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The Consumer Rights Bill and the Inherent Dangers of Opt-out Collective Actions

The Consumer Rights Bill, which is currently before Parliament, would introduce opt-out collective actions to the UK for claims based on competition law. This proposal threatens to upset the balance of the UK civil justice system and harm the wider economy by:

- steering the UK away from the European consensus in favour of opt-in collective actions and towards the opt-out model that has fuelled so much abusive litigation in the United States;

- creating lucrative opportunities for third parties to promote mass litigation (which may be unknown to many of the consumers and businesses alleged to have suffered harm) rather than focusing on ways of delivering compensation without expensive court proceedings; and

- further increasing the liability costs faced by businesses operating in the UK.

Opt-out collective actions do not represent a sensible solution to problems perceived with the current regime for collective competition actions. For these reasons, which are expanded upon below, it is imperative that the provisions on opt-out actions contained Schedule 8 of the Bill are removed.

Introduction

The Consumer Rights Bill represents the most significant overhaul of UK consumer law reform in decades. Additionally, paragraph 5 of Schedule 8 of the Bill would introduce opt-out collective actions for claims based on alleged infringements of competition law. These claims could be brought on behalf of both consumers and businesses. The concept is a radical departure for the UK since opt-out proceedings are alien to its legal culture, and indeed alien to the legal culture of the European Union.1

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1 A 2012 study for the European Parliament’s Economic and Monetary Affairs Committee identified just one EU Member State (Portugal) as having a full opt-out model and only a handful of others that apply the opt-out principle as part of a “hybrid” solution (see Lear, Collective Redress in Antitrust, June 2012, at p. 20). The Portuguese procedure has rarely been used since its introduction, likely due to the length of time taken for a case to pass through the Portuguese court system and the availability of more efficient alternative dispute resolution schemes. It is therefore
The U.S. Chamber Institute for Legal Reform (ILR) firmly believes that the introduction of opt-out collective actions in the UK would have a detrimental impact on the UK’s legal environment by encouraging more litigation, larger claims and, in some cases, speculative claims driven by lawyers and potentially third party investors. The costs of this additional activity would also have negative consequences for business, investment and ultimately the wider economy.

Yet the move to an opt-out model is not necessary. Making adjustments to the existing procedure for collective actions based on competition law would be far less damaging. Urgent action is needed to remove the provisions on opt-out proceedings from the Consumer Rights Bill.

**Opt-in versus opt-out**

Of all the issues faced by policymakers contemplating the design of collective action procedures, whether to adopt an opt-out or an opt-in model is undoubtedly one of the most significant. In simple terms, this is the choice between allowing representative claimants to claim damages:

- only on behalf of those who choose to take positive steps to participate in litigation (i.e., those who ‘opt-in’); or

- on behalf of all persons with potential claims, whether or not they are aware of the action, simply on the grounds that they have not taken action to prevent litigation being pursued in their name (i.e., those who do not ‘opt-out’).

The opt-in approach is favoured by the European Commission\(^2\) and the European Parliament.\(^3\) The Commission has recommended that the claimant party in any collective action should be formed on the basis of express consent from the people or businesses who claim to have been harmed. Any exception to the opt-in model should be justified by reasons of sound administration of justice.

ILR is alarmed that the UK government continues to support the introduction of opt-out collective actions for claims based on breach of competition law. This is also surprising given that in the context of consumer law the Government has rightly recognised the economic cost of collective litigation and the “*heavy burden it largely untested and does not provide a reliable indicator of the consequences of introducing opt-out actions in the UK, whose markedly different legal environment and economy further undermine comparisons with Portugal.


\(^3\) European Parliament Resolution of 2 February on ‘Towards a Coherent European Approach to Collective Redress’ (2011/2099(INI)). See article 20, second indent: “the European approach to collective redress must be founded on the opt-in principle, whereby victims are clearly identified and take part in the procedure only if they have expressly indicated their wish to do so”; available at: http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2012-0021+0+DOC+XML+V0//EN.
Would place on businesses.

ILR has for many years drawn attention to the heavy burden created by collective actions across the world and believes that if the availability of collective procedures in the UK is to be expanded then abandoning the opt-out mechanism is an essential step to minimize the harm that such an expansion will cause.

**Why the opt-out model should be rejected:**

**Opt-out compromises legal autonomy**

- The ability of representative claimants in opt-out proceedings to assert claims on behalf of potentially thousands of other parties without their authorisation (or even their knowledge) robs those parties of their legal autonomy.

- The opt-out model was pioneered in the United States and has been described by the European Commission as one of the key ingredients of the ‘toxic cocktail’ which gave rise to the infamous U.S. class action system.

- The U.S. experience is that opt-out class actions result in apathy, lawyer-driven lawsuits and lawsuit abuse. Opt-in procedures are vastly superior in deterring abusive litigation and in protecting the rights of all group members. They ensure that the only individuals who affirmatively seek to be a member of the group can participate in (and be bound by) a lawsuit.

- The consequences of opt-out class actions should not be seen as a purely American problem. The opt-out model has been adopted by other jurisdictions which do not have all the features of the U.S. legal system. For example, in Australia a thriving class actions industry is being driven by the profits available to lawyers and third party litigation funders.

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4 Department for Business, Innovation & Skills, Civil Enforcement Remedies: Consultation on extending the range of remedies available to public enforcers of consumer law (November 2012). See paragraph 3.10.


7 Ibid. Page 10.
Opt-out is most lucrative for third parties

- A key part of the rationale for introducing opt-out proceedings is to facilitate collective claims where the sum that may be recovered by each member of the class is not large enough to incentivize each class member to pursue a claim individually. In such cases, the amount recovered by each class member is likely to be a fraction of the fees generated by the lawyers and claims management companies who will be incentivized to promote mass claims (as demonstrated by the Australian case described above).

- Instead of expanding collective actions, the Government should focus on ways of requiring businesses who have engaged in anti-competitive conduct to pay compensation without the need for expensive and mutually burdensome litigation, such as through public enforcement or alternative dispute resolution (ADR) mechanisms. The implementation of the EU Directive on ADR, which must be achieved by July 2015, is intended to improve the availability and quality of ADR in the consumer sphere and could be a catalyst for greater use of ADR in disputes between businesses. These improvements should be given time to take effect before contemplating the introduction of opt-out collective actions, which will create commercial opportunities for the parties with which ADR cannot compete.

- The Consumer Rights Bill as put before Parliament would at least prevent lawyers from recovering fees calculated as a proportion of the total amount recovered by the class in opt-out proceedings (i.e., damages-based agreements). What is not clear, however, is whether third party litigation funders would also be prohibited from entering into similar agreements.

- If the possibility of opt-out proceedings remains in the Bill, it should be clarified that third party litigation funding will not be permitted and the prohibition should in any case be extended to all collective proceedings (including opt-in). Third party litigation funding presents a greater risk in connection with collective actions than damages-based agreements entered into by lawyers, because lawyers are at least subject to professional conduct rules.

- Litigation funders in the UK are presently subject only to a voluntary code of conduct. In a House of Lords debate on the Damages-Based Agreements Regulations 2013 Lord Beecham observed that, of 25 litigation funders then established in the UK, only nine were members of the Association of Litigation Funders that administers the voluntary code. He went on to remark that “[litigation funders] are not even joining their own association,
let alone being responsible to any independent and impartial organisation to oversee their work.”

In the recent English case of *Excalibur Ventures LLC v Texas Keystone and others*, three litigation funders supported what were described by Lord Justice Christopher Clarke as “a range of bad, artificial or misconceived claims” with a “grossly exaggerated” quantum of US$1.65 billion and none were members of the Association of Litigation Funders.

Following the introduction of ‘alternative business structures’ there is also now the possibility that litigation funders could own and manage law firms. A law firm may therefore find itself conducting collective proceedings under an ordinary fee arrangement but with litigation funding provided by the firm’s owners (assuming that would not be caught by the prohibition on damages-based agreements in opt-out proceedings). Through the influence and instructions of its owners, the lawyers conducting the case would find themselves subject to the same influences that the prohibition was intended to avoid, which further illustrates why the prohibition must extend to third party litigation funding.

**Opt-out fuels abusive claims**

- The U.S. experience has amply shown that opt-out collective actions impose substantial settlement pressure on defendants, independent of the merits of the litigation, because of the scale of their exposure. The settlement pressure generated in such circumstances is so great and so disconnected from the merits of the case that it leads to what have been described as ‘blackmail settlements’. The availability of such settlements creates a spiral effect, in which the pressure on defendants to settle claims regardless of merit encourages the filing of ever more non-meritorious claims.

- The Consumer Rights Bill provides for supervision of collective proceedings, which could only move forward if permitted by the Competition Appeal Tribunal. It is clear from the U.S. class action system, where a similar gateway mechanism does exist, that an order allowing opt-out proceedings will take on huge tactical significance and allow settlements to be extracted from businesses that simply cannot afford to take the risk of opt-out proceedings going ahead.

- More generally, it is palpably clear that creating the opportunity to commence mass claims on behalf of potentially unknowing members of the

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8 Hansard HL Deb 26 February 2013, vol 743, col GC130.
9 *Excalibur Ventures LLC v Texas Keystone and others* [2013] EWHC 4278 (Comm), paragraphs [24] and [29].
10 *Rhone-Poulenc Rorer*, 51 F.3d at 1298.
public (which is not to be confused with ‘access to justice’) necessarily increases the risk of meritless litigation, and the attendant harm to business, the economy and, ultimately, to consumers themselves.

**Opt-out is damaging for growth**

- The devastating effects of massive settlements or adverse judgments under an opt-out model are not only felt by defendants. Their impact on businesses reverberates throughout the economy, affecting the business’s employees, shareholders, and potentially customers through higher prices.

- Recent analysis shows that liability costs as a proportion of GDP are greater in the United States, where opt-out class actions are well established, than in other developed economies (1.66% in 2011). Meanwhile, liability costs in the UK as proportion of GDP have risen in recent years and are already greater than in other European countries (1.05% compared with 0.63% in the Euro zone).11 These high costs may deter investment and increase business’s borrowing costs, which would have a negative impact on growth, investment and job creation at precisely the time when the UK economy is experiencing a fragile recovery.

**An opt-out model is not the solution to problems perceived with the current regime**

- Outside of the field of competition law, there have been numerous group actions brought under the existing procedure for Group Litigation Orders, which is essentially an opt-in form of collective action. It is therefore unclear why competition law should be treated as a special case requiring an opt-out model.

- Only one case has been brought under the existing opt-in procedure for collective competition law claims: The Consumer Association (Which?) v JJB Sports plc. Despite the case receiving extensive press coverage, fewer than 0.1% of affected consumers chose to join the action seeking compensation for over-charges on replica football shirts. The Government views the lack of more cases and the low number of consumers who participated in the football shirts case as meaning that the current regime has failed and an opt-out model is the solution.

- This single case is not capable of demonstrating the need for an opt-out procedure and nor is the absence of more cases. Instead of making such a radical change to the justice system the Government should focus on what

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can be done to improve the existing opt-in procedure and answer questions such as: Why did individuals who allegedly suffered harm not take the opportunity to have a third party claim compensation on their behalves? Were they aware of that possibility? Was the legal process and its potential consequences adequately explained to them?

- Opting-in to a legal action is a serious matter to any consumer, and ILR strongly believes that it is not fairer to adopt an opt-out regime which risks consumers having this decision made for them than to improve the opt-in regime. Provided consumers and businesses make informed choices about whether or not to participate in a legal process, those choices should be respected.

- It is also worth asking whether people actually want redress to be delivered via private litigation, rather than as part of the public enforcement process or out of court through alternative dispute resolution. The Consumer Rights Bill would allow anyone to act as a representative claimant in opt-out proceedings provided he was approved by the Competition Appeal Tribunal at the outset of the case, yet the public may be more comfortable obtaining compensation without involving commercial parties whose interest in their rights is primarily financial.

For all of the reasons set out above, ILR firmly believes that if Parliament wishes to expand the regime for collective actions based on competition law, restricting such actions to an opt-in model is among the most important safeguards to prevent abuse. An opt-out model is highly likely to lead to abusive litigation and ‘blackmail settlements’, to excessive cost, to economic harm – there are far superior means available to address the perceived failings of the current system.