

LEGAL UPDATE | DISPUTE RESOLUTION

New representative action regime passed into law

On 7 July 2023, Germany's parliament, the Bundestag, passed the Act to implement the EU Representative Actions Directive¹. Until the very end, the Act had been the subject of intense discussions between the coalition parties. The European Commission had meanwhile initiated an infringement procedure against Germany for failing to transpose the Directive into national law on time². The new statutory provisions are to enter into force after the German upper house, the Bundesrat, deliberates on them in autumn 2023.

Content

I. Conditions for the new representative action	2
II. Envisaged timeline for an action for redress measures	5
III. Funding representative actions	7
IV. Suspension of limitation periods	8
V. Disclosure of evidence	9
VI. Outlook and assessment	9
Contact	10

The new law³ will result in a reorganisation of the German collective redress system, which has to date only been rudimentary. The linchpin of the Act is the 'Consumer Rights Enforcement Act' ('VDuG'), which is to implement the Directive's provisions on the institution of a representative action for redress measures mechanism. Since the model declaratory action, which was only introduced in 2018, has not proven to be particularly prolific, the new representative action is intended to eliminate significant deficits of the current legal protection system.

Unlike the model declaratory action, which to date has allowed the courts only to make legal determinations applicable to a large number of plaintiffs, the VDuG introduces a representative action for redress (such as the payment of damages). The redress sought with a representative action is intended to benefit consumers directly, without them having to initiate additional individual proceedings. Consumer protection associations first and foremost will be entitled to file representative actions. The entity bringing the action can choose whether to seek a redress measure, an injunctive measure or merely a determina-

¹ Directive (EU) 2020/1828 of the European Parliament and of the Council of 25 November 2020 on representative actions for the protection of the collective interests of consumers and repealing Directive 2009/22/EC (the "Directive").

² For more detail, see the European Commission's press release dated 27 January 2023, https://ec.europa.eu/commission/presscorner/detail/en/inf_23_262 (last accessed on 16 February 2023).

³ Beschlussempfehlung und Bericht des Rechtsausschusses zum Entwurf eines Gesetzes zur Umsetzung der Richtlinie (EU) 2020/1828 über Verbandsklagen zum Schutz der Kollektivinteressen der Verbraucher und zur Aufhebung der Richtlinie 2009/22/EG (Verbandsklagenrichtlinienumsetzungsgesetz – VRUG) (Recommendation for a decision and report of the Committee on Legal Affairs on the draft of an act to implement Directive (EU) 2020/1828 on representative actions for the protection of the collective interests of consumers and repealing Directive 2009/22/EC (Representative Actions Directive Implementation Act – VRUG)), Bundestag-Drucksache 20/7631.



Content

I. Conditions for the new representative action	2
II. Envisaged timeline for an action for redress measures	5
III. Funding representative actions	7
IV. Suspension of limitation periods	8
V. Disclosure of evidence	9
VI. Outlook and assessment	9
Contact	10

tion under the rules governing the model declaratory action. The Capital Markets Model Case Act (KapMuG), originally set to expire at the end of 2023, has been renewed for eight months and will (at least initially) remain in place alongside the VDuG. A revised version of the KapMuG has been announced for the period thereafter.

Unlike the model declaratory action, which to date has allowed the courts only to make legal determinations applicable to a large number of plaintiffs, the VDuG introduces a representative action for redress (such as the payment of damages). The redress sought with a representative action is intended to benefit consumers directly, without them having to initiate additional individual proceedings. Consumer protection associations first and foremost will be entitled to file representative actions. The entity bringing the action can choose whether to seek a redress measure, an injunctive measure or merely a determination under the rules governing the model declaratory action. The Capital Markets Model Case Act (KapMuG), originally set to expire at the end of 2023, has been renewed for eight months and will (at least initially) remain in place alongside the VDuG. A revised version of the KapMuG has been announced for the period thereafter.

Companies must prepare themselves for comprehensive changes: in addition to the action for redress measures, which can also be brought as a cross-border representative action, the new law provides for innovations in inter alia the third-party funding of the entities entitled to bring these actions, the suspension of the limitation period for the claims asserted and the disclosure of evidence.

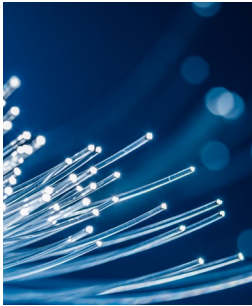
I. Conditions for the new representative action

1. Broad scope of applicability

The Directive limits the mandatory scope of application of the representative action to infringements of certain provisions of European consumer protection law (in particular in the areas of data protection, financial services, energy, environment, telecommunication, health, digital services and product liability). The VDuG goes beyond these provisions and extends the scope of application of representative actions to include *all* civil law disputes between traders and consumers (cf. Sec. 1 (1) VDuG). Thus, claims in tort will also be covered under the new law. This reflects what has been the legal situation to date with regard to the model declaratory action, while expanding the scope of application for actions for injunctions under the German Act on Injunctive Relief (*Unterlassungsklagegesetz*).

For a representative action to be permissible, the association bringing the action must verifiably demonstrate that at least 50 consumers may be affected by the representative action. What legal standard is associated with 'verifiably demonstrate' is an unanswered question. In contrast to the draft version of the Act, which provided for a demonstration to the satisfaction of the court (*Glaubhaftmachung*) pursuant to Sec. 294 of the German Code of Civil Procedure (ZPO), the final version of the provision will likely mean a simplified standard of proof from consumer protection associations' perspective.

In addition, actions brought by capital market investors could also fall within the scope of the Act. To date, these were governed solely by the KapMuG. The VDuG does not address the issue of a potential competition between it and the KapMuG. In any event, it seems



Content

I. Conditions for the new representative action	2
II. Envisaged timeline for an action for redress measures	5
III. Funding representative actions	7
IV. Suspension of limitation periods	8
V. Disclosure of evidence	9
VI. Outlook and assessment	9
Contact	10

conceivable that issuers will see themselves confronted with not just capital investor model case proceedings, but also with redress actions for damages.

Furthermore, as the agreement between the current German Government's coalition partners already provides, the representative action will also be open to small businesses. Small businesses are defined in the Act as businesses with less than 10 employees and with an annual turnover or an annual balance sheet total not exceeding EUR two million (cf. Sec. 1 (2) VDuG). An intrinsic right of trade associations to file representative actions is not provided for in the VDuG.

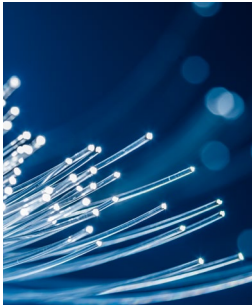
2. 'Similarity' of the claims

One of the central requirements for a representative action to be permissible is that the claims that at least 50 consumers are enforcing by means of the representative action must be similar (*gleichartig*) (Sec. 15 (1) VDuG). This is deemed the case if the claims are based essentially on the same or comparable facts, and the same factual issues and questions of law are essentially relevant for the decision regarding such claims (Sec. 15 (1) nos. 1, 2 VDuG). According to the Act's explanatory memorandum, a degree of similarity is required that allows for a 'template-like' (*schablonenhaft*) examination of the claims. To illustrate the required similarity, the explanatory memorandum lists as examples (1) compensation claims asserted under the European Air Passenger Rights Regulation for one and the same flight and (2) the fulfilment of claims for back payments of interest that arise due to (a bank's) invalid general terms and conditions. The explanatory memorandum does not consider claims to be similar, however, if they become time-barred at different points in time or if they are based to a decisive extent on the knowledge of the actual consumer. The similarity of claims is also deemed to be lacking if not all products of a series are defective, and if it has to be clarified in each individual case whether the relevant product purchased is actually defective or not.

It will be interesting to see how the German courts interpret the similarity requirement. The explanatory memorandum originally suggested a narrow understanding of the term. The fact that the explanatory memorandum of the Act's draft refers specifically to air passenger compensation claims, where individual case-related considerations are hard to imagine, shows the difficulties involved in examining the similarity of the claims. For that reason, during the legislative process, the Bundestag took up a suggestion from the Bundesrat and has now set down that claims must be 'essentially' similar. The intent is that this will enable an appropriate examination on a case-by-case basis. In principle, German courts will have to examine each consumer's claim separately in order to assess similarity. The question of which standard of 'similarity' is to be applied will foreseeably become an issue to be dealt with by the European Court of Justice in view of the importance for the efficient conduct of proceedings⁴.

If the claims are not similar, plaintiffs could opt in favour of filing a model declaratory action or enforcing their claims by way of *de facto* class actions, as has already been done for instance through assignment models. In addition, the filing of several representative actions – each with narrowly defined consumer groups – is also conceivable in order to

⁴ The Directive emphasises that the national rules on the similarity of claims should not hamper the effective functioning of the procedural mechanism for representative actions required by the Directive (recital 12, fourth sentence).



Content

I. Conditions for the new representative action	2
II. Envisaged timeline for an action for redress measures	5
III. Funding representative actions	7
IV. Suspension of limitation periods	8
V. Disclosure of evidence	9
VI. Outlook and assessment	9
Contact	10

ensure similarity. Pursuant to Sec. 13 (1) VDuG and Sec. 260 ZPO, several representative actions may be pursued jointly by way of aggregating the claims. Sec. 7 (1) sentence 2 VDuG makes that explicitly clear.

3. Entities entitled to bring an action

Only registered qualified consumer associations are entitled to bring representative actions (Sec. 2 (1) no. 1 VDuG): in terms of members, associations must have at least 350 consumers or 10 associations from the same field of activity. Likewise, the association must have been registered as a qualified entity for four years. The statutory purpose of the association must be to safeguard consumers' interests. Associations must not aim at making a profit and may not receive more than 5 per cent of their financial resources through donations from companies. Qualified entities from other Member States may have legal standing for the purpose of cross-border representative actions if they are entered in the European Commission's qualified entities list (cf. Sec. 2 (1) no. 2 VDuG).

4. Registration with the register of representative actions (Opt-In)

In line with the legal situation to date, the VDuG provides that consumers must 'opt in': the affected consumers will not automatically become parties to a representative action. Rather, they must actively register with the register of representative actions (*Verbandsklageregister*) in order to join the representative action (Sec. 46 VDuG). This does not come as a surprise. While the Directive does allow for the possibility of introducing an opt-out model along the lines of the US's class action mechanism, the introduction of such a model in Germany has been rejected by the majority of lawmakers. This is due to the German civil-law principle known as the *Dispositionsmaxime*, according to which the parties to proceedings must have the freedom to control all relevant aspects of the proceedings, such as initiating it, selecting its subject matter and terminating it. If the representative action is dismissed by the court, consumers are bound by their opt-in decision and can no longer bring individual actions in the same matter (cf. Sec. 11 (3) VDuG).

Up to three weeks after the conclusion of the oral proceedings, consumers have the right to join the representative action (Sec. 46 (1) VDuG). A ruling cannot be issued until an additional three weeks have passed (Sec. 13 (4) VDuG). The draft of the Act originally provided that any opt-in by consumers must have taken place by the end of the day preceding the start of the oral proceedings. In the course of the legislative process, lawmakers opted in favour of a consumer-friendly provision in this respect. The ability to register at such a late stage gives consumers the opportunity to wait for the proceedings to progress and see if there is any indication in the oral proceedings whether the representative action will be successful. Thus, consumers can wait to see if joining the action is likely to be promising.

5. Filing representative actions in different jurisdictions

With the implementation of the Representative Actions Directive in all EU Member States, consumer associations will have the opportunity to sue companies in different countries. Entities with legal standing will be able to file representative actions outside their own Member State of domicile or together with entities with legal standing in other Member States (as joined parties). Additionally, companies in other jurisdictions may also be con-



Content

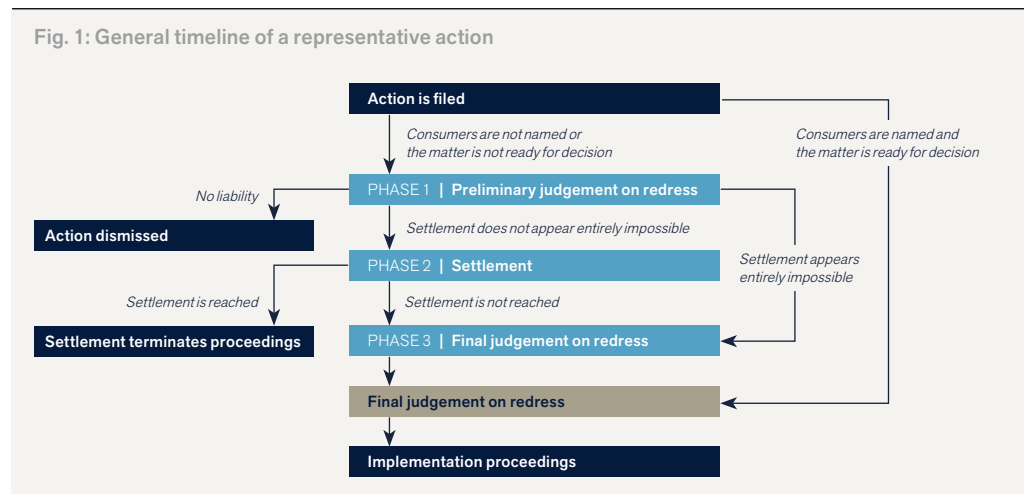
- I. Conditions for the new representative action 2
- II. Envisaged timeline for an action for redress measures 5
- III. Funding representative actions 7
- IV. Suspension of limitation periods 8
- V. Disclosure of evidence 9
- VI. Outlook and assessment 9
- Contact 10

fronted with claims asserted by associations based in those jurisdictions. Representative actions with a foreign element are conceivable primarily in the case of tort claims. For such claims, not only the court at the company's registered office is competent, but also the court at the place where the harm arose. Thus, a claim can be filed wherever damage has occurred.

The requirements and mechanisms of representative actions vary significantly between EU Member States. In cases involving cross-border liability claims, German companies therefore have to expect that they will be confronted in another Member State with a representative action that is based on a far more plaintiff-friendly regime than that applicable in Germany (for example in the Netherlands).

As soon as a representative action against a defendant trader is pending, another representative action may not be brought if its subject matter relates to the same situation of fact and the same claims or to the same declaratory objectives. This helps prevent parallel proceedings from being initiated in Germany that relate to the same subject matter. The Act does not rule out the possibility of parallel representative actions being conducted in other Member States. The permissibility of such actions is governed by the procedural law of the relevant Member State. The Directive merely provides that consumers who have decided to join a representative action cannot 'be represented in other representative actions with the same cause of action and against the same trader' (Article 9(4) of the Directive).

II. Envisaged timeline for an action for redress measures



1. The three phases of the action for redress

The Act divides the representative action for redress measures into three phases (cf. Secs. 16 et seqq. VDuG):

a) Phase 1: Preliminary judgment on redress

In the first phase, the court examines whether the plaintiffs' claims show the required degree of similarity (cf. Sec. 15 VDuG). If the claims are essentially similar, liability is then assessed on the merits of the claims. If the court deems there to be liability, it issues a preliminary judgment on redress (*Abhilfegrundurteil*).



Content

I. Conditions for the new representative action	2
II. Envisaged timeline for an action for redress measures	5
III. Funding representative actions	7
IV. Suspension of limitation periods	8
V. Disclosure of evidence	9
VI. Outlook and assessment	9
Contact	10

In the preliminary judgment on redress, the court sets out the specific criteria according to which the eligibility of individual consumers is determined. The court also specifies what evidence the individual consumer must provide in order to prove they meet the eligibility requirements that the court has also defined. If the action for redress measures seeks a collective total amount, the preliminary judgment will also determine the amount due to each eligible consumer. If the amounts due to the eligible consumers are different, the judgement is to state the method to be used to calculate the individual amounts due to the eligible consumers. If the entity entitled to bring the action is already seeking enforcement of certain claims for the benefit of named consumers, the court may issue a final judgment on redress directly. For that to happen, Sec. 16 (4) VDuG requires that the parties submit a petition to this effect and that the efforts to reach a settlement must have failed.

b) Phase 2: Settlement

After that, the Act provides for a phase in which the litigating parties are given the opportunity to agree on a settlement (Sec. 17 VDuG). The parties are to submit a written settlement proposal to the court on the basis of the preliminary judgment on redress. The purpose of any settlement agreement is for the parties to mutually agree on a verification and distribution system for implementing the preliminary judgment on redress. The explanatory memorandum points out as an advantage that companies will thereby be able to influence not only the implementation of the preliminary judgment on redress, but also the costs arising from the settlement.

c) Phase 3: Final judgment on redress

If the parties do not reach an agreement, the court will issue a final judgment on redress (*Abhilfeendurteil* – cf. Sec. 18 VDuG). In that judgment, the court may order the defendant company to pay a specific collective total amount or it may order implementation proceedings (*Umsetzungsverfahren*) aimed at satisfying the plaintiffs.

In this context, the plaintiffs will have the burden of demonstrating in concrete terms the amount of their total loss. According to the explanatory memorandum, an extract from the register of representative actions can show how many consumers are registered. Additionally, the amount of the claim must be substantiated in concrete terms. Following commonly accepted legal principles, the court is authorised pursuant to Sec. 287 ZPO to estimate the loss. In determining the specific collective total amount, the court may also assume that all claims asserted by the plaintiffs are fully justified.

The respective individual claims will only be examined at the stage of the implementation proceedings. If individual claims turn out to be unjustified, any excess amount is to be reimbursed to the defendant afterwards. This leans more towards being a business-friendly provision. In other jurisdictions, such unclaimed funds often fall to charitable organisations.

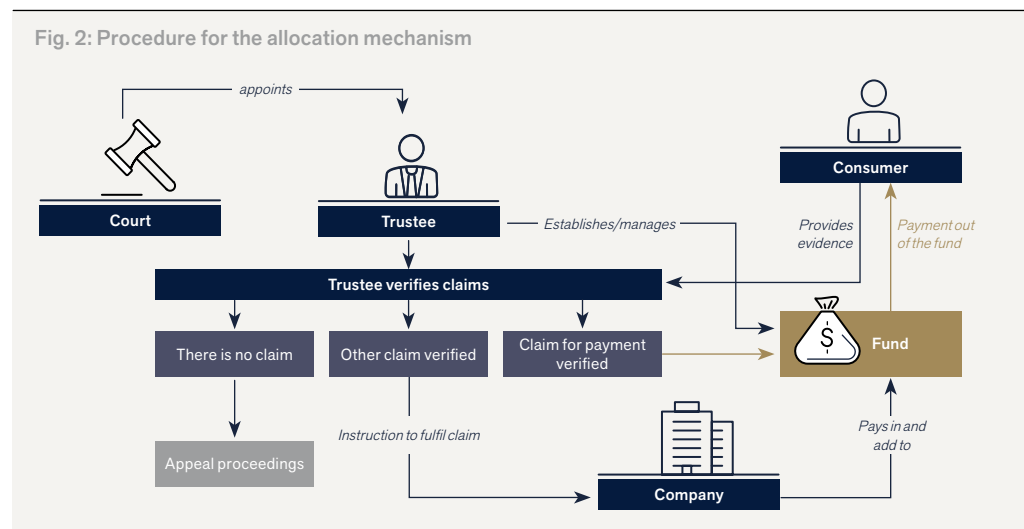


Content

- I. Conditions for the new representative action 2
- II. Envisaged timeline for an action for redress measures 5
- III. Funding representative actions 7
- IV. Suspension of limitation periods 8
- V. Disclosure of evidence 9
- VI. Outlook and assessment 9
- Contact 10

2. The allocation mechanism

The court's judgment on redress is to be carried out by a trustee (*Sachwalter*) appointed for that task by the court (Secs. 22 et seqq. VDuG). The trustee sets up an 'implementation fund' (*Umsetzungsfonds*), in which the defendant is required to deposit the total amount of damages plus procedural costs (Sec. 25 VDuG). The trustee then verifies whether the registered consumers meet the criteria set out in the preliminary judgment on redress (cf. Sec. 27 (1) nos. 3, 4 VDuG). Where a consumer provides the required evidence, they receive a payment out of the implementation fund. In the case of other consumer claims, the trustee requests the defendant to fulfil the specific individual claim, for example make repairs or supply defect-free products, and sets a reasonable deadline for doing so (cf. Sec. 27 (1) no. 5 VDuG).

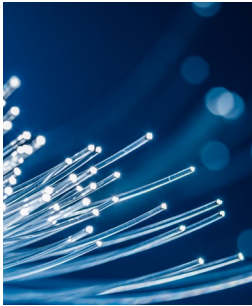


Consumers and companies may file an objection to the trustee's decision pursuant to Sec. 28 (2) VDuG. If the trustee rejects the objection, a court decision may be petitioned (Sec. 29 (4) VDuG). This possibility of the court to have the oversight over the proceedings was added during the legislative process only after extensive criticism had been voiced. If a consumer's claim is not or only partially fulfilled, the consumer will, as a rule, be able to pursue that claim, insofar as it still exists, in an individual action after the implementation proceedings have ended. This applies, however, only if the consumer was unable to enforce the claim previously in the appeal proceedings (Sec. 39 VDuG). If a consumer's claims were wrongfully satisfied in the implementation proceedings, companies must initiate individual recovery proceedings (Sec. 40 (1) VDuG). In those situations, German law on unjust enrichment applies. This could lead to an additional burden on companies with consumer solvency risks that are difficult to calculate.

III. Funding representative actions

The new law leaves it unclear how consumer associations are to finance the proceedings for them to be conducted properly.

For lawyers, representing an association on the basis of the statutory fees is not likely to be attractive. The principles underlying the fee calculation are derived, pursuant to Sec. 18



Content

I. Conditions for the new representative action	2
II. Envisaged timeline for an action for redress measures	5
III. Funding representative actions	7
IV. Suspension of limitation periods	8
V. Disclosure of evidence	9
VI. Outlook and assessment	9
Contact	10

(1) no. 4 VDuG, Sec. 91 ZPO, from the principles set forth in the ZPO and/or the German Court Fees Act (*Gerichtskostengesetz*) and the German Act on the Remuneration of Lawyers (*Rechtsanwaltsvergütungsgesetz*). The amount in dispute in a representative action is capped at EUR 300,000. For fees calculated on the basis of this amount in dispute, it is hardly possible for a lawyer (let alone a team of lawyers) to manage complex and lengthy collective proceedings properly.

Additional remuneration, such as an agreement on hourly rates, is legally possible for the consumer protection associations. However, the question arises as to where the funds for such remuneration are to come from, especially since that remuneration cannot be recovered from opposing parties even if the action is successful.

Third-party funding of representative actions is allowed under Sec. 4 (2) VDuG provided that the litigation funder (i) is not a competitor of the defendant, (ii) it is not controlled by the defendant and (iii) it will not influence the entity entitled to bring the action to manage the lawsuit to the detriment of consumers. However, consumer associations will generally be unable to offer litigation funders market-conform remuneration in the form of a share in the award amount. If an action is successful, a maximum of ten per cent of the total amount sued for may go to a litigation funder (cf. Sec. 4 (2) no. 3 VDuG). Furthermore, if an action is funded by a third party, all the agreements between the consumer association and the litigation funder must be disclosed pursuant to Sec. 4 (3) VDuG.

It remains to be seen whether litigation funders are willing to invest under these restrictive conditions. Until the legislature provides other ways of at least covering the costs of litigation (through additional public funds for instance), the path for most consumer associations to bring numerous and/or major representative actions will likely be blocked for the time being.

IV. Suspension of limitation periods

Actions for redress measures and model declaratory actions trigger a suspension of limitation periods for consumers who have effectively registered in the register of actions (Sec. 204a (1) nos. 3, 4 of the new version of the German Civil Code (BGB). This is consistent with the law to date in relation to model declaratory actions. The limitation period is also suspended by representative actions in other Member States if consumers become a party to them (Sec. 204a (2) BGB).

Representative actions for injunctive measures have a far-reaching suspensive effect on limitation periods (Sec. 204a (1) no. 2 BGB). To date, the requirement has been either that claims for injunctive relief must be pursued individually or that at least the preparations for pursuing such claims must be done individually. The Act has now removed this requirement: any impact on the consumer by a contested infringement is sufficient to suspend the limitation period.

Unlike in actions for redress measures, in a representative action for injunctive measures consumers are not required to declare their intent to participate in the action, for example by registering with the register of representative actions. According to Sec. 5 (2) VDuG, the required impact on consumers would be established solely on the basis of a 'brief description' of the underlying situation of fact. It is debatable whether and to what extent



Content

I. Conditions for the new representative action	2
II. Envisaged timeline for an action for redress measures	5
III. Funding representative actions	7
IV. Suspension of limitation periods	8
V. Disclosure of evidence	9
VI. Outlook and assessment	9
Contact	10

this mechanism will prove to be practical and help provide legal certainty. The limitation period for claims will be suspended for a potentially indeterminate group of consumers. For companies against which such claims are asserted, the legal certainty associated with the statute of limitations is thus drastically reduced.

V. Disclosure of evidence

It is the plaintiff's responsibility to present the facts favourable to the action and to obtain relevant evidence. In the past, this burden has proven to be a considerable hurdle for consumer plaintiffs. The Directive therefore suggests more far-reaching rules on the disclosure of evidence.

The new German Act, however, provides for only modest changes to the current law. An expansion of disclosure duties is not provided for. It therefore remains the case, as applicable law has allowed to date, that a court can only order a party to produce certain, precisely specified evidence.

Sec. 6 (1) and (2) VDuG do, however, newly provide that the failure to comply with a disclosure order can be sanctioned with a fine of up to EUR 250,000, which can be imposed more than once. Whether or not the possibility of a fine will in fact make a difference remains to be seen.

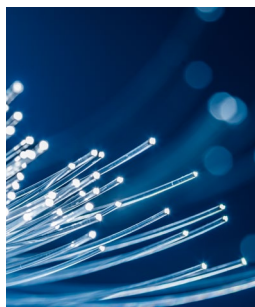
VI. Outlook and assessment

It seems doubtful that the new law will actually lead to a noticeable reduction in the workload of the German justice system. Legal standing is limited to not-for-profit associations, which do not have the option of involving commercially-minded lawyers and litigation funders. Therefore, both law firms representing plaintiffs as well as for-profit litigation funders will likely continue to have incentives to pursue claims (additionally) through assignment models or by bundling a large number of plaintiffs as co-joined litigants.

A considerable hurdle for representative actions will likely be the narrowly defined conditions set out in the Act for lawsuits to permissibly be funded by third parties. Using their own funds, associations will likely only be able to finance complex and costly proceedings to a limited extent. This is true all the more since the statutory fees lawyers can demand are unattractive with the amount in dispute being capped at EUR 300,000.

Liability risks for companies are nevertheless exacerbated by the new legal protection regime. For essentially similar claims (such as claims arising under the GDPR because of data leaks), companies may be facing significant amounts of damages due to potentially very high numbers of affected consumers. The judicial estimation of damages and the open questions surrounding limitation periods will lead to noticeable liquidity burdens and legal uncertainties for companies, in particular with regard to provisions. From the defendant company's perspective, the amount of damages will be unclear until all of the claims have been satisfied. The judicial estimation of damages is only preliminary and can be increased if the amount is insufficient.

In summary, the representative action is an expansion of consumer protection associations' repertoire to challenge companies. It remains to be seen how greatly the tool will be utilised.



Contact



Maximilian Bülau
Partner | Frankfurt
maximilian.buelau@hengeler.com



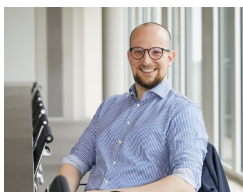
Philipp Hanfland
Partner | Frankfurt
philipp.hanfland@hengeler.com



Mathäus Mogendorf
Partner | Berlin
mathaeus.mogendorf@hengeler.com



Anja Meier-Hoffmann
Associate | Berlin
anja.meier-hoffmann@hengeler.com



Roman F. Kehrberger
Associate | Frankfurt
roman.kehrberger@hengeler.com



Hedger Roisenwasser
Associate | Berlin
hedger.roisenwasser@hengeler.com



Megan Schrader
Associate | Frankfurt
megan.schrader@hengeler.com

> www.hengeler.com