# Proposal for a Directive on Representative Actions:

# ILR Comments on Draft JURI Report

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The European Parliament's Committee on Legal Affairs has published its Draft Report[1] on the Proposal for a directive of the European Parliament and of the Council on representative actions for the protection of the collective interests of consumers.[2]

As ILR has previously outlined, the Commission's Proposal has serious shortcomings, and, if adopted without amendment, would not achieve the Commission's stated objectives of a fair and efficient collective redress mechanism. Many aspects of the Proposal are anti-consumer, and would create both the opportunity and the incentive for intermediaries to pursue claims for their own benefit, rather than the benefit of consumers.

ILR is gratified to see that the Draft Report addresses and rectifies a number of the Proposal's most significant shortcomings.

However, despite the good progress made so far, ILR believes that a small number of additional adjustments are desirable in order to ensure that the mechanism is both effective and balanced.

## Good Progress Made

The Draft Report recognizes a number of the Proposal's key deficiencies. For example, the Draft Report:

- Adds important threshold requirements regarding which entities shall be entitled to become "qualified entities" capable of suing on behalf of consumers across all Member States.

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[1] Draft JURI Report on the Proposal for a directive of the European Parliament and of the Council on representative actions for the protection of the collective interests of consumers and repealing Directive 2009/22/EC.

[2] Commission Proposal for a Directive of the European Parliament and Council on representative actions for the protection of the collective interests of consumers and repealing Directive 2009/22/EC.

- Enhances the ability of courts to supervise the suitability of qualified entities. These additions significantly reduce the scope for unsuitable entities to pursue litigation.

- Removes the possibility for "ad hoc" entities to pursue claims, which was an invitation for commercial enterprises to set up special purpose litigation vehicles.

- Removes the most troubling and extreme suggestion in the Proposal, which is that consumer claims for "small individual amounts" could be pursued without any consumer mandate, and any awards made would not go to consumers, but would instead go to a "public purpose". This suggestion would create a system more open to abuse than any in the world. It would deliver no benefit to victims, but would allow vast and uncontrolled claims to be made on their behalf by intermediaries hoping to earn fees from such cases.

- Introduces several much needed safeguards, and does a better job of recognizing the safeguards that the Commission itself has proposed in its own Recommendation on collective redress. For example, it recognizes that punitive damages must be prohibited, and that the "loser pays" rule must apply.

- Recognizes that third party litigation funding in the collective redress context creates a toxic cocktail, which is likely to fuel litigation designed to enrich those funders at the expense of consumers.

- Adds helpful language to seek to limit one of the key weaknesses of the Proposal: a multitude of overlapping and conflicting claims in multiple jurisdictions.

- Adds helpful language to encourage settlements, and to create much desired finality for all parties that do settle.

- Limits the possibility for evidential disclosure processes to be abused and used as a "fishing expedition" or as a lever to cause unjustified costs and pressure traders into unmerited settlements.

The Report's authors should be commended for appreciating many of the flaws of the Proposal and for taking concrete steps in response. However, ILR would respectfully suggest that a limited number of areas need improvement, or have been addressed in ways that may not fully resolve the issues the Proposal will raise.

## Suggestions for Additional Improvements

### *(a) Jurisdiction*

ILR recommends closer consideration of how the mechanisms in the Proposal could work in conjunction with the rules on private international law and the rules related to Court jurisdiction.

As thoroughly explained in the October 2018 study commissioned by the European Parliament's Policy Department for Citizens' Rights and Constitutional Affairs at the request of the Committee on Legal Affairs[3], the existing rules are highly ill suited to collective redress. According to the study's key findings:

"*[i]t notably follows from the current choice of law and choice of jurisdiction rules that the bundling of claims is particularly burdensome and unattractive, if not completely impossible*".

**The likely result of adopting the Proposal in its current form is that large numbers of complicated, parallel (and potentially overlapping) proceedings will arise, and claims will not be resolved in a manner that is simple, quick, fair or efficient.**

The study proposes several adjustments to mitigate the main concerns, which merit close consideration. Some of the suggestions would require adjustments to Regulations (including the Brussels 1a Regulation), which cannot be achieved via a Directive.

**ILR therefore recommends that the Draft Report should include (a) a provision stating that the mechanisms foreseen in the Proposal should come into effect only *after* the adaptation of the relevant jurisdictional rules to accommodate cross border collective redress scenarios, and (b) a request for the Commission to make a (separate) legislative proposal which would make the necessary adjustments to existing rules so that collective redress may be accommodated.**

### *(b) Laws covered*

ILR considers that the list of 59 laws identified in the Annex to the Proposal is misconceived and should be reconsidered. The Annex is not the result of careful analysis, and identifies a number of EU laws that set up regulatory architectures and mechanisms, rather than create easily identifiable consumer rights that could be enforced under the Proposal.

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[3] See Part 3 of the EP Study, requested by the JURI committee, on Collective Redress in the Member States of the European Union

The potential scope of application of the Proposal therefore remains highly unclear. Certain laws (such as the General Data Protection Regulation[4]) contain their own provisions on redress.

Other laws, such as the ADR Directive[5], create no obvious consumer rights at all. **The CPC Regulation[6] contains a far more thoroughly analyzed list of 26 laws, which create enforceable consumer rights, and consideration should be given to reducing the scope of that list until a coherent justification is made for the inclusion of other laws.**

### *(c) Scope restriction needed*

Article 2, paragraph 1 of the Proposal suggests that collective actions can be taken for any breach harming the collective interest of any number of consumers, whether "domestic" (*i.e.,* affecting one Member State only) or cross border.

**Amendment 5 of the Draft Report suggests limiting cases to those with a "broad public impact". While this is helpful, ILR proposes that this concept must be clearly defined, and strictly limited to cases with an EU (and by definition cross-border) dimension.**

There appears to be no justification for EU legislation governing disputes which have no cross-border impact and affect one Member State only, so we suggest the word "domestic" should be deleted from Article 2, paragraph 1. Also, although the Draft Report (in the definition of "collective interests of consumers") would limit cases to those with a minimum of 50 consumers, in circumstances where an "opt-out" may be possible, this would be met in almost every case conceivable, and therefore would provide no practical limitation. **Instead, a definition is required of cases with material, cross-border impacts, and which affect large numbers of consumers.** The CPC Regulation may provide inspiration, in that it describes varying grades of infringements with EU effects.[7] Without clarification, different Member States may take different views on what is "broad" and the purpose of the limitation (to avoid this pan-EU mechanism being used unnecessarily) could be circumvented.

### *(d) Minimum number of consumers*

Amendment 11 of the Draft Report rightly seeks to ensure that a qualified entity is representative of a minimum number of consumers (250) or associations (5) before it could be included in the list of entities entitled to bring actions. This is commendable.

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4 See Annex 1, item 53

5 See Annex 1, item 40

6 See CPC Regulation of 12 December 2017 on cooperation between national authorities responsible for the enforcement of consumer protection laws and repealing Regulation (EC) No 2006/2004.

7 See the concepts of "intra-Union infringement", "widespread infringement" and "widespread infringement with a union dimension" in Article 3 of the CPC Regulation, *ibid*.

**However, Amendment 11 also suggests that for those on a "local level or those representing small countries" the minimum number could be adjusted based on the "size of the territory considered".**

ILR fears that any lowering of the minimum criteria could lead to representative entities seeking accreditation in whichever Member State appears to have the lowest standards (*i.e.,* a type of forum shopping). Also, the concepts of "small" and "local" are subjective, and basing the criteria on the "size of territory represented" seems unworkable (*e.g.,* because there are many Member States with a territory more than 250 times larger than Malta, so if numbers were reduced *pro rata*, the number of consumers to be represented in Malta could be one). **ILR suggests the exception is unnecessary, as it is vital that qualified entities are genuinely representative of a material segment of consumers, and – as above – we suggest that local (national/domestic) cases should not be addressed by these mechanisms in any case.**

*(e) Financial connections to lawyers*

Amendment 13 of the Draft Report rightly seeks to limit the possibility of qualified entities being mere vehicles for financially interested backers. ILR strongly supports this limitation, though the wording could be refined. The suggestion is that a qualified entity is "neither financed by, nor has lucrative agreements with, plaintiff law firms". The word "plaintiff" is unnecessary here, as law firms often cannot readily be categorized into plaintiff or defendant firms. The word "lucrative" could also be reconsidered, as it could be synonymous with "money-making", and might therefore include all agreements in which a lawyer is hired and is paid a fee. The main mischief to be avoided is that law firms (like litigation funders) are not steering qualified entities and litigation for their own interests, which arises in particular when contingency fees are paid. A safeguard identified in the Commission's own Recommendation was that lawyers' contingency fees should be circumscribed.

**We therefore suggest that "qualified entities should neither be financed by, have structural or ownership relationships with, nor have contingency fee agreements with lawyers, nor have any other fee arrangement which risks compromising either the qualified entity's independence, or the lawyer's duty to protect his or her client's interests".**

*(f) Type of action*

Amendment 18 of the Draft report provides that qualified entities should be able to choose "the most suitable instrument available" to protect consumers' interests. It is unclear whether "instrument" refers to the type of action that may be initiated (*e.g.,* an injunction, a declaratory action, or "opt-in" or "opt-out" damages action).

**If so, we recommend that this amendment be deleted, as the availability of different types of action should depend on satisfying the criteria applicable to them, which will greatly depend on the circumstances, and will require court approval.** If such a choice is granted by right in legislation, a court may find it impossible to stop a case proceeding even when it is using an unsuitable "instrument" or mechanism.

### *(g) Admissibility*

Amendment 22 of the Draft Report rightly introduces the concept of "admissibility criteria". These are essential to ensure that meritless cases are excluded at the earliest possible stage. In addition to those criteria identified, **ILR suggests (i) that it is essential that courts be required to assess admissibility at the earliest practicable stage**, to prevent meritless cases being launched to harass, drive up costs and look for "blackmail settlements"; (**ii) that the early assessment include a *prima facie* merits tests** (*i.e.,* is there a real case to be tried?); (iii) that the assessment determine whether there **are sufficient *common issues* to be resolved** for a collective case (cases which have predominantly individual issues, such as most personal injury claims, are not suitable for common resolution); and (iv) that **court-based collective action is the most suitable and efficient way to proceed**, including after consideration of non-court based alternatives (see *(k)* below).

### *(h) Mandate required*

Amendment 24 of the Draft Report contains perhaps the most problematic language of the amendments put forward. As a starting principle, ILR believes strongly that a mandate (*i.e.,* that consumers must actively choose to take part in the actions that concern them and appoint the relevant entity to be their representative) must be secured in every collective case. Without a requirement to secure a mandate, representative entities will be licensed by law to take actions on behalf of consumers without consumers' knowledge or consent, or even against their explicit wishes. It is exactly in circumstances where entities represent no one in particular that they can be tempted to represent and pursue their own interests. Where no consumers are required to approve of actions taken ostensibly on their behalf, no element of control exists, as there is no individual involved to complain to a court or Member State authority that consumers' grievances are being misrepresented or misused.

Amendment 24 suggests that a mandate "shall" be given "at an advanced stage of the proceedings, except as a condition to initiate the action, both for national and cross-border cases". Qualified entities should be encouraged to secure at least a minimum number of mandates at the beginning of the action in order to verify that the case is legitimate and viable, with the potential for others to join at a later stage (up to, we would suggest, the hearing on the merits).

As drafted, the language would seem to prohibit a qualified entity from accepting a mandate at an early stage, even if there were consumers willing to give such a mandate.

Amendment 24 goes on to say, "Member States may not require a mandate from individual consumers that have suffered a small amount of loss in national cases involving only consumers from the same Member State".

This sentence raises multiple issues:

- As mentioned above, ILR believes that EU law should regulate cross-border cases, but not national cases. This is especially so where a case involves "only consumers from the same Member State". Such cases can readily be resolved under domestic/national law.

- Providing that "Member States may not require a mandate" could be read either as an option (*i.e.,* Member States might choose whether to require a mandate) or as a prohibition (*i.e.,* Member States will prohibit all consumer mandates in all circumstances). **ILR proposes that mandates be required in all cases, but if the Draft Report is intentionally taking a different position, at a minimum it must be for Member States to choose whether to require a mandate or not. There is no basis for making mandates illegal.**

- The concept of "small amount of loss" is unclear, and would likely be applied very differently across the EU.

**On balance, we would recommend withdrawing Amendment 24 in its entirety.**

*(i) Undistributed awards*

Amendment 26 of the Draft Report wisely insists that redress measures shall aim to grant consumers full compensation for their loss. However, it goes on to specify that the Court shall decide what to do with any unclaimed amount, though this should not go to the qualified entity or the trader.

Although this is significantly better than the Proposal's concept of awards being diverted to a "public purpose" (which could have included qualified entities themselves, thereby motivating them to take such actions) it still requires refinement, as *cy pres* awards in the U.S. class action system have proved highly problematic.

In the first instance, the issue of "unclaimed amounts" becomes moot if consumers have explicitly mandated all actions. One of the advantages of mandated/opt-in actions is that the relevant consumers are identified and their compensation can be directed to them immediately. It is only when actions are taken on behalf of unknown consumers, who may not exist, or who may have no interest in, or may even oppose the action that traders are forced to payout amounts that compensate nobody.

Second, the provision as drafted seems to contradict both the concept that redress measures are designed to compensate consumers and the provisions in Amendment 27 stating that compensation awarded should not exceed the amount owed to cover the actual harm suffered by consumers and should not be punitive.

By explicitly foreseeing that traders will be required to pay out money that will not compensate anyone, traders are by definition being punished by being forced to payout beyond the amount required to cover the actual harm suffered by consumers. Punishment – including the punishment of disgorgement of illegally obtained profit – is not the role of private civil damages actions in Europe. This is exclusively the role of regulators, and mechanisms already exist to achieve this when necessary. For example, the General Data Protection Regulation foresees fines and a range of other punishments available to regulators, including fines that take account the level of damage suffered by data subjects (Article 83(2)(a)). Separately, at Article 82, it foresees the payment of full compensation to those actually harmed through civil damages. The GDPR does not foresee traders paying out compensation for unnamed, non-existent or hypothetical data subjects.

**In ILR's view, there should be no undistributed awards, which is achievable in an opt-in only system. Traders should pay full compensation to identified consumers with a valid claim, but should not be required to pay more than that amount through a civil damages system designed to compensate, not punish.**

### *(j) Third party funding*

Amendment 30 includes a critical safeguard: the prohibition of third party litigation funding. Without this safeguard, it is highly likely that private commercial operators will seek to capture collective redress systems for their own benefit.

Amendment 30, however, simultaneously seeks to permit funding by "individual contributions". ILR expects that this is intended to permit circumstances where cases are funded by individual member donations or are somehow "crowd-funded", though as drafted this could allow circumvention (*e.g.,* an individual funder could contribute in exchange for later rewards). The intention is not to prohibit member contributions, the use of own resources or donated funds, the use of public resources and support (such as civil legal aid) or even the taking of loans or using legal risk insurance to facilitate a claim.

The main mischief to be avoided is where funding is provided on a commercial investment basis by a third party in exchange for a share of the proceeds in the event of a successful outcome. **This can be achieved simply by prohibiting a third party from providing funding "on a commercial basis in exchange for a share in any fee or award".**

If any third party funding is to be permitted in any Member States, it is critical that a common set of EU-wide safeguards are imposed, including that all funding is transparent and court-approved; that funders are prohibited from participating in any decisions regarding the action (including on settlement); that funders are prohibited from having any form of structural, ownership or other control relationship with qualified entities; that funders' compensation should never be prioritized over compensation to consumers; that funders must demonstrate the existence of adequate resources to support the claim and that they must be liable for adverse costs; and that any fee paid to a funder must be a proportion of the money actually paid to consumers, so that funders are incentivized to deliver redress, rather than design claims mainly for the benefit of the funders themselves.

### *(k) Encouragement of settlements and alternatives to litigation*

Amendment 32 of the Draft Report includes welcome encouragement of settlements. However, Article 8 of the Proposal is exclusively concerned with settlement of court-based litigation. **ILR would propose and encourage that equal emphasis and treatment be given to other forms of dispute resolution which do not depend on cases coming before courts for resolution.**

For example, there are multiple regulatory redress schemes and alternative dispute resolution schemes (including those created by the EU itself) that are typically more effective than court-based collective redress litigation. The Draft Report should (a) ensure that any litigation be suspended while other, potentially more efficient, mechanisms are being pursued by the parties in good faith, and (b) should ensure that when Courts are considering at admissibility stage the suitability of a court-based action to resolve a dispute involving multiple consumers, that Courts have the option of requiring that other alternatives (including any available means, including both ADR and regulatory redress schemes), be attempted first.

## Conclusion

ILR commends the Committee on Legal Affairs for its thoughtful and balanced work to date. With the addition of the suggestions described above, ILR believes that the Proposal can be brought closer to its goal of creating an efficient consumer redress mechanism, without unnecessarily penalizing traders or creating business opportunities for intermediaries at the expense of consumers.

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