EU Recommendation

COLLECTIVE REDRESS: REPRESENTATIVE AND CLASS ACTIONS

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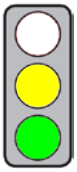
Centrum für Europäische Politik

KEY ISSUES

Objective of the Recommendation: The Commission recommends that the Member States introduce collective actions.

Parties affected: Companies and citizens, consumer associations and other associations.



Pro: (1) Collective actions allow legitimate claims to be brought more easily.

(2) The Commission is trying to achieve a balance between protecting the interests of potential claimants and the need for companies and society as a whole to prevent abusive litigation.

Contra: (1) The option for Member States to use the opt-out principle for reasons of "sound administration of justice" gives rise to legal uncertainty.

(2) The recommended binding effect upon the courts of decisions by authorities results in a curtailment of the legal process if affected parties cannot take action against the decisions of authorities.

CONTENT

Title

Commission Recommendation 2013/396/EU of 11 June 2013 on common principles for **injunctive and compensatory collective redress** mechanisms in the Member States concerning violations of rights granted under Union Law

Brief Summary

- **Context and objectives**
  - The Commission recommends that the Member States introduce collective redress mechanisms ("collective actions", No. 2). The Recommendation contains non-binding, EU-wide uniform principles to that effect.
  - "Collective actions" are actions before a national court in which [No. 3 (a) and (d)]
    - two or more affected parties claim together (class actions - referred to as "group actions" by the Commission) or
    - an authority or entity claims on behalf of two or more affected parties ("representative action").
  - Collective actions will be possible in the form of [No. 2, 3 (a)]
    - compensatory claims, where two or more affected parties have suffered harm resulting from the same illegal practices of a company ["mass harm situation", No. 3 (b)] and
    - injunctive claims, where two or more affected parties can apply to stop a company's illegal practices.
  - The principles set out in the Recommendation will
    - facilitate the enforcement of legal rights ("access to justice"), particularly where individual actions are too costly for affected parties (No. 1, Recitals 1 and 9), and
    - prevent abusive litigation (No. 1); abusive litigation exists where a claimant brings unfounded claims against law-abiding companies in order to [Communication COM(2013) 401, page 7 et seq.]
      - cause damage to the company, particularly reputational or financial, or
      - obtain undue compensation by speculating on a settlement, which the company will be more willing to conclude in the case of a collective action in order to ward off damage to its reputation.
  - Member States are to implement the Recommendation by 26 July 2015 (No. 38). The Commission wants to assess whether "further measures" should be taken to "strengthen the horizontal approach reflected in the Recommendation" by 26 July 2017 (No. 41).
- **Area of application**
  - Collective actions should be available in those areas of law in which citizens and companies are granted rights under EU law (No. 1). That means, in particular, the areas of consumer protection, competition, environment protection, protection of personal data, financial services and investor protection (Recital 7).
  - In some areas of consumer protection, e.g. consumer contracts, EU-wide collective injunctive redress already exists (Directive 2009/22/EC).
- **Legal standing**
  - In the case of class actions, those with legal standing are (Recital 17, No. 17)
    - national groups of claimants and
    - in cross-border cases, groups of claimants from other Member States.

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– In the case of representative actions – depending on the stipulation of the individual Member State – those with legal standing are
  - national authorities which have been recognised as having legal standing by their Member State (No. 7),
  - entities generally recognised as having legal standing by a Member State ("representative entities", No. 6, 18) and/or
  - entities which have been recognised as having legal standing on an "ad hoc basis" for a particular action by the national authorities or courts of a Member State in which the action is to take place (No. 6).
– In order to be recognised as a representative entity, the entity should (No. 4)
  - be non-profit making,
  - pursue objectives with a direct relationship to the rights claimed to have been violated and
  - have sufficient financial and human resources as well as legal expertise.

► **Information on the actions**
– Groups of claimants and representative entities should inform affected parties about (No. 10)
  - the mass harm situation or the illegal practices of the company,
  - their intention to claim compensatory or injunctive relief, and
  - on-going compensatory actions.
– Affected parties should also be informed of on-going compensatory claims by the authorities and by entities that have been recognised as having legal standing on an "ad hoc" basis (No. 10).
– In disseminating information, e.g. via the media, the Defendant's right to the protection of its reputation and company value should be taken into account [No. 11, Communication COM(2013) 401, p. 12].
– Member States are to establish coordinated national registries (No. 35– 37)
  - in which the individual collective actions are recorded and
  - which are available to interested persons free of charge.

► **Financing the action and lawyers' fees**
– The party that loses the legal dispute should bear the legal costs of the winning party (No. 13).
– The claimant should disclose to the court its source of funds that it is going to use to finance the action (No. 14).
– A third party that is not the claimant or defendant should only be allowed to bear the claimant's legal costs if
  - it has sufficient resources to cover not only the claimant's costs but also, if necessary, those of the defendant (No. 15) and
  - there is no conflict of interest between the third party and the claimant (No. 15) and
  - it is not a competitor of the defendant (No. 16) and
  - it is not dependant on the defendant's funds (No. 16).
– A private third party that bears the claimant's legal costs should not
  - influence the procedural decisions of the claimant (No. 16),
  - charge "excessive" interest on the funds provided (No. 16) or
  - in the case of compensatory claims, base remuneration for funding on the amount of compensation awarded unless such funding is approved by a public authority (No. 32).
– In the case of compensatory claims, lawyers' fees should not create any incentive for lawyers to bring "unnecessary" actions. In particular, Member States can only permit contingency fees if the national regulation of those fees takes account of the affected party's right "to full compensation" (No. 29 and 30).

► **Compensatory claims: opt-in principle and limitation of compensation**
– In principle, it is the case that: affected parties may (only) take part in compensatory claims where they have given express consent and they may give or withdraw their consent at any time until the case has come to an end (opt-in principle, No. 21– 23).
– There is an exception to this where the Member State provides, by law or court order, "for reasons of sound administration of justice" (No. 21): that affected parties are automatically party to a compensatory claim provided they do not expressly object [opt-out principle, Communication COM(2013) 401, p. 11].
– The compensation which the individual affected party receives should not be higher (No. 31)
  - than that which it would have received if the affected party had pursued an individual action and
  - than that which is necessary to compensate for the loss suffered (prohibition of punitive damages).

► **Compensatory claims: relationship to other proceedings**
– Any administrative proceedings relating to the same illegal practices by a company should have been concluded prior to commencement of a compensatory claim. Where the claim has already been initiated, the court should not give a decision which would conflict with a decision contemplated by the public authority (No. 33).
– Extra-judicial dispute resolution proceedings should be available to the parties alongside the compensatory claim at all times (No. 25 and 26).
  - They should only be used with the consent of the parties (No. 26).
  - If the outcome of a settlement is to be binding, a court must verify its legality (No. 28).

- **Additional regulations for the prevention of abusive litigation**
  - The court should verify at an early stage whether the claim is admissible and not "manifestly unfounded" (No. 8).
  - Member States should avoid "intrusive pre-trial discovery procedures" (Recital 15); these involve an order by a judge, before the start of the trial, for the defendant to provide all relevant documents.

Statement on Subsidiarity by the Commission

The existing collective actions vary widely between the Member States (Recital 12). This can result in citizens being unable to assert their rights [COM(2013) 401, p. 5 and SEC(2011) 173, p. 4].

Policy Context

In 2005, the Commission published a Green Paper [COM(2005) 672] and in 2008 a White Paper [COM(2008) 165, see cep**PolicyBrief**] and a Green Paper [COM(2008) 794, see cep**PolicyBrief**] containing ideas on collective actions. In 2011 it carried out a consultation [SEC(2011) 173]. In 2012, the European Parliament welcomed the creation of a uniform EU concept on collective redress [2011/2089(INI)]. Along with the Recommendation, the Commission also presented a proposal on actions for damages under competition law [COM(2013) 404, see cep**PolicyBrief**].

Options for Influencing the Political Process

Directorates General:	DG Justice, DG Health and Consumers, DG Competition
Federal Ministries:	Federal Ministry of Justice (leading)

ASSESSMENT

Economic Impact Assessment

Ordoliberal Assessment

On the one hand, **because the affected parties can share the cost and the time involved, collective actions can facilitate claims for damages** which, though small for each individual affected party, are substantial when added together. This strengthens society's confidence in the legal system and deters potential wrongdoers. On the other hand, collective actions can lead to abusive litigation. Firstly, abusive litigation increases costs for companies and thus also consumer prices. Secondly, companies become overcautious and refrain from e.g. developing new products because they fear legal action even where they are acting lawfully.

In its Recommendation, **the Commission is trying to achieve a balance between protecting the interests of potential claimants and the need for both companies and society as a whole to prevent abusive litigation.**

The option for Member States, in the case of representative actions, **only to grant legal standing to authorities and/or certain entities, reduces the danger of abusive litigation** which is aimed at obtaining undue compensation or at damaging companies, because authorities a priori do not pursue such aims. In addition, the requirements that an entity has to fulfil in order to be recognised as a representative organisation with legal standing, reduces the danger of its pursuing such aims: the requirement that it should be non-profit-making reduces the danger of abusive litigation aimed at obtaining undue compensation, and the requirement that the entity must pursue objectives which relate to the action reduces the danger of abusive litigation aimed at damaging companies.

Due to the increased risk to the claimant, **the obligation for the losing party to bear the legal costs also reduces the danger of abusive litigation** aimed at obtaining undue compensation.

The fact that a third party can, in principle, bear the claimant's legal costs may, in certain cases, be the only way for a representative organisation to finance a collective action at all. However, there is the danger, on the one hand, that third-party fund providers will finance unfounded claims for purely financial reasons by speculating on the claimant obtaining undue compensation from a settlement. This danger has been reduced by limiting the remuneration and interest payable to third-party fund providers but it has not been ruled out. On the other hand, there is also the danger that persons with their own interests, e.g. competitors, will emerge as third-party fund providers in order to damage the company. This danger is reduced by the requirement that competitive relationships and dependencies between the third-party fund provider and the defendant are to be prohibited.

The principle that contingency fees must take account of the right of the affected parties to receive full compensation, in conjunction with the ban on excessive compensation, acts as **a limitation on lawyers' fees**. This **reduces the incentive for lawyers to bring unfounded claims** for purely financial reasons.

The opt-in principle reduces the incentive for lawyers and third-party fund providers to bring or finance unfounded claims purely for financial reasons: since affected parties have to actively decide to join an action, the group of claimants is generally smaller than is the case under the opt-out principle. Thus the value of the dispute, on which lawyers' fees and court costs are based, is also lower which in turn reduces the profits available to lawyers and third-party fund providers. The opt-in principle also secures individual freedom of choice because affected parties choose to take part in an action the result of which will be binding on them.

The option for Member States to use the opt-out principle for reasons of "sound administration of

justice" carries with it the danger that this wording will be given a broad interpretation. Thus **gives rise to legal uncertainty.**

Impact on Europe as Business Location

Collective actions increase costs for companies that have their registered office or branches in the EU. Companies with their registered office outside the EU can only be sued outside the EU where collective actions are not always available. Relocations may take place in order to avoid collective actions in the EU. This will change when the new Brussels I Regulation [Regulation (EU) No. 1215/2012] comes into effect on 10 January 2015. Consumers will then also be able to sue companies, whose registered office is outside the EU, in their home EU country.

Legal Assessment

Legislative competence

The Commission is empowered to adopt Recommendations (Art. 292, sentence 4 TFEU). **Since Recommendations have no binding force** (Art. 288 TFEU) the Member States decide whether and how to implement them. **A substantive competence is** therefore **not required.**
Different rules apply to a legislative act: the Commission wants to facilitate the enforcement of legal rights – it talks about "access to justice". In that case, substantive competence can only be based on judicial cooperation in civil matters with cross-border implications [Art. 81 (2) (e) and (f) TFEU]. This only applies to civil matters with cross-border implications, however. The principles of the Recommendation which do also relate to purely national civil matters therefore do not fall under this substantive competence.

Impact on German Law

If Germany is to implement the Recommendation it will have to modify its law on civil procedure. Claimants can already bring joint claims as joined parties (Section 59 Code of Civil Procedure, ZPO) which are similar to collective actions. Existing entities such as consumer associations can claim, in particular, where consumer claims are assigned to them [Section 79 (2), sentence 2, No. 3 ZPO] or in order to stop or remedy breaches of duty [Section 8 Act against Unfair Competition, UWG in conjunction with Sections 1 to 3 Act on Action for an Injunction, UKlaG]. In addition, the claimant has not previously had to disclose its source of funds to finance the claim nor are there any restrictions on third-party fund providers. Under German law, **courts are not bound by the decisions of authorities** and can therefore contradict them. **The recommended binding effect** whereby the courts should not overrule the decisions of public authorities in the same matter, also outside competition law - and even decisions which are only being contemplated - is problematic: it **results in a curtailment of the legal process if affected parties cannot take action against the decisions of authorities.** There is already binding effect under competition law. This serves to protect the affected parties, however, because they no longer have to prove, in court proceedings, that there is a breach of competition law if it has been ascertained by an authority [Section 33 (4) Act against Restraints of Competition, GWB in conjunction with Section 16 Regulation (EC) No. 1/2003]. The binding effect should therefore be expressly restricted to competition law.

Possible Follow-up Measures by the EU

Under current EU legislation on jurisdiction, a collective action could be brought against a company in several Member States based on a single act causing harm, in each case, by consumers in each of these Member States [Art. 16 Regulation (EC) No. 44/2001 or Art. 18 Regulation (EU) No. 1215/2012 for proceedings instituted after 10 January 2015]. In order to avoid this, the Brussels I Regulation could be amended such that in future a single jurisdiction will be stipulated for such a case. This would mean that the company could only be sued in one Member State, e.g. that of its registered office. This has advantages for companies because the costs are lower. However, it takes away from consumers their existing right to sue in their own country.
In addition, where consumers from different Member States are involved in a collective action, the court currently has to apply the law of all these Member States [Art. 6 Regulation (EC) No. 593/2008 ("Rome I"), Art. 4 et seq. Regulation (EC) No. 864/2007 ("Rome II")]. In order to avoid this, "Rome I" and "Rome II" could be amended such that a single applicable law will be stipulated. However, this would have the result for consumers that the - possibly more favourable - law of their own country would no longer apply.

Conclusion

Collective actions can facilitate claims for damages because the affected parties can share the cost and the time involved. The Commission is trying to achieve a balance between protecting the interests of potential claimants and the need for both companies and society as a whole to prevent abusive litigation. The restrictions on collective actions recommended by the Commission reduce the danger of abusive litigation. The option for Member States to use the opt-out principle for reasons of "sound administration of justice" gives rise to legal uncertainty. Since Recommendations have no binding force, a substantive competence is not required. If Germany is to implement the Recommendation it will have to modify its law on civil procedure. The recommended binding effect upon the courts of decisions by authorities results in a curtailment of the legal process if affected parties cannot take action against the decisions of authorities.