	107	7521
(% of Aust total)	(50%)	(26%)	(15%)	(4%)	(4%)	(1%)	(0%)	(1%)	
2008	4172	2472	1541	322	393	44	24	145	9113
(% of Aust total)	(46%)	(27%)	(17%)	(4%)	(4%)	(0%)	(0%)	(2%)	
% change within state/territory from 2007 to 2008	up 11%	up 27%	up 40%	up 20%	up 43%	up 2%	up 60%	up 36%	up 21%

These statistics show the number of companies entering administration for the FIRST time, based on documents lodged with ASIC in the given period. A company is only included in the statistics ONCE, regardless of whether it enters another form of external administration. The only exception occurs where a company is taken out of external administration, eg by a court order, and at a later date re-enters external administration. Voluntary windings up are EXCLUDED.

Insolvency appointments in Australia – number and per cent from each state and territory

	NSW	Vic	Qld	SA	WA	Tas	NT	ACT	Total
2007	5691	2986	2076	475	490	81	36	183	12018
(% of Aust total)	(47%)	(25%)	(17%)	(4%)	(4%)	(1%)	(0%)	(2%)	
2008	6287	3831	2553	525	648	69	30	230	14173
(% of Aust total)	(44%)	(27%)	(18%)	(4%)	(5%)	(0%)	(0%)	(2%)	
% change within state/territory from 2007 to 2008	up 10%	up 28%	up 23%	up 11%	up 32%	down 15%	down 17%	up 26%	up 18%

This is the number of insolvency appointments recorded by ASIC. As a company can be under more than one form of insolvency administration at any one time and can progress from one type to another, a company can be included in these statistics MORE THAN ONCE. For this reason, the number of insolvency appointments will always be greater than the number of companies going into external administration for the first time. Voluntary windings up are EXCLUDED.

Source: Australian Securities and Investments Commission – figures available as at 2 February 2009.