



DELIVERING COLLECTIVE REDRESS

Response to the European Commission's Inception Impact Assessment
'A New Deal for Consumers – revision of the Injunctions Directive'
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Policy Recommendations

1. The mechanisms that deliver collective redress (CR) should be adopted; the mechanisms that do not work well should not be adopted.
2. The mechanisms that deliver CR well are:
 - a. Regulatory Authorities with CR powers ('regulatory redress'); and
 - b. Consumer Ombudsmen (a particular form of ADR bodies).³
3. There are real dangers with some options. In dealing with large sums of money, and a system that involves facilitative intermediaries who have any commercial interest will produce the abuse that the EU has declared not to accept.⁴ This means that intermediaries must be public or regulated not-for-profit ombudsman bodies—and not trade or consumer associations, that are vulnerable to capture by lawyers and litigation funders, and are not individuals.

Analysis

4. **The requirement to base policy on an examination of all the options, and on empirical evidence.** The European Commission has committed itself to basing policy and rule-making on evi-

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³ The Consumer Ombudsman mechanism is the form of ADR that is adopted in some Member States. This type of ombudsman differs from the Consumer Ombudsman found in the Nordic states, which is a (highly effective) national regulatory/enforcement authority but one that does not have a function of resolving individual disputes (i.e. it is type (a) above rather than type (b) above).

⁴ Commission Recommendation of 11 June 2013 on common principles for collective redress mechanisms in the Member States for injunctions against and claims on damages caused by violations of EU rights, COM(2013) 3539/3, 11.6.2013.

dence, and to reducing regulatory burdens.⁵ It is a Better Regulation requirement that policy on CR should be based on an objective analysis of *all options*.⁶

5. However, too often, assertions on CR assume that only one mechanism (the court-based collective action) is the only option.
6. There are said to be two goals of collective redress: compensation and deterrence. The evidence is that collective actions rarely provide full compensation: damages are reduced by transactional and intermediaries' costs, and sums can remain undistributed to those who have suffered losses.
7. The evidence that collective actions deter future behaviour is extremely limited, and the evidence that exists is not very strong. In fact, the evidence that public or private fines or damages delivered through enforcement adequately affects future behaviour *in an effective regulatory capacity* is highly unimpressive.⁷
8. There is increasing and strong evidence that the most effective way to affect future behaviour of most businesses is through a supportive approach to achieving compliance, especially a relationship that is based on evidence supporting mutual trust and cooperation.⁸
9. **Evaluating the different options.** There is overwhelming evidence that the collective action mechanism is “too complex, costly and lengthy to fully reach its objectives”.⁹
10. EU-style collective actions that need to apply extensive safeguards against abuse suffer from an inherent ‘catch 22’ problem: they will not be particularly effective in delivering CR. In contrast, the US class action model contains weak safeguards and positively encourages private litigation, which inherently produces abuse because of the uncontrolled financial forces that arise and overwhelm the inherent conflicts of interest of the private sector intermediaries (lawyers and funders).¹⁰ In order to solve that problem, one needs to look ‘outside the box’ of litigation.
11. Other mechanisms that are now widely used to deliver collective redress are:
 - a. Civil claims piggy-backing on criminal prosecution;
 - b. Regulatory redress: where a public enforcement body has power to order, or seek a court order for, collective redress;¹¹

⁵ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, *Better regulation for better results: An EU agenda*, COM(2015) 215 final, 19.5.2015.

⁶ Communication from the Commission to the European Parliament, the European Council and the Council, *Better Regulation: Delivering better results for a stronger Union* (European Commission, 2016), COM(2016) 615 final, 14.9.2016.

⁷ C. Hodges, *Law and Corporate Behaviour: Integrating Theories of Regulation and Enforcement* (Oxford: Hart Publishing, 2015).

⁸ Some examples of this new approach are: *Supervision of Behaviour and Culture. Foundations, practice & future developments* (DeNederlandscheBank, 2015); *Delivering better outcomes for consumers and businesses in Scotland* (Scottish Government, 2016); *Primary Authority Statutory Guidance* (Department for Business, Energy & Industrial Strategy, Regulatory Delivery, 2017), https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/648597/primary-authority-statutory-guidance-2017.pdf

⁹ Inception Impact Assessment, *A New deal for Consumers – revision of the Injunctions Directive* (European Commission, 31/10/2017) Ares(2017)5324969, citing Study supporting the assessment of the implementation of 2013 EC Recommendation on Collective redress.

¹⁰ C Hodges, ‘Collective Redress: A Breakthrough or a Damp Squibb?’ (2014) 34 *Journal of Consumer Policy* 67–89; DOI 10.1007/s10603-013-9242-0.

¹¹ Regulatory redress powers may be diverse: the mechanism and a typology are at C Hodges, ‘Mass Collective Redress: Consumer ADR and Regulatory Techniques’ (2015) 5 *European Review of Private Law* 829.

- c. Consumer Ombudsmen (operating as dispute resolution bodies, not in the Nordic sense as enforcement authorities) – but not other forms of ADR;
- d. Personal injuries administrative schemes.¹²

12. Empirical research on an extensive database of case studies in European Member States has clearly demonstrated the superiority in delivering CR of the mechanisms of ‘regulatory redress’ and consumer ombudsmen, which far surpass any court-based CR mechanisms.¹³ The various models were evaluated against objective criteria, set out in Box 1. The difference in terms of performance is clear.¹⁴

Box 1. Evaluation Criteria of Collective Redress mechanisms

1. Speedy identification of a mass issue
2. Ease of ability to identify relevant consumers and contact or refund them
3. Ease of access by consumers: user-friendliness
4. Cost to consumers of accessing the procedure and obtaining redress
5. Duration of the process
6. Total transactional cost
7. Cost of intermediaries/process
8. Delivery of full redress
9. Regulatory outcome: changing behaviour, reducing risk of recurrence

13. **Regulatory Redress.** All sectoral regulators and generic public consumer enforcement authorities should have redress powers as part of their enforcement toolboxes, subject to appropriate oversight mechanisms. The most advanced authorities now approach enforcement by:

- a. identifying the root cause of the problem,
- b. agreeing actions to reduce the risk of reoccurrence of the problem,
- c. ensuring that such actions are implemented by the infringer and others,
- d. ensuring that redress/rectification is made, and
- e. imposing a proportionate supervisory sanction.

14. **Consumer Ombudsmen.** The consumer Ombudsman mechanism that we refer to here is a specific form of ADR body. It is the ADR form that is capable of aggregating individual cases, and data from cases, and feeding it back into regulatory and compliance systems.

15. The Consumer Ombudsman model that we refer to here is:

- (a) an ADR entity that is independent of businesses, trade associations or consumer associations,
- (b) usually created by statute or a not-for-profit company,
- (c) whose dispute resolution process typically involves the following stages in sequence: triage, assisted negotiation between the parties (mediation), a decision that is either legally binding on the trader (but not usually the consumer) or non-legally binding but in practice having strongly persuasive effect,
- (d) free to consumers,
- (e) funded by traders either through a statutory levy or contractual fees,
- (f) satisfies all the quality requirements of Directive 2013/11/EU, arts 5-12,

¹² See S Macleod and C Hodges, *Redress Schemes for Personal Injuries* (Hart, 2017).

¹³ C Hodges and S Voet, *Delivering Collective Redress in Markets: New Technologies* (Foundation for Law Justice & Society, 2017), at <file:///G:/1611%20Oxford%20CR%20conference/FLJS%20Delivering%20Collective%20Redress%20in%20Markets-New%20Technologies.pdf>

¹⁴ The full evidence will be published in C Hodges and S Voet, *Delivering Collective Redress: New Technologies* (Hart Publishing, 2018).

- (g) publishes and feeds back data on cases to support improvements in trading and market behaviour, not identifying individual consumers.
16. The Consumer Ombudsman model exists in some Member States in some regulated sectors, working closely with sectoral regulators, such as a Financial Ombudsman, Energy Ombudsman, Communications Ombudsman and so on. Other forms of ADR bodies, especially ADR schemes that decide individual decisions in arbitration-like processes, do not generally have the capacity to aggregate individual claims and decide them collectively, as most Ombudsman schemes do. ADR bodies should migrate from models of individual arbitration to this ombudsman model. Thus, both sectoral legislation that requires ADR, and the generic consumer ADR legislation,¹⁵ should specify that consumer ombudsmen models should be required, rather than other types of general ADR.
17. **Designing the system to provide efficient and early identification of mass problems.** One should consider *how* mass problems are identified. This usually occurs when *individual* consumers come forward, with individual claims, and scrutiny of the subject matter of all claims by an expert intermediary identifies ones that are similar, and that there is a systemic issue. The expert intermediary identifies that there is a *mass* problem, which gives rise to a number of similar individual claims. But with whom do consumers raise such problems, and how can this be done in a manner that is most efficient, that identifies a systemic problem as quickly as possible, and determines that the issue does give rise to breaches of law that give rise to the need for redress? Who should the intermediaries be?
18. Such intermediaries may in theory be public authorities, not-for-profit ombudsmen, ADR schemes, consumer advisers, ECC-NET offices, consumer associations, trade associations, the media and so on. But not all of them will perform with the same efficiency or effectiveness in identifying a systemic issue. Some of these bodies can be arranged in national landscapes so as to be more effective and efficient than others. National landscapes that have single websites providing advice and access to an ombudsman system have been shown to identify trends and systemic issues quickly because they attract a sufficiently large number of individual contacts, for which the subject matter can be electronically analysed swiftly. A good example is the unique portal / access point of the Belgian Consumer Mediation Service, or resolver.co.uk in the UK.
19. After a systemic issue has been identified, it has to be resolved through a structure and process that is *available* and that meets the criteria set out above. The available dispute resolution process has to be permanent in order to be available, trusted and reliable. If it is not rational that the collective damages process takes place within a court structure—because courts fail to satisfy the criteria—then the standing process has to be a pre-existing consumer ombudsmen scheme or, in the case of personal injuries, an effective administrative compensation scheme. Accordingly, consumer ombudsman schemes need to be available in every Member State so to administer mass claims, since they do this far more efficiently and swiftly than courts, as the data shows.
20. **The proposal to add CR onto the Injunctions Directive.** A proposal recently announced by Commissioner Jurova is to add redress powers on to the injunction powers exercised by approved bodies.¹⁶ We see two major difficulties with this model.
21. **The right model (regulators and ombudsmen), not the wrong model (lawyers, funders and courts).** The first issue is the preference for a model of awarding mass damages that has been shown to be highly ineffective and worse than other possible models—and one that the Commission has explicitly seriously criticised in its own Initial Impact Assessment. The proposal appears to be that damages in mass cases would be awarded by a court process, as a second stage to a

¹⁵ Directive 2013/11 of 21 May 2013 on Alternative Dispute Resolution for Consumer Disputes.

¹⁶ Speech of Commissioner Jurova at the release of the U.S. Chamber Institute for Legal Reform's Consumer public opinion poll on European collective redress and third party litigation funding, entitled 'Are consumers in the EU equipped to defend their rights?', Brussels, 28 September 2017.

finding of breach. But the empirical evidence is that such a (court-based) process would not satisfy the criteria, and that other approaches—regulatory redress and consumer ombudsmen—would be ignored. That would not be rational policy.

22. **The requirement for independence.** The second issue concerns the nature of the intermediaries. It is essential that the intermediaries who are involved can be trusted to act impartially. Some of the possible intermediaries can be trusted to act in the public interest, and consumers' interests, to stop ongoing infringements. However, not all of the bodies can be trusted to act in the public or consumers' interests in seeking collective redress.
23. Both the two mechanisms that are effective in delivering collective redress—regulatory redress and consumer ombudsmen—involve intermediaries that are *independent* of any parties, and subject to objective governance and transparency requirements that support their acting objectively in the public interest. Neither public regulators/enforcement authorities nor regulated not-for-profit ombudsmen (unlike other potential bodies) have commercial conflicts of interest in seeking damages or costs from infringers. Hence, they can be expected to independently, will only pursue meritorious cases and will not pursue or settle cases influenced by their own financial interest.
24. However, there are clear dangers in endowing non-independent bodies—such as consumer associations or trade associations—with CR damages powers because of the conflict of interest that arises through the commercial incentives inherent in large money claims and costs issues, and the risk of capture of such bodies by other commercial service providers (litigation funders and lawyers). The risk of abuse arising out of empowering such bodies is considerable, and there has already been evidence of it.¹⁷ Both consumer associations and trade associations are effective in using injunction powers, but they should *not* be given damages powers.
25. We suggest that entities that may be appropriate for enforcing general consumer protection law backed by a power to seek an injunction are not, therefore, necessarily entities that should be permitted to exercise a power to seek damages. Introducing a major financial incentive into the outcome of an activity introduces a major financial incentive and conflict of interest, which has been clearly shown to be the cause of abuse in the US system.¹⁸ There is a risk here that the Commission may be stepping into the very elephant trap that it had earlier affirmed to avoid.¹⁹
26. **Facilitating settlement: the requirement for structures to be available.** It may be intended that the existence of the compulsory powers of the court will encourage parties to settle cases. But it is not as easy as that in large cases, or where the merits of individual cases have to be assessed. There needs to be readily available an effective *mechanism* that the parties can use. A theory that defendants who are found to have infringed trading law would then typically avoid mass damages claims by settling them has not been established to be valid in practice. Indeed, there is empirical evidence that cases of this type have not been swiftly settled. Arguments on whether an infringement has occurred, and appeals, could be expected to rise in cases where the financial implications were high for defendants, leaving both parties (especially claimants) without resolution for some time. This is what typically happens at the initial certification stage in collective litigation. One of the main reasons why fighting rather than settling is the outcome here is that the primary

¹⁷ We note a worrying number of instances in our forthcoming book.

¹⁸ JC Coffee Jr, *Entrepreneurial Litigation: Its Rise, Fall, and Future* (Harvard University Press, 2015); *US Class Actions: Theory and Reality* EUI Florence working paper 2015/36 (ERC ERPL 14) <http://hdl.handle.net/1814/36536>; in German at <http://hdl.handle.net/1814/46464>

¹⁹ Commission Recommendation 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 (2013/396/EU), recital 15, referred expressly to the need to 'avoid the development of an abusive litigation culture in mass harm situations', and recital 20 stated 'In order to avoid an abuse of the system and in the interest of the sound administration of justice, no judicial collective redress action should be permitted to proceed unless admissibility conditions set out by law are met.' (emphasis added).

process (here, the court procedure) does not *itself* include options of triage, *mediation* and decision, in that sequence. In other words, the parties have to agree to go into a different system and process if they wish to negotiate. The existence of a single integrated process is what makes the consumer ombudsman model distinctive from other ADR schemes, and particularly effective. Consumer ombudsmen can apply the rules of either the law or an ad hoc scheme, and they can triage multiple individual cases, assessing them against acceptance criteria, before facilitating a mediated negotiation.

27. Accordingly, various consequences would flow from access to a damages claim being as a second stage to the right to exercise an injunction power. First, this perpetuates a court-based system, rather than involving more efficient ombudsman bodies. It would tie both claimants and defendants into slow and costly court procedures. Second, injunctions are not a relevant first stage in every case (such as infringements that have already ceased, or infringements where the initial regulatory response is wider and more sophisticated than an order to stop²⁰). So would there be an increase in injunctions threats and actions by those seeking to claim damages? Third, a two-stage process (finding of infringement and calculation of damages) is inappropriate for some types of case, where individual issues predominate (such as reliance of statements, and personal injury causation), and has been shown to attract abusive ‘legal blackmail’ claims.²¹

28. **Fundamental design issues.** The key design questions for the system therefore arise from the need to deliver the following functions:

- a. *Identification* of a mass problem;
- b. *Feedback.* Passing on information on the existence of a mass problem to independent authorities who do not have conflicts of interest for them to act in addressing the problem and obtaining collective redress.
- c. Providing *standing mechanisms* to which consumers and traders can refer individual and collective issues to have them resolved efficiently and expeditiously. The traditional answer to that has been courts, but courts have proved to be far from ideal in handling both small value individual cases and aggregations of multiple cases. If that is so, alternative structures need to exist and to be readily and permanently accessible. The best structures are *consumer ombudsmen*, as outlined above.

29. **The suggested model.** We strongly suggest the following model:

- a. All entities that collect information on market activities should pool their data on problems in the market, so that systemic issues can be identified swiftly. In order to achieve this, the *national landscape* of consumer advice and consumer complaints (i.e. ADR entities) should be *rationalised and connected* with other formal market surveillance mechanisms. *A small number of integrated consumer ombudsmen* operating with a single national website should replace an ADR landscape that contains too many isolated ADR entities.
- b. Any entity that is authorised to use injunction powers should be *required to inform* the entities that are authorised to use damages powers of the existence of an infringement that has been established in circumstances where similar infringements may also have occurred.

²⁰ See C Hodges and R Steinholtz, *Ethical Business Practice and Regulation: A Behavioural and Values-Based Approach to Compliance and Enforcement* (Hart, 2017).

²¹ See C Hodges, *Multi-Party Actions* (Oxford University Press, 2001).

- c. The power to seek damages—individually and collectively—should only be exercisable by approved *independent* entities that do not have any commercial conflict of interest, i.e. public authorities or not-for-profit approved ombudsmen.