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# Response to the Commission Staff Working Document "Towards a Coherent European Approach to Collective Redress" (SEC(2011)173 final).

The European Commission ("**Commission**") has initiated consultation proceedings on the Commission Staff Working Document "Towards a Coherent European Approach to Collective Redress" ("**Working Document**") and has requested that interested parties submit replies thereto by 30 April 2011. Linklaters LLP is an international law firm which specialises in advising leading global corporations and financial institutions on their most important and challenging legal assignments. We and our clients take a deep interest in policy issues in the area of collective actions, and we regularly publish comparative reviews on this topic.[1] We therefore appreciate the opportunity to submit a response to the Working Document.

## Introductory remarks

Collective redress has been a controversial topic for a number of years. The Commission's proposal to review its approach at a European level has therefore much to commend itself. However, in our view the Working Document is based on a number of assumptions that are at least questionable, and we also consider that some of the measures envisaged by the Commission run the risk of being detrimental to European consumers and businesses alike. This holds true in particular for the mechanism that is at the centre of the current debate: compensatory collective redress. The Working Document covers other options as well,[2] but it is clear from previous official documents such as the *White Paper on damages actions for breach of the EC antitrust rules*[3] as well as the *Green Paper on Consumer Collective Redress*[4] that the Commission is primarily considering introducing mechanisms of compensatory collective redress. This is also confirmed by the contents of the draft directive on damages actions for infringements of antitrust law which provided for group actions and representative actions for damage claims in this area.[5]

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[1] See our report *Collective actions across the globe – a summary*, 2011, available online at www.linklaters.com/pdfs/mkt/london/A13187695%20v0.0%201103_Collective%20actions.pdf.
[2] Cf. SEC(2011)173 final, 4 February 2011, para. 7.
[3] COM(2008)165 final, 2 April 2008.
[4] COM(2008)794 final, 27 November 2008.
[5] The proposal has not been officially published but is circulating in interested circles. On its contents, see Burkhard Hess, "Kartellrechtliche Kollektivklagen in der Europäischen Union – Aktuelle Perspektiven" (2010) Wirtschaft und Wettbewerb 493, 496; Robert Lane, "EU Law: Competition" (2010) International & Comparative Law Quarterly 489, 498.

In our view, the introduction of compensatory collective redress mechanisms at EU level is unattractive for a number of reasons. First, legislative action of that sort would imply a comprehensive rewriting of national laws and national legal traditions and therefore amount to a policy change that cannot easily be reconciled with the principle of procedural autonomy. Second, there is no valid basis for the Working Document's hypothesis that EU law is not being enforced properly without the availability of compensatory collective redress. Third, the collective redress mechanisms envisaged by the Commission do not stand the test of a cost-benefit analysis. Fourth, the experience with compensatory collective redress mechanisms at a national level suggests that it is almost impossible to devise a workable European solution that would achieve the Commission's goal in terms of enforcement and still be politically viable. Fifth, it is far from clear whether there is a valid legal basis for a binding EU instrument.

## Additional collective redress mechanisms would conflict with the principle of procedural autonomy

The Working Document is based on a broad concept of collective redress: it encompasses both "injunctive relief", i.e. cases where representative bodies or similar institutions may seek an order to stop allegedly illegal behaviour, and "compensatory relief", i.e. money damage claims.[6] While injunctive collective redress for consumer organisations emerged, at a national level, as early as the 1960s and 1970s[7] and, more recently, also at EU level,[8] compensatory collective redress mechanisms are comparatively new and exist only in a limited number of EU member states.[9]

Dealing with both phenomena under the same heading creates the impression that compensatory collective redress follows on naturally from the pre-existing injunctive redress mechanisms, and that it would not result in substantial change. This impression is, however, misleading. While *injunctive* collective relief involves little more than introducing procedural provisions giving consumer organisations or other relevant bodies standing to apply for appropriate court orders, *compensatory* collective relief would require legislating on numerous issues of substantive and procedural law, namely questions of evidence, discovery, case management, funding, fees, assessment of damages, jurisdiction and applicable law. It would have significant consequences for the traditions of procedural law in the member states.[10] Introducing mechanisms of that sort at EU level would therefore amount to a major shift in policy. In particular, legislative activity in that direction would be in conflict with

[6] SEC(2011)173 final, 4 February 2011, para. 7.

[7] E.g., in Germany (§ 13(1a) *Gesetz gegen den unlauteren Wettbewerb* as amended on 21 July 1965, Bundesgesetzblatt I 1965, 625) and Belgium (article 52(2) *Loi sur les pratiques du commerce* of 14 July 1971, Moniteur Belge, 30 July 1971, p. 9057).

[8] See injunctions directive 98/27/EC, OJ, L 166, 11 June 1998, p. 51, repealed by directive 2009/22/EC, OJ, L 110, 1 May 2009, p. 30. An earlier example is art. 7(1) of the unfair terms directive 93/13/EEC, OJ, L 95, 21 April 1993, p. 29.

[9] For an account on recent legislative reform in the EU member states see the Linklaters report (above n. 1) as well as Duncan Fairgrieve and Geraint Howells, "Collective redress procedures – European debates" (2009) International & Comparative Law Quarterly 379, 383-399.

[10] Burkhard Hess (above n. 5) at p. 502.

the principle of procedural autonomy[11] which is the traditional basis for enforcement of EU law and which implies that in the field of procedural law, policies are primarily made by the member states, not the EU. The Working Document does not address the impact that such a policy change could have.

## There is limited evidence for lack of enforcement of EU law

The policy change proposed by the Commission is based on the assumption that EU law is not enforced properly because "[c]itizens and businesses are often reluctant to initiate private lawsuits against unlawful practices, in particular if the individual loss is small in comparison to the costs of litigation".[12] There is, however, only limited evidence for this hypothesis.[13] Studies undertaken on a European-wide basis indicate that the threshold for consumers to take a complaint beyond a supplier is as low as €18 in some member states, and does not exceed €500 on the other end of the scale.[14] The alleged systematic enforcement deficit therefore exists (if it exists at all) only on a limited basis. More importantly, the research shows that costs are not the primary factor in deciding whether to litigate: in fact, emotional factors play a much more important role. The "biggest driver" for taking a complaint beyond the supplier is the consumer being "unhappy" with the response received from his supplier[15] or finding "initial feelings of disappointment turning to frustration, anger and affront".[16] In other words: in serious cases of illegal behaviour, claimants are likely to bring their cases even where the costs for doing so are relatively high. It appears therefore that the issue of lack of enforcement is less pronounced in those cases where proper enforcement is of particular importance, that is, in cases of serious misconduct.

This empirical analysis suggests that a significant enforcement deficit (if any) will arise primarily in cases of a less serious nature. However, in such cases, the "enforcement argument" becomes somewhat circular, because in as much as there is no court decision, there is no way of telling whether there was any illegal conduct that would have required sanctions.[17] This in itself makes the Commission's enforcement deficit theory less convincing. It also raises further concerns with regard to the principle of procedural autonomy. In terms of effectiveness, this principle is subject to the proviso that national procedural law "must not render practically impossible or excessively difficult the exercise of rights conferred by Community law".[18] The implication is that EU law does not require member states to ensure that in *all* cases of alleged

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[11] On the principle of procedural autonomy see Anthony Arnull, "The principle of effective judicial protection in EU law: an unruly horse?" (2011) E.L.Rev. 51.

[12] SEC(2011)173 final, 4 February 2011, para. 4.

[13] See also the critical remarks of Christopher Hodges, "From class actions to collective redress: a revolution in approach to compensation" (2009) Civil Justice Quarterly 41, 48-49, 55-56.

[14] *Consumer Redress in the European Union: Consumer experiences, perceptions and choices*, Aggregate Report, August 2009, p. 36 (http://ec.europa.eu/consumers/redress_cons/docs/cons_redress_EU_qual_study_report_en.pdf).

[15] *Consumer Redress in the European Union* (above n. 14) at p. 34.

[16] *Consumer Redress in the European Union* (above n. 14) at p. 7.

[17] This phenomenon makes it also difficult to assess, in systems where class actions exist, whether settled cases really reflect illegal conduct or just the nuisance value of the proceedings: see Deborah R. Hensler, "Revisiting the Monster: New Myths and Realities of Class Action and Other Large Scale Litigation" (2001) 11 Duke Journal of Comparative & International Law 179, 198.

[18] Case C-432/05 – *Unibet (London) Ltd. and another v. Justitiekanslern,* [2007] ECR I-2271 [43].

breaches of EU law proceedings will be brought. Against that background, even assuming that the Commission is correct that some breaches of EU law currently go unsanctioned, this would not warrant the significant interference with national procedural laws that the introduction of compensatory collective redress mechanisms at an EU level would require.

## The cost-benefit analysis of compensatory collective redress mechanisms is unfavourable

The Working Document does not address the question of whether compensatory collective redress is an economically sound remedy for the alleged enforcement problems. The statistical data available from EU member states raises serious doubts in that regard. In fact, the aggregate claims in compensatory collective redress proceedings in EU member states are usually below €100,000 and in practice rarely exceed €1m.[19] In light of the sums involved, it is likely that the costs of implementing EU-wide compensatory collective redress would be disproportionately high. The initial step in U.S. class actions of notifying potential class members can incur costs in the region of several million Euros.[20] This figure is likely to be even higher in the EU where cross-border situations are bound to arise, and one would also have to add court and lawyers fees. The cost-benefit analysis is even less favourable in cases of so-called "large scale low value claims" where individual damages are relatively low. In fact, consumers are unwilling to join collective actions involving such claims: for example, in the only consumer collective redress action brought under section 47B of the UK Competition Act 1998, individual damages were in the region of £10–20, and less than 0.1 % of an estimated 1 million consumers joined the action.[21] The same phenomenon exists also in opt-out systems such as the U.S., where experience shows that even in successful class actions, individual damages of less than $100 often go unclaimed.[22]

These figures suggest that there is a risk that compensatory collective redress may be no more than an expensive attempt to sanction minor offences. At any rate, it is unclear where appropriate funding should come from. Whether this is provided by the taxpayer or by businesses which will inevitably pass on their costs, consumers will ultimately pay at least part of the bill. Given the figures indicated above, careful thought must be given to whether the benefits would outweigh the costs.

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[19] *Evaluation of the effectiveness and efficiency of collective redress mechanisms in the EU*, *Final Report*, Part I: Main Report, p. 42: in 73 % of the cases, the aggregate amount in dispute was below €100,000, and in 90 % of the cases below €1m (http://ec.europa.eu/consumers/redress_cons/finalreportevaluationstudypart1-final2008-11-26.pdf).

[20] Stefan Madaus, "Die Kontrolle unternehmerischen Handelns durch eine europäische class action – eine unmögliche Quadratur des Kreises?" (2010) Jahrbuch Junger Zivilrechtswissenschaftler 103, 114.

[21] "JJB and Which? settle football shirt case", Financial Times, 10 January 2008, p. 2; "A thousand football fans win 'rip off' replica shirt refunds", The Times, 10 January 2008, p. 5.

[22] For example in the recent HP inkjet printer class action (*In re HP Inkjet Printer Litigation*, 2011 WL 1158635 (N.D. Cal. 29 March 2011)), less than 1 % of the class members collected their e-credits worth between $2 and $6 (http://www.consumerclassactionsmasstorts.com/2011/04/articles/settlement/federal-court-finds-cafa-doesnt-preclude-settling-bullh-cases-for-nuisance-value-but-it-should-limit-class-counsels-fee-award/). Even case studies by proponents of class actions show low claim rates of about 30 % where individual claims are less than 100 USD, see Deborah R. Hensler (above n. 17) at p. 201.

## The experiences at a national level raise doubts as to the feasibility of compensatory collective redress legislation

The experiences in those EU member states that have already introduced mechanisms of compensatory collective redress also do little to support the Commission's initiative in that area. In fact, the compensatory redress procedures currently in place in many EU member states do not include all of the procedural mechanisms that have contributed to abuses of the class action system in the U.S., in particular the discovery process, jury trial and punitive damages.[23] This sort of collective redress meets with little enthusiasm in practice: studies undertaken for the Commission identified, for all EU member states, just over 300 collective compensatory redress actions in the last couple of years.[24] In Germany, for example, the collective action enabling consumer organisations to represent several individual consumers in one set of proceedings (§ 79(2)(3) *Zivilprozessordnung*) is said to be of little or no practical relevance,[25] and the test case procedure in the area of financial services (*Gesetz über Musterverfahren in kapitalmarktrechtlichen Streitigkeiten*) led to only 25 cases and 2 court decisions on the merits in five years.[26] In the UK, there were just 75 group litigation orders between 2001 and 2010.[27]

By contrast, in the period 1995-1996 about 1,000 court decisions on class actions were registered in the U.S. and about 3,200 cases were reported in the press.[28] These figures suggest that class actions are popular with plaintiffs in the U.S. and their lawyers precisely because of those elements that many EU member states have chosen not to adopt. Where these elements are not present, compensatory collective redress appears to be relatively unattractive to claimants. This observation has important consequences for EU policy in the area of collective redress because it indicates that it is very difficult to conceive a compensatory collective redress mechanism that will lead to a substantial increase in proceedings without providing the incentives necessary to encourage claimants to seek redress.[29] A collective redress mechanism that does provide such incentives is likely to have much in common with U.S. class actions. This option, however, does not seem attractive to the Commission[30] and would, at any rate, be politically unacceptable in many, if not most EU member states.[31]

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[23] See SEC(2011)173 final, 4 February 2011, para. 21.

[24] *Evaluation of the effectiveness and efficiency of collective redress mechanisms in the EU* (above n. 19), Part I: Main Report, p. 6-7.

[25] Caroline Meller-Hannich and Armin Höland, *Evaluierung der Effektivität kollektiver Rechtsschutzinstrumente für Verbrauch im nationalen Recht und rechtliche Bewertung ausgewählter Ansätze zu ihrer Fortentwicklung*, *Abschlussbericht für die Bundesanstalt für Landwirtschaft und Ernährung*, 2011, p. 123 (http://download.ble.de/09HS011.pdf).

[26] Caroline Meller-Hannich and Armin Höland (above n. 25) at p. 19.

[27] A list of group litigation orders is available online at www.justice.gov.uk/guidance/courts-and-tribunals/courts/queens-bench/group-litigation-orders.htm.

[28] Deborah R. Hensler (above n. 17) at p. 185.

[29] See the similar remarks of Duncan Fairgrieve and Geraint Howells (above n. 9), at p. 408.

[30] SEC(2011)173 final, 4 February 2011, paras 21, 22.

[31] See Gerhard Wagner, "Collective redress – categories of loss and legislative options" (2011) Law Quarterly Review 55 as to scepticism in Europe regarding class actions in the U.S.: "the perception on this side of the Atlantic is that the class action is responsible for a large part of the abuses of the civil justice system to be observed in the United States."

## Insufficient legal basis for EU legislation

It should also be noted that it is far from clear whether there is a sufficient legal basis for introducing European compensatory collective redress mechanisms. In that context, a distinction should be drawn between mechanisms intended to coordinate mass litigation ("mass torts"), and mechanisms geared towards large scale low value claims ("scattered losses"), that is, claims that may otherwise not be viable.[32] In scenarios of mass litigation of viable individual claims, collective redress mechanisms primarily have the function of streamlining procedures. In this context, the question is essentially one of national procedural law,[33] and the EU has no competence to legislate in this area as such.[34] At any rate, the Commission's concerns seem directed more towards cases of perceived enforcement deficits, that is, large scale low value claims where individual claims would not be litigated at all.[35] However, the mere claim that enforcement of EU law might be improved by mechanisms of collective redress may prove insufficient to create EU competence. In that context, it should be recalled that it was subject to debate whether the EU treaties provide for a legal basis for the injunction directive.[36] Article 81(2) TFEU (ex article 65 EC) allows legislation on procedural laws, but only for cross-border matters, and it is politically and technically difficult to conceive a European collective redress mechanism that would not cover purely domestic cases. Article 114 TFEU (ex article 95 EC) allows legislation with a view to harmonising the member states' laws that affect the establishment and the functioning of the internal market. However, this provision is no general basis for regulation of the internal market,[37] and therefore does not allow measures for consumer protection simply because they have a single market aspect. Harmonisation measures are not possible where the legal act in question only harmonises the market conditions "in passing", while it is mainly directed at other aims.[38] Moreover (and perhaps more importantly), article 114 TFEU does not allow harmonisation where there are only minor distortions of competition.[39] Similar principles would apply to article 352 TFEU (ex article 308 EC).[40] It is therefore questionable whether the injunctions directive 98/27/EC is a suitable model for passing EU legislation providing for a general collective redress scheme.

## Conclusion

Compensatory collective redress is, in our view, not an appropriate matter for EU legislative intervention. Policy considerations as well as a cost-benefit

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[32] On the functional difference between these two devices and the implications for EU legislation see Duncan Fairgrieve and Geraint Howells (above n. 9) at p. 381 and Gerhard Wagner (above n. 31) at p. 82.
[33] Duncan Fairgrieve and Geraint Howells (above n. 9) at p. 381.
[34] See also Gerhard Wagner (above n. 31) at p. 82.
[35] Duncan Fairgrieve and Geraint Howells (above n. 9) at p. 407.
[36] See Hans-W. Micklitz and Peter Rott, in: Eberhard Grabitz and Meinhard Hilf, *Das Recht der Europäischen Union*, 40th ed. 2009, comment on directive 98/27/EG, introduction para. 14 et seqq. For a discussion of the proper legal basis for the draft directive on antitrust damage actions see Robert Lane (above n. 5) at p. 498.
[37] Case C-376/98 *Tobacco Advertising I* [2000] ECR I-8419 [83].
[38] Case C-376/98 *Tobacco Advertising I* [2000] ECR I-8419 [33].
[39] Case C-376/98 *Tobacco Advertising I* [2000] ECR I-8419 [107, 109].
[40] Case T-306/01 *Yusuf and another v. Council and Commission* [2005] ECR II-3533 [145}-[147].

analysis are clearly in favour of more traditional devices such as the widely used stop now orders, e.g. on the basis of the injunctions directive 98/27/EC (now 2009/22/EC). Where these mechanisms prove to be insufficient, regulatory intervention may be more effective. The solution to perceived enforcement deficits should, therefore, be sought through a reform of existing legal mechanisms rather than by introducing compensatory collective redress at EU level. Against that background, we would answer the applicable questions of the Working Document as follows:

Question 1 (added value of new mechanisms of collective redress): We do not share the Commission's assessment that there is a material enforcement deficit, and therefore do not think additional collective redress mechanisms would have a measurable added value for the enforcement of EU law. In any event, we would not be in favour of mechanisms of compensatory collective redress.

Question 2 (private collective redress and enforcement by public bodies): Available data suggests that existing compensatory redress mechanisms in EU member states cannot replace enforcement by public bodies.

Question 3 (strengthen enforcement of EU law): See the answer to question 1 (we do not see a material enforcement deficit).

Question 4 (principles of EU law to be observed): European legislative intervention would have to comply with the principle of procedural autonomy of the EU member states. For an EU measure to be based on articles 114 or 352 TFEU, the Commission would have to show that the absence of an EU-wide collective redress mechanism leads to considerable distortions of competition.

Question 5 (need for extending injunctive redress or introducing compensatory redress at EU level): See the answer to question 1 above. We see no need for extending the existing mechanisms, and would not be in favour of introducing compensatory collective redress mechanisms.

Question 6 (binding or non-binding approach): We think that there is no valid legal basis in the TFEU for a legally binding instrument introducing compensatory collective redress at EU level.

Questions 7 – 31: Not applicable given that we do not see any need for further action at EU level.

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