

## Written Evidence submitted from the U.S. Chamber Institute for Legal Reform (CR 18)

### Concerning Schedule 8 of the Consumer Rights Bill

#### About the U.S. Chamber Institute for Legal Reform

1. The U.S. Chamber Institute for Legal Reform is a not-for-profit public advocacy organisation affiliated with the U.S. Chamber of Commerce, the world's largest business federation, which represents the interests of more than three million businesses of all sizes, sectors and regions, in addition to state and local chambers and industry associations. Many of the U.S. Chamber's members are companies that conduct substantial business in the UK. ILR is therefore deeply interested in the orderly administration of justice in the UK.
2. ILR's mission is to restore balance, ensure justice and maintain integrity within the civil legal system. We do this by creating broad awareness of the impact of litigation on society and by championing common sense legal reforms at the state, federal and global levels. Since its founding in 1998, ILR has worked diligently to limit the incidence of litigation abuse and has participated actively in legal reform efforts in the United States, the UK and elsewhere.

#### Summary

3. ILR's primary interest in the Consumer Rights Bill is not the reforms of consumer law contained in the body of the Bill but the changes to private actions in competition law that would be introduced by clause 80 and Schedule 8 of the Bill. In particular, paragraph 5 of Schedule 8 would introduce opt-out collective litigation to the UK for the first time.
4. ILR's experience of this model of litigation, not only in the U.S. but also in other jurisdictions such as Australia, is that it is prone to abuse and generates significant costs for businesses of all sizes. These costs sometimes arise as a result of businesses being pressured into taking strategic decisions to settle weak or altogether meritless cases. Therefore, these costs will not fall exclusively on those businesses that are adjudged by the Courts not to have complied with the Competition Act.<sup>1</sup> Even businesses that contest claims all the way to judgement and succeed cannot expect to recover their legal costs in full, let alone the costs incurred in devoting time and internal

---

<sup>1</sup> Department for Business, Innovation & Skills, *Private Actions in Competition Law: A consultation on options for reform – final impact assessment* (January 2013). See summary analysis of Policy Options 2 and 3.

resources to litigation (especially if recoverable costs are capped). ILR calls on the Committee to amend paragraph 5 of Schedule 8 of the bill by removing the possibility of opt-out collective proceedings, which would be the most costly aspect of any additional litigation that occurred as a result of the changes set out in Schedule 8.

5. If, despite the attendant risks, opt-out collective proceedings are to be introduced in the UK, ILR calls for clarification that it will not be possible for third party litigation funders to invest in such cases. As currently drafted, paragraph 6 of Schedule 8 to the Bill would prohibit “damages-based agreements” in relation to such proceedings. While it seems clear on the face of current legislation that third party litigation funding agreements would be captured by this prohibition (see paragraph 20 and footnote 14, below) the Bill would be improved by explicitly stating that this is the case.
6. ILR also comments below on: the authorisation of representatives in collective proceedings; the eligibility of claims for collective proceedings; the choice of whether proceedings should be opt-out or opt-in; and the assessment of damages in collective proceedings.

### The Introduction of Opt-out Collective Proceedings

7. In 2012, the Department for Business Innovation and Skills carried out a public consultation on proposals for the UK regime on private competition litigation. In its response, published in January 2013, the Government reported that its proposals had provoked a strong reaction from stakeholders, particularly on the question of whether opt-out actions should be introduced.<sup>2</sup> Respondents were said to be sharply divided on this point.
8. ILR has significant experience of the negative consequences of opt-out collective or “class” litigation and was alarmed that the proposal to introduce an opt-out mechanism in the UK was taken forward in the Consumer Rights Bill. ILR also finds it difficult to understand why the Government proposes to expand the possibilities for collective litigation based on competition law when, in relation to consumer law, it has rightly recognised that collective litigation generally (not only opt-out proceedings) creates incentives for intermediaries which result in a heavy burden on businesses.<sup>3</sup> The attempt to distinguish collective litigation based on one particular area of law, which is well known to generate complex and protracted disputes, is unconvincing.

---

<sup>2</sup> Department for Business Innovation & Skills, *Private Actions in Competition Law: A consultation on options for reform – government response* (January 2013). See paragraph 5.7.

<sup>3</sup> 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.

9. The experience of the U.S. class action system, and other jurisdictions that have opt-out proceedings such as Australia, is that they are inherently prone to abuse by profit-seeking third parties such as lawyers and litigation funders.<sup>4</sup> The scale of liability in such cases provides an opportunity for these parties to extract lucrative settlements from businesses which choose to settle claims as a means of avoiding the time, costs and negative publicity associated with large-scale litigation, regardless of the merits of the litigation itself.
10. 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 major jurisdictions (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 Eurozone).<sup>5</sup> 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. In the view of the Australian Institute of Company Directors, class actions, due to their size and scale "*can impose costs on the public in the form of higher consumer prices, the diminution in share value ... and decreased tax revenue*".<sup>6</sup>
11. ILR also opposes the provision in paragraph 6 of Schedule 8 to the Bill that envisages unclaimed damages in opt-out proceedings being distributed to charity. Without commenting on the merits of the work done by the designated charity (currently the Access to Justice Foundation), ILR considers the idea of distributing damages awards to non-parties to be at odds with the principle that damages should be compensatory. Furthermore, such a mechanism greatly reduces the incentive for representatives to identify those actually harmed. Instead it allows lawyers and third party funders to focus on their own reward, without having to be concerned about whether victims are actually compensated. Designating a particular charity to receive unclaimed sums may remove some of the problems associated with the use of *cy pres* mechanisms in litigation, but it

---

<sup>4</sup> King & Wood Mallesons, *Class Actions in Australia: The Year in Review 2012*, available at: [http://www.mallesons.com/Documents/Class Actions in Australia-The Year in Review 2012.pdf](http://www.mallesons.com/Documents/Class%20Actions%20in%20Australia-The%20Year%20in%20Review%202012.pdf).

<sup>5</sup> NERA Economic Consulting for ILR, *International Comparisons of Litigation Costs: Europe, the United States and Canada* (May 2013), available at: <http://www.instituteforlegalreform.com/sites/default/files/NERA%20FULL.pdf>.

<sup>6</sup> Australian Institute of Company Directors, *Corporations Amendment Regulations 2012* (27 January 2012), available at: <http://www.companydirectors.com.au/Director-Resource-Centre/Policy-on-director-issues/Policy-Submissions/2012/Litigation-Funding-Corporations-Amendment-Regulations-2012>.

does not address the fundamental issue that the damages awarded will not benefit the absent class members.<sup>7</sup>

12. Moreover, the fact that opt-out proceedings result in large sums going unclaimed calls into question whether opt-out collective actions are necessary to achieve the goal of compensation.
13. For the reasons set out above and in its submission to the 2012 consultation on private competition actions,<sup>8</sup> ILR does not believe that the case has been made for introducing an opt-out model in the UK, particularly given the attendant risk of further increases in liability costs to UK businesses and the wider economy.
14. Notwithstanding its opposition to the introduction of opt-out collective proceedings, ILR offers the following comments on the detailed provisions set out in Schedule 8.

### Damages-Based Agreements in Collective Proceedings

15. It is proposed that damages-based agreements (“DBAs”) (i.e., agreements pursuant to which lawyers are paid a proportion of the money recovered by their clients) should be unenforceable if they relate to opt-out collective proceedings.<sup>9</sup>
16. ILR welcomes this proposal but does not believe the absence of DBAs will necessarily prevent abuse, especially if DBAs are interpreted as encompassing only agreements by which claimants agree to give up a share of the proceeds of litigation to lawyers. After all, third party litigation financing also involves agreements by which claimants agree to give up a portion or percentage of litigation proceeds, in such instances to the litigation funders. The example of Australia is particularly instructive given that opt-out collective actions have been available there for some time, but, unlike in England and Wales, lawyers in Australia are not permitted to enter into agreements equivalent to DBAs. This has not prevented abuse in the Australian class actions system, primarily as a result of third party litigation funding, which is well-established in Australia<sup>10</sup> and is becoming increasingly prominent in the UK. Litigation funding is also problematic in opt-out collective actions because in an opt-out lawsuit where many, if not most, group members are absent, these absent group members will not have

---

<sup>7</sup> For an in-depth view of the problems associated with cy pres mechanisms in class actions, see ILR’s *Cy Pres: A Not So Charitable Contribution To Class Actions Practice* (October 2012), available at: [http://www.instituteforlegalreform.com/sites/default/files/cypres\\_0.pdf](http://www.instituteforlegalreform.com/sites/default/files/cypres_0.pdf).

<sup>8</sup> See: [http://www.instituteforlegalreform.com/uploads/sites/1/ILR\\_BIS\\_Response20287-24-201229-5.pdf](http://www.instituteforlegalreform.com/uploads/sites/1/ILR_BIS_Response20287-24-201229-5.pdf).

<sup>9</sup> Paragraph 6 of Schedule 8 (new section 47C(7) of the Competition Act 1998).

<sup>10</sup> King & Wood Mallesons, *Class Actions in Australia: The Year in Review 2012*, available at: [http://www.mallesons.com/Documents/Class\\_Actions\\_in\\_Australia-The\\_Year\\_in\\_Review\\_2012.pdf](http://www.mallesons.com/Documents/Class_Actions_in_Australia-The_Year_in_Review_2012.pdf).

an agreement with the funder. This circumstance creates conflicts of interest within the group, especially where a funder seeks its premium in respect of recoveries by non-funded group members.

17. It has recently been reported that one Australian law firm created its own litigation funding vehicle, effectively circumventing the prohibition on DBAs.<sup>11</sup> It was proposed that this vehicle would co-fund class members who were participating in a class action conducted by the same law firm, with the class members waiving any conflict of interest that arose as a result. The law firm initially sought approval from the Court for this arrangement but withdrew its application following unfavourable statements by the Commonwealth Attorney-General. Those statements also reveal that the Attorney-General is to propose further regulation of litigation funding (something that should be done in the UK).
18. In many respects, third party litigation funding presents a greater risk in connection with opt-out collective actions than DBAs between claimants and lawyers, because lawyers are at least subject to professional conduct rules, whereas litigation funders in the UK have only a voluntary code of conduct. In a debate in the House of Lords 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 which administers the voluntary code. He went on to remark that “[t]hey [litigation funders] are not even joining their own association, let alone being responsible to any independent and impartial organisation to oversee their work.”<sup>12</sup>
19. In the recent English case of *Excalibur Ventures LLC v Texas Keystone and others*, three 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.<sup>13</sup> None of the three funders, two of which were U.S. companies and the third a company incorporated in the Cayman Islands, were members of the Association of Litigation Funders, and there are doubts over whether one of them even continues to exist.
20. The prohibition contained in the Bill on damages-based agreements in opt-out collective proceedings already appears to capture litigation funding agreements on the basis that they fall within the definition of a DBA

---

<sup>11</sup> Jones Day, *Litigation Funding in Australia: More Swings and Roundabouts as Lawyers Withdraw Application to be Funders* (February 2014), available at: <http://www.jonesday.com/files/Publication/90f16e70-74c5-4c29-9083-f68810f07e66/Presentation/PublicationAttachment/fd611866-6ffa-40be-8961-f76145057184/Litigation%20Funding.pdf>.

<sup>12</sup> Hansard HL Deb 26 February 2013, vol 743, col GC130.

<sup>13</sup> *Excalibur Ventures LLC v Texas Keystone and others* [2013] EWHC 4278 (Comm), paragraphs [24] and [29].

contained in section 58AA of the Courts and Legal Services Act 1990.<sup>14</sup> However, in the absence of case law to clarify whether litigation funding agreements do amount to DBAs, an express prohibition on litigation funding agreements in opt-out collective proceedings should be included in the Bill. The prohibition should also be extended to opt-in collective proceedings to avoid a scenario in which litigation funders rather than claimants become the driving forces behind collective litigation and are incentivised to promote spurious claims.

### Comments on Other Aspects of Schedule 8 of the Bill

#### *Authorisation to act as a representative in collective proceedings*

21. Paragraph 5 of Schedule 8 to the Bill provides that the Competition Appeal Tribunal (the “Tribunal”) could only authorise a person to act as representative in collective proceedings if the Tribunal considered it “*just and reasonable*”.<sup>15</sup> The same condition would apply to the new collective settlement procedure contained in the Bill. It is further proposed that the factors to be taken into account by the Tribunal when deciding whether to authorise a person to act as a representative should be set out in the Tribunal’s procedural rules.
22. In its response to the consultation, the Government stated that claimants or “*genuinely representative bodies*” should be permitted to act as representatives but not law firms, third party litigation funders or special purpose vehicles. ILR understands that the Government intends to publish draft Tribunal rules on collective actions that will address this point. The Bill must be read carefully alongside those draft rules.
23. To ensure that representatives are genuinely representative, the Bill or the Tribunal rules should require at least the following factors to be taken into account:
  - (a) *track record and expertise* – any non-claimant representative (i.e., any representative which is not itself a member of the class) should be required to demonstrate that it has acted in the interests of the parties making up the majority of the class (e.g., consumers) for a number of years and has the relevant expertise to serve their interests;

---

<sup>14</sup> A “damages-based agreement” is defined as “*an agreement between a person providing advocacy services, litigation services or claims management services* [emphasis added] *and the recipient of those services which provides that—(i) the recipient is to make a payment to the person providing the services if the recipient obtains a specified financial benefit in connection with the matter in relation to which the services are provided, and (ii) the amount of that payment is to be determined by reference to the amount of the financial benefit obtained*”. For these purposes, “claims management services” means “*advice or other services in relation to the making of a claim*” including “*the provision of financial services or assistance*” (section 4 of the Compensation Act 2006).

<sup>15</sup> Paragraph 5 of Schedule 8 (new section 47A(8)(b) of the Competition Act 1998).

- (b) *non-profit making character* – non-claimant representatives should not have any financial motive for commencing litigation beyond their desire to obtain redress for those who have genuinely suffered harm;
- (c) *ownership, governance and sources of funding* – to ensure representatives are not merely fronts for profit-making enterprises with an interest in litigation (e.g., law firms, third party litigation funders and claims management companies), the Tribunal should take account of who owns, controls and funds (as applicable) parties seeking to act as representatives;
- (d) *ability to comply with an adverse costs order* – the “loser pays” rule is an important deterrent against frivolous litigation and provides protection to parties who are forced to incur costs responding to cases which ultimately prove to be without merit. To ensure defendants are not deprived of this protection, it is essential that representatives have the financial means to pay defendants’ costs if ordered to do so;
- (e) *previous conduct* – the Tribunal should be permitted to take account of previous conduct, including, for example, whether the person seeking to act as representative has a history of being a vexatious litigant or failing to comply with regulations and codes on direct marketing.

*Eligibility of claims for collective proceedings and choice of opt-in vs. opt-out*

24. It is proposed that claims would only be eligible for inclusion in collective proceedings if the Tribunal considered that they raised “*the same, similar or related issues of fact and law and [were] suitable to be brought in collective proceedings.*”<sup>16</sup> The same condition would apply in relation to the new collective settlement procedure contained in the Bill. It is envisaged that factors to be taken into account when the Tribunal determines whether claims are “*suitable to be brought in collective proceedings*” (but not whether they raise the same, similar or related issues of fact or law) will be set out in new procedural rules. However, ILR considers that given the importance of the certification process for preventing abuse, the Bill should at least specify that as a threshold matter:

- (a) the common, similar or related issues of fact and law should predominate over other issues so that resolving them will go a substantial way to dispensing with all of the claims; and

---

<sup>16</sup> Paragraph 5 of Schedule 8 (new section 47A(6) of the Competition Act 1998).

- (b) there should be a sufficient volume of claims to make individual proceedings impractical.
25. When considering an application for a collective proceedings order, the Tribunal will also have to decide whether, if it grants such an order, it should specify the proceedings as opt-in or opt-out. This decision will be crucial given the greater risk of abuse with opt-out proceedings, yet the Bill is silent on the point and it is unclear whether this will be dealt with in new Tribunal rules. If the Bill continues to include a provision for opt-out proceedings, it should clarify that the burden to be discharged by an applicant for a collective proceedings order will be greater where the order sought is for opt-out proceedings. The applicant should be required to demonstrate the existence of genuine interest in the proceedings, for example by producing evidence of a threshold volume of unsolicited complaints or claims, and give reasons why opt-in proceedings would be inadequate.

#### *Assessment of damages*

26. The Bill proposes that the Tribunal would be permitted to award damages in collective proceedings without assessing the amount of damages recoverable in respect of each individual claim but leaves further detail on the assessment of damages to be dealt with in new procedural rules.<sup>17</sup> To ensure genuine claimants receive a fair amount of compensation and avoid disputes over distributions, the Bill should at least require that any award of damages which is made on an aggregate basis specifies the terms upon which damages are to be divided among class members. In ILR's view, those terms should always require any unclaimed damages to be returned to the defendant.
27. ILR is grateful for the opportunity to provide this evidence to the Committee and should be happy to provide further information about the negative consequences of opt-out collective actions in other jurisdictions, if that would be of assistance.

*February 2014*

---

<sup>17</sup> Paragraph 6 of Schedule 8 (new section 47C(2) of the Competition Act 1998).