

German Government Releases Draft Act on Class Actions in Germany

IN SHORT

The Situation: As agreed in the [Coalition Contract of the current German government](#), the Federal Ministry of Justice officially presented the Act on Model Declaratory Proceedings ("Draft Act") on May 9, 2018, after protracted last-minute negotiations within the government.

The Plan: The Draft Act, if ratified, would give qualified institutions the right to raise claims on behalf of groups of consumers in order to obtain a declaratory judgment. The plan is to enact the Draft Act by November 1, 2018.

Looking Ahead: The [European Commission has issued a proposal](#) along the same lines, and its suggestions go far beyond the draft provided by the German government. Germany is therefore already under pressure to anticipate the next legislation in this regard, even though the Draft Act has not even been enacted yet. It is therefore expected that extensive—potentially divergent—actions will be taken on Member State and EU level in this area of law.

Presented by Germany's Federal Ministry of Justice, the Draft Act, if ratified, would grant qualified institutions the right to bring class actions for groups of consumers in order to attain a declaratory judgment. Enactment of the Draft Act is planned for November 1, 2018.

The Draft Act's Core Elements

An action in relation to a claim or legal relationship between a consumer and a company may be raised by any qualified institution that has been registered for four years under the German Injunctive Relief Act or (if foreign) with the European Commission under Directive 2009/22/EC. Further, the institution must consist of 10 associations or 350 natural persons. It may not receive more than 5 percent of its financial means from corporate entities and may not raise model proceedings in order to make profits.

In order to initiate the claim proceedings, the consumer association needs to demonstrate that it represents 10 identified consumers that are affected. The initiation of the proceedings does not prevent consumers from filing individual claims. Once a model proceeding has been initiated, no further model proceedings may be commenced based on the same set of facts against the same defendant.

To have the proceedings executed in court, 50 applicants must access the claim by registering their claims with the claims register within a time frame of two months.

Any consumer affected by the alleged wrongdoing has the right to join the ongoing model proceedings by registering his or her claim at least one day before the oral hearing. Any consumer who has already joined the model proceedings may withdraw from the proceedings until the same point in time.

Model proceedings are terminated either by the court's issuance of a declaratory judgment or by means of settlement.

The court's declaratory judgment findings have binding effect for any consumer who accessed the proceedings before the oral hearing. On the basis of these findings, the consumer may initiate an individual proceeding for damages.

Alternatively, the qualified institution may settle the claim on behalf of all registered consumers. Any settlement must be approved by the competent court, which will grant approval if the agreement between the parties constitutes an "adequate amicable settlement." The settlement becomes valid unless 30 percent or more of all consumers registered explicitly opt out of settlement.

Assessment

The right to initiate a model proceeding is granted to any qualified institution registered under the Injunctive Relief Act (*Unterlassungsklagegesetz*) or Directive 2009/22/EC. The question of who should have the right to initiate a claim was highly disputed in the preparation of the Draft Act, as there is a legitimate concern that the right to sue may be abused.

The current draft shows that certain limitations on the right to sue were implemented. In particular, the requirement that a qualified institution has been registered for four years will prevent the creation of such institutions merely for the sake of being able to file model proceeding claims. However, these limitations do not fully eliminate the concern that an eligible qualified institution might team up with third-



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party funders and/or law firms that specialize in class action or group claims. Such a combination could be highly profitable for the law firm or litigation funder and, at the same time, would not affect the qualified institution's right to sue. The Draft Act therefore drastically increases litigation risks for consumer-facing companies.

Further, the rationale behind the Draft Act was to enhance consumer rights by overcoming the so-called "rational lack of interest" that a consumer faces when presented with filing an expensive claim for a small damage amount. However, under the Draft Act, any consumer would still need to complete a two-step process. First, the consumer would have to initiate or accede to a claim filed by a qualified entity in order to obtain a declaratory judgment. Second, the consumer would have to file a separate, follow-on claim for damages.

It is doubtful whether consumers will want to go through such a cumbersome process for small amounts of damages. Consequently, neither consumers nor consumer-facing companies seem to be better off with the Model Proceedings Act.

TWO KEY TAKEAWAYS

1. Under the Draft Act, it is expected that qualified institutions will team up with law firms that specialize in class action claims and with litigation funding companies so that they may file model proceedings, particularly against well-funded companies. At the same time, it is questionable whether consumers will actually profit from the model proceedings filed in their name.
2. Further far-reaching changes are to be expected in the area of collective redress in Germany and the European Union, as the European Commission is already pushing for the implementation of further consumer rights in this area.

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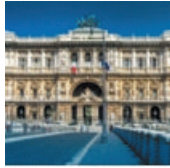
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