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Collective Redress/Class Action: Current Status of EU Directive

On 30 June 2020, the Council approved the agreement between the three European Institutions (Commission, Parliament, Council) on the draft directive on representative actions for the protection of the collective interests of consumers[1]. On the basis of the agreed text the Council will first officially adopt its position which will then be approved by the Parliament. Presently, a date for this formal adoption is not set yet.

Representative actions, i.e. collective redress/ class actions, are relevant for legal protection insurers because they are a form of redress for insured people and have an impact on the financing side of legal proceedings. Therefore, Legal Protection International aisbl centred its Congress 2019 around this topic (about the congress here) and asked Professor Dr Domenik Wendt to look at a particular question in this context: does the free choice of lawyer (Article 201(1)(a) of Directive 2009/138/EC) present an obstacle for legal protection insurers in case they want to finance mass claims procedures? (Prof. Wendt's paper for download here)

Here is a summary of some features of the compromise reached between Council, Commission and Parliament:

Qualified entities (Article 4): as originally foreseen by the Commission, all actions must be brought by so-called Qualified Entities (QE), i.e. consumer protection organisations. In its adapted form, the directive only establishes minimum requirements for QE that intend to bring cross-border actions: a minimum of 12 months actual activity, consumer protection must be the statutory purpose, safeguards to assure independence. If a QE is registered solemnly to bring domestic actions, Member States are free to regulate the requirements (e.g. for domestic actions a Member State can admit ad hoc QEs).

Domestic action (Article 3 (4a) means the QE brings the action in the Member State where it has been designated. Cross-border (Article 4b) action means the QE brings the action in a different Member State other than that where it has been designated.

Actions can be brought if a trader infringes one of 66 different EU consumer protection laws listed in the annex, for instance in the context of the supply of digital content and digital services (Directive (EU) 2019/770), processing of personal data (Directive 2002/58/EC and Regulation (EU) 2016/679), or insurance distribution (Directive (EU) 2016/97).

Available remedies are 1) injunctions (Article 5a) and 2) redress measures (Article 5b): compensation, repair, replacement, price reduction, contract termination or reimbursement of the price.

[1] See the original proposal from April 2018: COM(2018)184

Opt-in: cross-border actions for redress measures have to be subjected to an opt-in mechanism, i.e. Member States must establish that consumers explicitly or tacitly express their will to be or not to be represented be the QE (Article 5b, para. 3). For consumers who are resident in the Member State where the representative action has been brought the opt-in mechanism is not mandatory.

Opt-out: for national consumer actions, Member States are free to determine whether consumers must express their will to be represented in an action for injunction (Article 5a para. 2) or whether an opt-out mechanism applies.

Funding (Article 7) and assistance for QE (Article 15): the compromise text is less detailed than the Commission's draft: Member States must ensure that conflicts of interest are avoided and that third-party funders who have an economic interest in the action are not able to divert the outcome of the action. In principle, while Member States can restrict third party funding, they are encouraged to take measures for publicly funding QEs and/or implementing measures to reduce costs of representative actions.

Loser-pays-principle: (Article 8a): the defeated party in an action for redress must pay the costs of the proceedings but Member States must assure that individual consumers are not burdened with the costs. In essence, this does not solve the problem who pays for representative actions and how these proceedings can be financed.

Jurisdiction, recognition of judgments (Article 10) and limitation periods (Article 11): the compromise directive does not establish which court has jurisdiction. Regarding the effects of final decisions of an infringement, Member States are requested to ensure that judgments on the existence (and non-existence) can be used as evidence in accordance with their national laws. Contrary to the Commission's draft and the text agreed by the Parliament all details in this regard have been dropped. Regarding limitation periods, Member States must ensure that pending actions for an injunction measure have the effect to suspend or interrupt limitation periods. Actions for injunction have to be treated by Member States' courts with due expediency (Article 12) and, in case of a definitive injunction measure prohibiting a practice, the injunction must be treated by way of a summary procedure.

For the compromise text of 30 June 2020 click here.

Judgment of the Court of Justice of the European Union in Case C-667/18

In its preliminary ruling of 14 May 2020, the Court decided that the term 'proceedings' in Article 201(1)(a) of Directive 2009/138/EC[2] (Solvency II) includes any judicial and extrajudicial mediation proceedings in which a court is involved – or is capable of being involved – whether at the initiation or at the end of this procedure. This judgment is precedentary and generally binding not only on the Belgian court on whose initiative the reference for a preliminary ruling was made but also on all of the national courts of the Member States. As a consequence insured persons can oblige insurers to cover lawyer costs during mediation.

In recent years, there have been numerous judgements of the Court of Justice of the European Union revolving around the free choice of lawyer and the meaning of "any inquiry or proceedings"[3] in Article 201(1)(a) of Directive 2009/138/EC. The present judgment confirms the Court's approach of a broad interpretation of the rights of insured persons and even expands its excessive application of the freedom of choice of a lawyer to mediation procedures.

Article 201(1)(a) of Directive 2009/138/EC provides:

"(1) Any contract of legal expenses insurance shall expressly provide that:

[2] DIRECTIVE 2009/138/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 25 November 2009on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II)

[3] See cases: Eschig, C-199/08; Stark, C-293/10; Sneller, C-442/12; Massar, C-460/14; Buyuktipi, C-5/15)

(a) where recourse is had to a lawyer or other person appropriately qualified according to national law in order to defend, represent or serve the interests of the insured person in any inquiry or proceedings, that insured person shall be free to choose such lawyer or other person".

In Case C-667/18 the request was made in proceedings between the Orde van Vlaamse Balies and the Ordre des barreaux francophones et germanophone – the bar associations – and the Ministerraad – Belgian Council of Ministers– relating to the freedom of an insured person to choose his or her representative in mediation proceedings in the context of a legal protection insurance contract. The bar associations sought annulment of a 2017 national law as infringing the Belgian constitution, when read with Article 201 of the Solvency II Directive because the national law does not stipulate that an insured person has the right to choose his or her lawyer for mediation proceedings.

Before that law came into force in 2017, legal protection insurance contracts had to prescribe that the insured person was free to choose a lawyer or other qualified person "when it was necessary to proceed to judicial or administrative proceedings". In 2017, the new law extended the free choice of lawyer to arbitration proceedings, while excluding it for mediation proceedings. Reasons to exclude mediation proceedings were, first, the presence of counsel is not likely to favour mediation and, second, mediation is not necessarily based on legal reasoning. The bar associations, however, argued that, since those proceedings are covered by the term 'proceedings' within the meaning of Article 201, the insured person should have the right to choose a lawyer.

In its ruling whether 'mediation' is caught by the term 'proceedings' in Article 201(1)(a) of Directive 2009/138/EC, the Court of Justice of the European Union was true to its prior verdicts, followed the line of reasoning of the bar associations and stipulated that the right of free choice of lawyer has to be extended to mediation proceedings.

It interpreted the term 'proceedings' just as broadly as the term 'inquiry' in Case *Massar* and considered that any stage, even a preliminary stage, which is capable of leading to proceedings before a judicial body, must be regarded as falling within the term 'proceedings'.

The Court argued that the proceedings can result in an agreement which can become binding and enforceable on request of only one of the parties. Consequently, the effect of the agreement is the same as that of a judgment'[4] and, because the court approving the agreement is bound by its content (except where it is contrary to public policy or to the interests of minor children involved), the role of the lawyer or representative appears even more important than in an inquiry in which the outcome is not binding[5].

Furthermore, the Court of Justice of the European Union states that, since the parties do not have a remedy to alter their positions by means of legal proceedings, the insured person needs legal protection and in view of the effects of the agreement resulting from the mediation being approved, "the interests of the insured person who uses mediation will be better protected if he or she can rely on the right to a free choice of representative [...] in the same way as an insured person who turns to the courts directly may so rely."[6]

It is the author's opinion that the Court misses some important aspects:

Mediation procedures are different than regular court proceedings in the sense of Article 201(1)(a) of Directive 2009/138/EC and therefore require different means to protect insured persons. The underlying principle of mediation is the will of the parties who, with the

[4] Paragraph 36 of the Judgment
[5] See Massar, Case C-460/14, paragraph 28
[6] Paragraph 38 of the Judgment

assistance of a mediator, want to find an amicable solution which meets their particular needs. Contrary to proceedings governed by a person or body (judge, arbitrator, or jury) who decides for the parties, mediation is governed by private autonomy and contractual freedom.

Consequently, in regular court proceedings, it is often necessary for parties to have legal assistance in order to guide them through the relevant laws and assure that they are not deprived of their rights. This information asymmetry, as well as the need to avoid conflicts of interests between the insured and the insurer, are the reasons for the free choice of lawyer in Article 201(1)(a) of Directive 2009/138/EC.

The simple fact that the parties' agreement binds the competent court which approves it and, after having become enforceable, has the same effect as a judgment, is not sufficient for applying the free choice of lawyer to mediation. On the contrary, the enforceability of an agreement makes mediation effective[7] and even if mediation is ordered by a judge or is legally prescribed (judicial mediation), the parties are still free not to agree but to request that the mediation is terminated.

In any case, although the Court argues with the binding effect of an agreement and repeatedly refers to the fact that the request of only one party is needed to make the agreement enforceable, it does not make the lack of legal remedies a condition for mediation to fall under 'proceedings' in the sense of Article 201(1)(a) of Directive 2009/138/EC since it is not mentioned in the verdict tenor which simply states "[…] includes judicial and extrajudicial mediation proceedings in which a court is involved or is capable of being involved, whether when those proceedings are initiated or after they are concluded".

In essence, the Court's judgment will have a counter-productive effect because, firstly, the involvement of lawyers often intimidates adverse parties and therefore impedes the possibility to negotiate and find amicable solutions. Secondly, one of the reasons for choosing mediation, namely because it is more cost-effective and quicker than in-court proceedings (last but not least because parties do not have to pay and involve lawyers), is rendered irrelevant. Thirdly, using the free choice of lawyer as the ultimate means of legal protection in the context of mediation is overshooting the target, because a) it is actually not necessary according to the nature of mediation (to be noted: in general, the approving courts are obliged to check the content of the agreements before approving them) and, b) obliging insurers to cover these costs may easily result in higher costs and/or an exclusion of mediation processes from legal protection coverage.

LPI aisbl will present and discuss the consequences of this judgment for legal protection insurers during an upcoming webinar.

Brussels, 28 October 2020 (Antje Fedderke, LPI Secretary General)

Click here to read the judgment.

United Kingdom:

There are two key developments for legal protection insurers:

1) The implementation of the Civil Liability Act: it has been delayed over the last couple of years but is now meant to come into place in April 2021. One effect is that it will increase the small claims limit and consequently more cases will be taken through the Small Claims' Court for low value personal injuries claims. The effect will be that the Personal After-The-Event market, which is of course quite significant in the UK, shrinks because there is no benefit for solicitors in providing the policy since the lack of costs recovery will mean they will be less keen to run cases at risk in the Small Claims Court. Conversely the Before-The-Event market will boom because the product will pick up the claims left by the ATE

[7] See Article 6(1) of Directive 2008/52/EC (Mediation Directive)

market. This most certainly will result in an increase in premiums. BTE has been under-priced anyway and this will put it back to what it was 10-15 years ago, i.e. it will become much more useful because there will be more engagement with clients. (read more: https://www.gov.uk/government/publications/civil-liability-bill)

2) Coronavirus Act: it was enacted in March 2020 and changed a number of things, for instance, an expansion of the use of video and audio technology for courts and tribunals. Most importantly for legal protection insurers, it has affected the products provided to landlords because evictions have basically been suspended and legal protection products give rent guarantees while evictions are in process. This puts insurers under severe pressure since claims will be much higher. Also, insurers are waiting for a large increase in employment claims as various government schemes supporting businesses will gradually fall away and wholesale reductions in employees will increase. This will have an effect on the products providing employment cover to both businesses and individuals. On the positive side, it will give legal protection insurers an unprecedented opportunity to show how their services work. So the Coronavirus Act will increase the claims costs and affect reserves but at the same time it will mean that people will understand the benefits of the services for the years to come. (read more: https://www.legislation.gov.uk/ukpga/2020/7/contents)

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The Netherlands:

1) Next year the country is expecting a new initiative from car insurers for settling claims from car accidents directly, subsequently motor insurers would handle claims without the intervention of legal protection insurers. The question here is whether this will affect the relevance of legal protection insurers in this particular area.
2) New legislation for solicitors: there are strict regulations for the company structure where solicitors are allowed to work. The system is quite old and prohibitive for the branch and some competitors are testing out the limitations. These changes can bring about new opportunities, shift the boundaries of what is allowed for insurers and can also impact business models.
3) For many years, the government has been looking to save costs for the subsidised legal aid system for people with lower income. But the Corona Virus developments have put this on hold and the government is still searching different business models and also looks into the possibilities legal protection insurers could offer. (read more: https://www.rvr.org/english)

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South Africa:

At present two changes to the regulatory environment in South African will have a significant impact on legal protection insurers, the first being the promulgation of data protection and related privacy laws via the Protection of Personal Information Act (POPIA) and the second being anticipated changes to the Legal Practice Act. With effect from 1 July 2020, responsible parties (known as data controllers in the rest of the world) have one year from the afore-mentioned date to ensure that all processing of personal information conforms to the provisions in POPIA. This will have a significant impact to business processes and operations, in addition to the anticipated costs to ensure compliance. The second regulatory change alluded to relates to the Legal Practice Act and the imperative on the Legal Practice Council (the Regulator) to make recommendations to the Minister of Justice on the statutory recognition of Paralegals and the creation of other forms of legal practice including multi-disciplinary practices and other limited liability practices. LegalWise South Africa was invited by the Regulator to make submissions which was done in April 2020. Such anticipated changes have far-reaching consequences for legal expenses insurers as the de-regulation of the profession would potentially allow insurers to own legal practices and have the entire service

chain with their control, which from a value proposition, servicing and cost point of view would be a game-changer.

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Germany:

The German Insurance Association forecasts a premium increase of 3.3% in 2020 and a combined ratio of 103%, i.e. a rather negative forecast due to the impact of corona. Actually, insurers see it differently: although there was a decrease of business during the lock-down, sales are presently picking up and, so far, there has not been a significant increase on the claims' side. The prospects for 2021 are, however, different because, besides the expected increase in claims spend, an approximate 10% increase in lawyers' fees, which are regulated by law, will have a negative effect on insurers. Particularly, the number of labour law cases are likely to increase significantly and, since Germans like to travel, we also already see an increase in claims related to travel contracts, e.g. cancellations, reimbursement claims for cancelled holidays etc. In this context, online bookings very often complicate the legal assessment because in many cases, for instance if a rented holiday home is located in another country, foreign law applies while people are convinced, since they booked online in Germany that also German law applies. However, this also has a positive side for our business because clients see that they need us.

In the Dieselgate-Case there have been several judgements of the Highest Civil Court (BGH) and we can expect that in Germany claims related to VW will be settled by the end of 2021. Meanwhile however, new claims for damages against other car producers are pursued. Consequently, it is very likely that this topic will remain on the agenda for the time being, also thanks to 'Claims Fishers' who are creative in finding new claim constellations which are brought into court.

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Switzerland:

As everywhere, in 2020, the Corona-Crisis overshadowed all business and was most decisive in Switzerland. We see a 20-30% increase in claims but have been able to handle these claims mainly with in-house staff. Most claims concern labour law and, just like in Germany, travel contracts, cancellations of flight tickets etc. However, presently it is difficult to determine whether this will affect insurers substantially because interventions have not been significant.

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France:

A crucial development in the French market has been that it is finally possible that insurers and lawyers talk to each other in a normal setting. As mentioned repeatedly, in the past couple of years, lawyers and insurers have not had a proper channel of communication but, finally, the national Bar Association and the national Federation of Insurers discussed the matter and were able to strike a consensus which resulted in a Charta. This Charta, which is non-binding, deals with claims settlement, training, enhancement for cooperation and it can be seen as a testament and cross-cutting approach between lawyers and insurers.

In France, it is difficult to quantify the impact of the Corona-Crisis. Regarding the services offered by legal protection insurers, there is an upside and a downside. Many people are seeking insurers' services and there is an increased interest in legal protection which is essential for the business because it has become suddenly very useful not only for answering legal questions but also for getting general support. Consequently, it is possible that the crisis proved to consumers how useful legal protection insurance is in these pandemic times which should improve sales of insurance.

In terms of claims, we see that areas like travel cancellation, labour law, business interruption in the context of restaurants, damages for loss of exploitation prevail. In 2021, we expect a

high number of claims but the downside will be that in many multi-risk professional contracts related to pandemic risks are excluded from cover which will frustrate many insured persons who assume that those loss of exploitation are covered.

In June/July the XerFi-Institute (economical institute that looks at banks and insurance) published a crucial study on legal protection insurance and predicted a sharp decrease for 2021 of 8% in premium income. French insurers doubt very much that the significant market of 1.5 billion € premiums will decrease that much, but rather think that the increase (hovering around 5% per annum) will slow down.

Whatever happens, this crisis will have pushed legal protection insurance companies to accelerate their digital transformation (underwriting, claims, legal information,...) and led to the emergence of new forms of links with policyholders: chat, video, digital hub, ...

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Norway and Nordic markets:

Since, with 5 million inhabitants, Norway is rather small, expansion into the Nordic market, i.e. Sweden and Denmark, is envisaged. The trend is to focus on mandatory schemes like, for instance, those offered to members by trade unions etc.

In Norway and Sweden discussions about costs are ongoing because legal expenditure, in particular for lawyers, are constantly on the rise. This has triggered the regulators to see whether they can introduce regulated fee schemes like in Germany. Insurers hope that this can be introduced quite quickly but, at the same time, in Norway insurers handle claims mainly with in-house staff which makes lawyers' costs less relevant. Overall, if lawyers' fees increase further, e.g. to 300€ and more per hour, consumer see in-house claims handling more positively and as a selling argument for legal insurers who can settle claims more efficiently and at much lower costs. Essentially, lawyers are pressing themselves out of the market because they are overstretching their monopoly while we see in the market that everything is becoming more cost-driven. Consequently, cost cutting and better services, in particular with the help of digitalisation, is becoming crucial in order to remain competitive.

In general, competition in the market is getting fiercer and legal protection for SMEs is picking up, also in Denmark and Sweden.

So far there have not been many consequences of the Corona-Crisis except that people packed-up their PCs in March and stayed home a couple of months. So, now people are back again to business as usual, a sign being that the home buyer market has picked-up and is going sky-high because people buy real estate in the mountains, houses on the sea etc. which is a good market for legal insurers. In essence, the market is quite normal except that everybody sits home.

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Spain:

The post-covid market is different and growth has been less than 3%. The combined ratio shows less than 90% which is artificial after 2 months without any activity during the Spanish lockdown.

Regulators are questioning insurers about solutions and the low combined ratios because they are looking for the real needs of customers and want to find out whether the solutions offered by insurers actually meet customers' needs.

While the market in general appears to be good there are significant differences between the lines of business. While there are not many claims in family law, the situation is quite different when you look at SMEs or real estate lines.

Regarding regulation, there will be a change in the insurance contract clauses where costs for lawyers' fees are presently referred to the fees of the professional association. The supervisory authority requires insurers to change this in order to make the costs more transparent for

clients. A possibility could be to calculate lawyers' fees as a percentage of the claim or amount in dispute. But the outcome of this discussion between insurers and the authorities is still uncertain.

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Czech Republic:

There have been no regulatory changes.

Regarding the financial side, pursuant to the IDD (Insurance Distribution Directive) all intermediaries, selling any kind of financial services, need to take a test before 30 November 2020. This means that ca. 70,000 people need to take this test of which 10,000 to 15,000 tests are still out-standing. At this point, it is rather unlikely that the legal requirement can be met within the set delay and, most likely, the date needs to be postponed.

2020 the Czech market had a good start. In March and April, the market obviously suffered from the Covid Crisis and saw a decrease of approx. 30%. Now we can see an increase of 6% which is due to the fact that DAS was able to conclude a big contract with 2 customers, one being a money bank and the other being a trade union dealing with schools.

Regarding claims we are more or less at the same level as in 2019 because many of our policy holders are transport companies, an area which came to a complete standstill. This means there were less claims, except incoming questions regarding the situations in other countries. However, there were more requests from private customers which were basically concerning travel contracts, flight cancellations etc.

In any case, there is a general uncertainty about what to expect over the next couple of months because the Czech Republic is facing a big crisis and possibly a lockdown after the situation was managed quite well in the beginning of the Covid-19 situation.

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Estonia:

There have not been many new developments, i.e. there is still only one legal protection insurance provider in Estonia. The main portfolio are family contracts while commercial customers are much less important. After selling only stand-alone products, the add-on market is now picking up.

Due to corona, claims have increased by 7%, mostly labour disputes.

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Austria:

Austria had a 2 months lockdown in spring which had quite an impact on the overall situation. The Austrian government released a number of covid-related measures to keep the economy running. Some Covid-19 laws affected the legal life, dealing with the referral of lands and credits, deferments of rents, extensions of legal delays which led to a sharp decrease of legally binding judgments. The government also reduced VAT rates regarding services, food served in restaurants and implemented state support schemes to avoid unemployment. As a result, there was an increased frequency of claims regarding travel and flight cancellations. In particular there was more need for legal advice, i.e. an increase of 20-25%.

However, overall these developments did not have an effect on claims spend because insurance terms and conditions contain a so-called authorities exemption clause. This means that claims related to mandatory regulations and official orders, addressed to a majority of persons in an extraordinary situation, are excluded from cover, which applies to all claims connected to Covid-19 laws. The advantage obviously is that this keeps expenditures for insurers low. On the other side, the disadvantage is that the reputation of legal insurers suffers because people do not get the support they need in a difficult situation. The consumer protection associations have already filed an action against this clause of which the effect is yet to be seen.

Due to the lockdown the production suffered significantly (around 30%) and the challenge was to switch the business of tied agents to a virtual mode in order to continue doing business. This is still a challenge but the goal is to close the gap until the end of this year. In any case, Covid-19 is not over yet. The real challenge will rather be in 2021, especially in the SME market, when state aid schemes come to an end and we'll face insolvencies, bankruptcies and foreclosures which will have an impact on the premium side because increased cancellations of contracts.

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