Are cases too good to litigate? Cost recovery in antitrust collective actions in the UK

Adrian Render & Sebastian Peyer

A. Introduction

The UK's nascent opt-out collective action regime has got off to a slow start. Since opt-out collective actions were introduced with the Consumer Rights Act (CRA) at the end of 2015, the Competition Appeal Tribunal (CAT) has heard two applications for collective proceedings orders.[1] Two more applications relating to the same infringement were filed in 2018 and another three in 2019.[2] The modest uptake of the new collective action regime has a number of reasons. Like any area of law with new rules, courts and tribunals need to settle on the interpretation of the legal requirements for class certification – a process that inevitably leads to appeals and costly delays. A main reason for the slow start, however, is the uncertainty over funding agreements and reimbursement of success fees.

To enable opt-out collective actions, the class representative usually requires some sort of external funding. Litigation funding is provided if there is a prospect for the funder to recover a success fee from a successfully litigated claim. This raises the question of if and how the funder of a collective action can claim a success fee. The only explicit arrangement for fees in opt-out collective actions can be found in section 47C(6) of the Competition Act 1998 (as amended by the CRA) and CAT Rule 93(4), the latter restating section 47C(6). These rules provide a route for costs and success fees to be recovered after the class members have received their damages, i.e. reimbursement *post-distribution*. CAT Rule 93(4) seemingly relies on a scenario in which damages cannot be completely distributed to all members of the class, i.e. it requires a sufficiently large amount of undistributed damages from which the funder can claim its success fee. If the class representative can (almost) perfectly allocate victims and distribute damages, the obvious risk is that there are insufficient undistributed damages to satisfy the funder's success fee or solicitor's uplift from a conditional fee agreement (CFA). Consequently, allocating funders' fees post-distribution severely reduces the incentives to fund claims in the first place if there is little or no prospect of left-over damages after distribution to the class. This is particularly likely in scenarios with smaller and/or readily identifiable groups of claimants represented.

We demonstrate that the narrow, post-distribution view on funders' and solicitors' reimbursement is problematic and that a wider approach has been, and indeed should be, taken. We will show that it was not Parliament's intention to limit recovery of success fees to just post-distribution, and the CAT has evidently not interpreted Rule

[1] In *Dorothy Gibson v Pride Mobility Products Ltd* [2017] CAT 9, the applicant ultimately withdrew the application after the CAT required a better definition of the class. In *Walter Hugh Merricks CBE v Mastercard Inc* the applicant successfully appealed against the CAT's initial rejection in the Court of Appeal and the case is still pending [2017] CAT 16; [2019] EWCA Civ 674.

[2] Case 1282/7/7/18 *UK Trucks Claim Limited v Fiat Chrysler Automobiles N.V.*; Case 1289/7/7/18 *Road Haulage Association Limited v Man SE and Others*; 1304/7/7/19 *Justin Gutmann v First MTR South Western Trains Ltd*; 1305/7/7/19 *Justin Gutmann v London & South Eastern Railway Ltd*; 1329/7/7/19 *Michael O'Higgins FX Class Representative Limited v Barclays Bank PLC and Others.*

93(4) to be the only way that success fees can be recovered. When the existing case law is analysed, it is clear that pre-distribution costs recovery is present in all opt-out cases brought thus far. Limiting recovery to post-distribution would also create a clear conflict of interest on behalf of the class representative. The representative must act in the best interests of the class, i.e. making sure that damages are distributed as effectively as possible, but would also be contractually obliged to ensure that there are sufficient undistributed damages to be returned to the funder. A perverse consequence of limiting recovery of funder's fees to post-distribution is that claims with a particularly good prospect of damages distribution are not being brought for lack of financial incentives. The risks of not being (sufficiently) reimbursed are likely to cause concern in the litigation funding market, and are preventing good cases with identifiable class members from being brought.

The article is structured as follows: in the next section, we will briefly outline the current rules for cost and fee recovery; in part C, we will demonstrate that funders' fees can be recovered pre-distribution and that this is particularly important in cases with little or no damages left post-distribution; we will deal with some of the criticism against such interpretation in part D; and conclude in part E.

B. The problem: Cost recovery in successful collective actions with substantial distribution

In this section, we will outline the framework that governs fee recovery in successful collective actions and highlight the misunderstanding regarding uplifts and funders' fees that currently exists. Opt-out collective actions usually require an external source of funding due to the considerable cost of the class action process. In the *Merricks* action, the certification process in the CAT – excluding appeals and further hearings – cost the defendant ca. £1.99 million whereas the applicant spent ca. £1.75 million.[3] These expenses are incurred before disclosure and trial. The class representative will normally enter into a funding agreement with a third party where the latter finances litigation expenses up to a predetermined limit.[4] The lawyers may also enter into a CFA with the class representative where they charge an uplift (success fee) in addition to base costs if the claim is successful (or a combination of the two financing methods).[5] It is clear that the litigation-funding model is based on the anticipation that a successful case will enable the funder to recover its costs and receive a fee (profit). However, success fees are no longer part of the recoverable costs that the successful claimant is entitled to receive from the defendant.[6] Any success or funder's fee must be paid out of the damages.

[3] *Walter Hugh Merricks CBE v Mastercard Inc* [2017] CAT 27.
[4] Funding arrangements can also include after-the-event (ATE) insurance to (partially) cover potential liability for the defendant's cost.
[5] Damages-based agreements (DBAs) are not permitted in opt-out collective actions. Section 47C(8) Competition Act 1998. For conditional fee agreements in general, see section 58 of the Courts and Legal Services Act 1990.
[6] Section 58A(6) of the Courts and Legal Services Act 1990 as amended by the Legal Aid, Sentencing and Punishment of Offenders Act 2012.

If a lawyer enters into a CFA with an individual claimant, the claimant agrees that the success fee is taken out of the damages award before it is paid out to the claimant, i.e. before distribution. With regard to collective actions in competition law, the situation is more complex because fee recovery appears to be limited to post-distribution according to section 47C(6) of the Competition Act 1998 and CAT Rule 93(4). As we will show below, this apparent restriction is not what the legislation intended and, if construed as such, would produce results that are against the spirit of the UK's collective action regime and Parliament's intention.

CAT Rule 93(4) reads

> *Where the Tribunal is notified that there are undistributed damages in accordance with paragraph (3)(b), it may make an order directing that all or part of any undistributed damages is paid to the class representative in respect of all or part of any costs, fees or disbursements incurred by the class representative in connection with the collective proceedings.*

CAT Rule 93(4) suggests that in collective actions success fees are to be paid after damages have been distributed to class members. This means that funders are only to make a profit if the distribution of damages is not perfect. This creates perverse incentives for funders.

Imagine a case that requires costs funding of £1m for a £5m damages claim. The case is fully successful, £5m damages are awarded and the claimant (funder) recovers 70% of costs, i.e. £700,000, from the losing defendant.[7] The class representative distributes £4m of the damages. The funder recovers its £300,000 shortfall regarding costs and its success fee from the undistributed damages (£1m), according to CAT Rule 93(4). This scenario is most likely when classes are large with many members that cannot be identified (*Merricks*, for example, is a claim on behalf of ca. 46 million individuals).

If, however, there is a reasonable prospect that the class representative is able to distribute all or substantially all of the £5m damages, the incentives for the funder change dramatically if recovery is limited to post-distribution. The funder, having taken the risk of the substantive claim, also takes the risk that that there might not be sufficient undistributed damages from which to recover the £300,000 shortfall let alone a return on investment. In this example, the funder loses £300,000 for having brought a successful claim and having successfully distributed the class's damages. Thus, construing CAT Rule 93(4) as being the only way that costs and fees are recovered (post-distribution) diminishes incentives to fund claims that have a very good prospect of winning and substantial damages distribution, which is exactly the type of claim that should be encouraged.

In the 'full distribution' example, the incentives to fund collective actions change with pre-distribution recovery: the funder recovers its £300,000 plus its return on investment and the class receives £4.7 million, agreed by the class representative and sanctioned by the CAT at class certification, whereas with no pre-distribution recovery the class recovers nothing.

[7] CAT Rule 104(2) gives the CAT discretion regarding cost orders. The CAT will order the reimbursement of 'reasonable and proportionate' costs which is normally less than full cost. See, for example, *Walter Hugh Merricks CBE v Mastercard Inc* [2017] CAT 27 (cost ruling).

No funder would risk investing in a successful case when they might lose money. If they did undertake the risk in a case with a good prospect of damages distribution and no pre-distribution recovery, it is easy to imagine the arguments that defence counsel would make in respect of the conflict of interest between acting in the best interests of the class (perfect distribution) and the funder's interests (left-over damages).

Where the take-up of damages by claimants is likely to be high (which will often be the case where there is a 'good' case), funders will simply not accept the risk. As a result, good cases will not proceed, the claimants will recover nothing, and the objective of the opt-out procedure will not be satisfied.

It could be said that in class actions there are 'always' substantial undistributed damages from which success fees can be paid. This is a misnomer - the vast majority of class actions in other jurisdictions have a few hundred to a few thousand class members, where class members are readily ascertainable.[8] In *Mobility Scooters*, for example, the 32,000 class members would have been ascertainable, which was a strength of the case. If funders had been involved in the *Mobility Scooters* case, it is likely that it would not have been brought.

C. The solution: pre-distribution recovery of cost and fees

As we have demonstrated above, Rule 93(4), if interpreted as the only way that costs can be recovered, creates a situation in which 'good' cases (from a distribution point of view) are unlikely to be brought and 'bad' cases (with less effective distribution) are more likely to be brought. In this section, we show that the seemingly narrow scope of Rule 93(4) has no support in the genesis of Rule 93(4), is not supported by the CAT's practice and could breach the EU principle of effectiveness if Articles 101 or 102 TFEU are concerned.

Below we follow a time-line approach to show how section 47C(6) and Rule 93(4) came into being. We will then analyse the opt-out case law and how Rule 93(4) has been interpreted. Adopting this approach the reader will be able to follow the development in the government's approach to costs recovery and how this approach has been applied in the cases. Our analysis shows that Rule 93(4) is a clarification meant for the special case of undistributed damages – a scenario that only occurs in opt-out collective actions where some victims may be unknown. It was Parliament's intention that costs would be recoverable in the normal manner, i.e. pre-distribution, and that Rule 93(4) is an additional way for costs to be recovered.

[8] E.g. Bruce I. Bertelsen; Mary S. Calfee; Gerald W. Connor, "The Rule 23(b)(3) Class Action: An Empirical Study" (1974) 62 GEO. L. J. 1123; Deborah R. Hensler, "The Future of Mass Litigation: Global Class Actions and Third-Party Litigation Funding", (2011) 79 GEO. WASH. L. REV. 306, 313. See also Department for Business, Innovation & Skills, *Private Actions in Competition Law: A Consultation on Options for Reform* (BIS/12/742, April 2012) ('Government Consultation 2012') at [5.19].

I. The Government's Consultation on private enforcement of competition law

The Government consulted on the collective action regime between April and July 2012 (the 'Consultation').[9] At various points in the Consultation the Government referred to unclaimed damages and the distribution options,[10] but never that this would be how costs are recovered.[11] The Consultation was only concerned with the special case that a damages award is being made that cannot fully be distributed to the class. In this context, the Government made it very clear that the purpose of private opt-out collective actions is to 'deliver redress to those who have suffered loss.'[12] When asking for stakeholder responses as to what should happen with undistributed funds, the Government proposed a number of possibilities: (i) *cy-près*, (ii) *escheat* to the Treasury, (iii) reversion to the defendants, (iv) distribution to a named scheme (including the Access to Justice Foundation), and (v) claimant-sharing (where unclaimed damages are shared amongst those class members who have made a claim).[13]

The Government published its Response to the Consultation submissions in January 2013.[14] On the question of how to deal with unclaimed funds, stakeholders were divided but none of the respondents treated this as a cost recovery issue or suggested that costs be paid out of the unclaimed pot.[15] A majority of the respondents were in favour of distributing unclaimed sums to the Access to Justice Foundation and the Government adopted this approach.[16]

> *The Government [ ] decided that any unclaimed sums must be paid to the Access to Justice Foundation, though leaving defendants free to settle on other bases, including on a cy-près or reversion-to-the-defendant basis, subject to approval by the CAT judge.*[17]

What is striking about the Government Consultation is that there was no mention that costs would be payable out of unclaimed damages. It is clear that the Government and stakeholders were only concerned with the distribution of funds that were left over. The purpose of section 47C(6) and, thus, CAT Rule 93(4) was not to limit cost recovery to post-distribution but to make sure that unclaimed funds are distributed in an orderly fashion. Since there are no other explanations regarding cost recovery in collective

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[9] The consultation documents are available at https://www.gov.uk/government/consultations/private-actions-in-competition-law-a-consultation-on-options-for-reform.
[10] Government Consultation 2012, at [5.34], [A.17], [A.34] and A.[37].
[11] Government Consultation 2012, Table 6 at [5.34]. At [A.11] the Government discusses cost shifting.
[12] Government Consultation 2012, at [A.34].
[13] Government Consultation 2012, at [A.34].
[14] Department for Business, Innovation & Skills, *Private Actions in Competition Law: A Consultation on Options for Reform – Government Response* (BIS/13/501, January 2013) ('Government Response').
[15] Government Response, at [5.46-5.51].
[16] Government Response, at [5.46].
[17] Government Response, at [5.70].

actions, it leaves only one possibility: that the normal practices of cost recovery apply, namely that they are recoverable from the damages received.[18]

II. The Consumer Rights Bill

Schedule 8 of the Consumer Rights Bill ('Private actions in competition law') is the direct result of the Government Consultation. In implementing the Government's approach, Schedule 8 proposed that unclaimed funds in opt-out collective actions are paid out to charity. When the Consumer Rights Bill was first tabled for debate in the House of Commons what became section 47C(6) was not present.[19] Section 47(c)(5) of the Consumer Rights Bill read:

> *Where the Tribunal makes an award of damages in opt-out collective proceedings, any damages not claimed by the represented persons within a specified period must be paid to the charity for the time being prescribed by order made by the Lord Chancellor under section 194(8) of the Legal Services Act 2007.*[20]

Thus, in the original Bill there was no express provision for lawyers or funders being paid at all. Stakeholders treated undistributed damages as a distribution problem rather than a rule meant to allocate costs and fees. By the time the second version of the Bill was placed before Parliament,[21] the amendment that is now section 47C(6) had been added and became part of the CRA.[22] This amendment allowed cost and fee recovery out of unclaimed funds.

The then Parliamentary Under-Secretary of State for Business, Innovation and Skill, Jenny Willott, stressed that the amendment is *one option* to fund opt-out class actions, i.e. making clear that there are other ways of funding and cost recovery. The reason for the addition given to the House of Commons is worth repeating:

> *One option to fund opt-out cases would be to use unclaimed damages to cover all or part of a claimant's costs, which could include any success fee agreed with a legal representative and any insurance taken out. It is imperative that consumers should be the beneficiaries of redress, and the amendment will mean that legal costs can be recovered only after consumers have claimed their redress. It is also right that any amendment on collective redress does not undermine the safeguards that are essential to the regime.*
> *First, if there are cases that do not result in any unclaimed damages, the representative will not be able to recover their legal costs from the damages pot. Secondly, businesses will not be paying any additional redress; they will*

[18] There is a second possibility that costs and success fees are not to be recovered at all but this would contradict the purpose of the regime which is to encourage recovery.
[19] Consumer Rights HC Bill 2013-14 [161], 23 January 2014.
[20] Available from https://publications.parliament.uk/pa/bills/cbill/2013-2014/0161/cbill_2013-20140161_en_12.htm#sch8.
[21] Consumer Rights HC Bill 2013-14 [180], 14 March 2014.
[22] Consumer Rights HC Bill 2013-14 [180], 14 March 2014.

> *still be paying only for the harm that they caused. Thirdly, the use of unclaimed damages to pay costs will have to be approved by the CAT.*
> *The amendments are integral to ensuring that consumer bodies and bodies for small and medium-sized enterprises will be able to fund collective action cases. Without them, it would be difficult for consumer bodies to bring a case.*[23]

To paraphrase the amendment therefore, the section 47C(6) route is <u>one</u> option for funding; the rest of the explanation sets out how this additional route to funding would work, and that it would be based on the condition that this additional route would be triggered only after class members have received their damages. There is no reference to this being the only route to payment, nor is there a reference to the previous situation whereby, without the amendment, lawyers and funders would not be paid at all, according to the argument that section 47C(6) is the only route to receive payment.

The Bill's debate in the House of Lords confirms this view, and explains in greater detail the reasons for the adoption of section 47C(6).[24] It becomes obvious that this addition to the Consumer Rights Bill was not meant to limit the pre-distribution recovery of cost and fees but was motivated by the cost arrangements that exist for *pro bono* actions under section 194 Legal Services Act 2007. Lord Phillips of Sudbury, then president of the Solicitors Pro Bono Group, explained that the amendment was designed to "bring these limited advances in the [Consumer Rights] Bill under the regime established by section 194 of the Legal Services Act 2007."[25]

Without section 194 the 'costs' of *pro bono* representation would not be recoverable. In the words of Lord Phillips: "[I]f you are acting for nowt you cannot get costs because you are [charging nowt]. That was thought to be unreasonable, so section 194 provided that the costs that would have been recoverable had the advocate not been acting *pro bono* but normally should be payable to a charity nominated by the Lord Chancellor."[26] Thus, section 47C(6) is designed to provide a similar costs recovery for *pro bono* representation:

> *[The] new Section 47C(6) allows the tribunal to order unclaimed damages to go towards the pro bono lawyer representing the collective claimants, for his or their costs*.[27]

Debated alongside 'the new Section 47C(6)' was an amendment to the Enterprise Act, which dovetails with section 47C(6), and confirms beyond doubt that the amendments were to provide compensation for *pro bono* representation:

> *Tribunal rules may make provision—*
> *...*
> *"(ha) allowing the Tribunal to order payments in respect of the representation of a party to proceedings under section 47A or 47B of the 1998 Act, where the representation by a legal representative was provided free of charge;*[28]

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[23] Consumer Rights Bill Deb Tuesday 11 March 2014, cols 588-589 (emphasis added).
[24] HL Deb 03 November 2014, vol 756, col 562.
[25] HL Deb 03 November 2014, vol 756, col 584.
[26] HL Deb 03 November 2014, vol 756, col 585.
[27] HL Deb 03 November 2014, vol 756, col 586.
[28] The amendment to paragraph 17 of Schedule 4 to the Enterprise Act 2002 (s 32 CRA 2015).

New sub-paragraph (ha) was in the initial draft Bill (section 32 of Bill 161 tabled on 23.1.14) - the same version that did not have what is now section 47C(6) – and instructed the CAT to make a rule permitting *pro bono* payments, but there was no underlying power to actually make the payments, hence the addition of section 47C(6).

Baroness King of Bow confirms Lord Phillip's view that section 47C(6) was added with pro bono representation of class action claimants in mind:

> *As we have seen, [the Amendment] allows money not claimed in opt-out collective proceedings to be paid to charity, and permits any money remaining after that to go to pro bono lawyers. That is also the substance of several of the amendments tabled … which, as we have heard, would allow lawyers who have worked for free in successful cases on behalf of consumers to get paid.*[29]

The debates in the House of Lords confirm that section 47C(6) is designed to provide some compensation to *pro bono* lawyers in accordance with section 194 Legal Services Act 2007. It is not meant to regulate cost and fee recovery in general. Our argument that the explicit funding arrangements post-distribution are meant for the specific case of *pro bono* litigation is supported by CAT Rule 104(1). It extends the definition of recoverable costs and expenses to those incurred "where the representation by a legal representative was provided free of charge".

The clearer debates in the House of Lords help to better explain Willcott's statement that the possibility of no damages being available to pay the representative would encourage litigation. In the context of *pro bono* representation it would encourage litigation, as there *is a chance* for funds to be left over. The *pro bono* litigant is likely to litigate even with no costs recovery - if there are no funds left over, the lawyers are in the same position because *pro bono* litigation is not pursued for profit. However, applying Wilcott's argument (and section 47C(6) itself) to private enforcement for profit does not make any sense. With the prospect of no profit (or a loss), no lawyer or funder would attempt expensive and risky litigation. Thus, as we have shown, section 47C(6) is not meant to apply to for-profit private enforcement.

III. Section 47C(6) and CAT Rule 93(4) in Practice

Thus far there have been three opt-out cases where the funding arrangements are publicly known, each having shown that unrecovered costs and success fees can be recovered out of undistributed damages. More importantly, the CAT's practice shows that costs and success fees could have been (or could be) taken pre-distribution – although the CAT has not directly addressed the issue 'head-on'.

The *Mobility Scooters* funding arrangement provided that the CFA success fee would only have been recovered pre-distribution of damages. The issue of funding was given no more than a cursory glance - less than a single page in the collective proceedings order (CPO) hearing transcript.[30] The lawyers were on a CFA and the ATE (after the

[29] HL Deb 03 November 2014, vol 756, col 587 (emphasis added).
[30] *Dorothy Gibson v Pride Mobility Products Ltd*, Transcript of CPO Application hearing (Day 3) 14 December 2016, p. 34.

event) premium was fully deferred, i.e. it would only be paid if the case was ultimately successful.[31] Therefore, with no objections from defence counsel or from the CAT, it is highly likely that the pre-distribution CFA success fees would have been approved had the case proceeded.

The CAT had a second chance to comment on *Mobility Scooters*' pre-distribution success fee recovery in the oral argument in *Merricks*, but did not.[32] Unlike *Mobility Scooters*, Merricks had proposed a different, two-stage recovery process where it must win (step 1) and then there must be money left over for recovery of the success fee (step 2).[33] However, the CAT was reminded of the pre-distribution arrangement in *Mobility Scooters* since Merricks referred to the *Mobility Scooters*' CFA and drew a distinction with its two-stage recovery process. Unlike the funding arrangement in *Mobility Scooters*, the Merricks litigation funding agreement ('LFA') was drafted on the basis that the funder's success fee would be recovered from the undistributed damages only. It is important to stress that the funder *could have* sought all or partial payment of the success fee pre-distribution, but chose not to do so: "the Funder has agreed completely to ring-fence the successful damages award in so far as it is collected by the class members".[34] Neither the CAT nor defendants commented on this choice – not to take any success fee pre-distribution – being available.

At the class certification hearing in *Merricks*, Mastercard argued that "costs or expenses" in section 47C(6) cannot cover a liability to pay the fee of a third party funder.[35] The CAT rejected this reading:[36]

> *[Section] 47(c) introduced new and distinct provisions concerning the costs of collective proceedings […] if a third party agrees to [fund] litigation, the payment which has to be made to that third party in consideration of this commitment, whether out of the damages recovered or otherwise, is a cost or expense incurred in connection with the proceedings.*

The terms of the *Merricks* LFA required the CAT to only consider post-distribution recovery according to Rule 93(4) and section 47C(6).[37] However, the judgment is useful as it is clear that the CAT considered Rule 93(4) to be *one of several possible routes* to recover success fees. The CAT's reference to 'otherwise' shows an acknowledgment that the reimbursement of success fees is not limited to post-distribution under Rule 93(4).

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[31] Ibid.
[32] *Walter Hugh Merricks CBE v Mastercard Inc*, Transcript of CPO Application Hearing (Day 3), 20 January 2017, p. 10-11.
[33] As we have argued above, collective proceedings with a large number of individuals represented in the claim are more likely to result in undistributed damages. *Merricks*, with a class of ca. 46 million individuals, is a typical case where seeking reimbursement out of left-over funds makes sense as the funder can expect incomplete distribution of the award should the claim be successful.
[34] Merricks Reply to Mastercard of 15. December 2016 at [84] available at https://mastercardconsumerclaim.co.uk/Content/Documents/Merricks%20Reply%20to%20Mastercard.pdf.
[35] However, the defendants conceded that the cost of an ATE insurance premium can be paid out to the class representative under s 47C(6), i.e. it can be paid out of left-over funds.
[36] *Walter Hugh Merricks CBE v Mastercard Inc* [2017] CAT 16 at [115] (emphasis added).
[37] CAT Rule 93(4) and section 47C(6) Competition Act.

More generally, the CAT fully recognises the importance of third party funding in enabling access to justice and, in this context, access to the collective opt-out litigation procedure. This is a clear shift away from the discussion in Parliament that was based on the assumption that opt-out collective actions are brought on a *pro bono* basis.[38] The CAT also acknowledges that payment of the funder's fee is essential for the operation of a funding agreement and that no commercial funder would assume the financial risk of major litigation without consideration:[39]

> *For the applicant, it was emphasised that payment of the fee charged by the funder was essential for the operation of the funding agreement. Clearly, no commercial funder would provide substantial funding and assume the significant financial risk of major litigation without consideration, and the structure of the collective proceedings regime for opt-out proceedings was to enable that consideration to be paid out of the unclaimed damages awarded to the class of claimants. The applicant could not be expected to assume an independent personal liability to the funder for its fee. The statute should accordingly be given a purposive interpretation to encompass a funding structure such as the present.*

In *Merricks* the issue was whether the success fee was covered by CAT Rule 93(4), post-distribution. The CAT makes it clear that this is indeed the case. However, the CAT's finding must not be misconstrued as limiting the recovery of funder's fee to unclaimed damages. The CAT suggests a 'purposive' interpretation of CAT Rule 93(4) and stresses that the applicant "could not be expected to assume an independent personal liability to the funder for its fee". Consequently, to satisfy these requirements in cases where it is anticipated that the take-up of damages will be high, it is necessary to provide for the costs of the action, inclusive of success fees, to be deducted pre-distribution, for without such an arrangement the cases could not be funded at all.

In the final case, *Boundary Fares*, for which the funding arrangement is known, the LFA makes it clear that the funder's return is to be paid partially pre-distribution if the case settles under a collective settlement order. The Class Certification Hearing is due to take place from 5th to 7th November 2019.[40]

IV. The CAT's Powers regarding costs and fees

We have demonstrated that section 47C(6) and CAT Rule 93(4) deal with the special case that funds are left over after distributing damages to all known class members. The history of section 47C(6) makes clear that the recovery of fees and cost is only to be limited to left-over funds in the context of *pro bono* actions. In this section, we complete our argument by showing that section 47C(6) is required in addition to normal cost rules to enable the CAT to authorise post-distribution payments. This means that in all

[38] See our arguments in the previous section.
[39] *Walter Hugh Merricks CBE v Mastercard Inc* [2017] CAT 16 at [119].
[40] 1304/7/7/19 *Justin Gutmann v First MTR South Western Trains Ltd*; 1305/7/7/19 *Justin Gutmann v London & South Eastern Railway Ltd*; 1305/7/7/19 Justin Gutmann v London & South Eastern Railway Ltd. Boundary Fares LFA.

other instances cost and fees are to be taken out damage *pre-distribution* following ordinary CAT cost allocation rules.

Also of importance in this context is that CAT Rule 104(1) on costs "also includes payments in respect of the representation of a party to proceedings … where the representation by a legal representative was provided free of charge".[41] This is a clear reference to the idea that class actions are brought *pro bono*, therefore incorporating section 194 Legal Services Act 2007 as explained in the House of Lords.

The main reason for introducing a post-distribution rule is that the CAT has no power to make an order for costs unless authorised by the statute.[42] There is therefore no denying that section 47C(6) provides that for distribution out of unclaimed damages. However, section 47(6) or the CAT Rules make no reference to cost and fee recovery pre-distribution, although Rule 104(2) "provides that the Tribunal has discretion, at any stage of the proceedings, to make any order it thinks fit in relation to the payment of costs by one party to another in respect of the whole or part of the proceedings. In the normal course, costs orders are made shortly after the delivery of the decision."[43] As we have shown above, section 47C(6) provides for the special case that funds are left over post-distribution, thus was required to authorise the CAT to distribute costs after funds are paid out to members of the class. When the class representative returns to the CAT to report on the level of undistributed damages, there will be no 'decision' in the sense of Rule 104, so the CAT would not have the power to award the undistributed damages to anyone other than the Access to Justice Charity (section 47C(5)), hence the need for section 47C(6) by way of additional power.

One could argue that in the absence of an explicit rule on pre-distribution, lawyers and funders are not entitled to costs *at all*. Such an argument would of course be consistent with the textual approach, advocated by those who say that Rule 93(4) is the *only* way that opt-out proceedings provide for success fees. However, this argument would ignore the context of section 47C(6) and CAT Rule 93(4).[44] More importantly, the CAT stressed that it has the general power under CAT Rule 104 to award costs, which applies to all proceedings before the Tribunal.[45]

The question then is whether the CAT is likely to accept that, despite its wording, CAT Rule 93(4) is a special case scenario and the pre-distribution recovery of cost and fees ought to be ordered in non-*pro bono* collective actions. The available cost rulings regarding CPO applications strongly argue that the CAT will interpret cost rules in a flexible manner to preserve a functioning collective action regime. In the *Merricks* cost ruling, the CAT was asked to determine the meaning of CAT Rule 98 – a rule clarifying that costs may not be awarded to or against individuals represented in the claim.[46] The CAT treated Rule 98 as a particular qualification of the general powers granted in CAT Rule 104 and refused to be limited to award costs only under that rule:

> *We should add that it is also not correct that even if a CPO were granted, the Tribunal would have no jurisdiction to award costs outside the scope of Rule*

[41] See also Competition Appeal Tribunal, *Guide to Proceedings 2015*, at [8.2].
[42] See CAT Rule 104.
[43] Competition Appeal Tribunal, *Guide to Proceedings 2015*, at [8.1].
[44] See previous section.
[45] *Walter Hugh Merricks CBE v Mastercard Inc* [2017] CAT 27 at [7].
[46] *Ibid.* at [7].

> *98. Consistent with the practice of the courts where there is a commercial third party funder, the Tribunal could in an appropriate case make a costs order under Rule 104 against the funder …*[47]

The CAT could not have stated in any clearer terms that its interpretation of the relevant statute and Rules is not limited by the text of the Competition Act and the CAT Rules. The CAT awarded costs against *Merricks*, the CPO applicant and the losing party, as the 'loser pays' principle applies in the CAT.[48] The CAT discerned the position with reference to the "Government's Response to its consultation on Private Actions in Competition Law."[49] Not only did the CAT have no qualms about referring to extra-judicial documents (a step further removed from Hansard and *Pepper v Hart*[50]) but the CAT also adopted case law which, under a textual interpretation of the CRA 2015 and CAT Rules, it should not have done. There is no reference to the 'loser pays' principle in the Consumer Rights Act nor in the CAT Rules (or Guidance), but the CAT adopted it.

Notwithstanding that there is no reference to the 'normal rules' of litigation financing whereby a client is contractually obliged to pay fees to those who are risking their capital, from the CAT's practice there is every reason to suggest that the CAT would look to Hansard and the *travaux preparatoires* and find that the 'normal rules' of litigation funding apply.

V. Collective settlements

The CAT Rules on collective settlements further strengthen the case for pre-distribution recovery of cost. The settlement provisions of Rule 94(9)(a), provide that the CAT can approve payments of costs, fees and disbursements as part of the settlement which include, for example, payments to funders and ATE premium. This 'mirrors' Rule 93(1) in the case of a judgment. If Rule 93(4) is the only way that funders can be paid, the rules on judgment would be less favourable than in respect of settlement. Rule 94(9) does not contain a mirror of Rule 93(4) and as part of a settlement (which is approved by the CAT) success fees can be agreed to be paid out of the damages, pre-distribution.

It would be very strange indeed, if the CAT could award costs pre-distribution in the case of a settlement but not after judgment. This may also create a conflict of interest for the class representative. If cost recovery rules for settlements are different from cost recovery rules for trial, the class representative faces an awkward choice. He can agree on success fees, take a chance on a trial and hope that there are sufficient unclaimed damages for the success fees to be paid, or he can agree on success fees and settle the case at the first opportunity to recover costs – which may not be in the interest of the represented class. The choice creates an issue that is substantial enough to place the class representative in a conflict with the class that he represents, it would create a possibility that the class would be decertified.

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[47] *Ibid.* at [8].
[48] *Walter Hugh Merricks CBE v Mastercard Inc* [2017] CAT 27 at [8].
[49] Government Response at [5.60].
[50] [1992] UKHL 3.

VI. The Principle of Effectiveness and the Damages Directive

The history of section 47C(6) clearly demonstrates that funders and lawyers can recover their costs and fees from the damages award before it is distributed to class members. In this section, we argue that limiting the recovery of funders' fees in collective actions with substantive distribution to the post-distribution stage is likely to be in breach of the individual's right to compensation and the EU principle of effectiveness. Refusing pre-distribution cost recovery in collective actions that effectively compensate victims, i.e. claims where funds are almost fully distributed, undermines funders' incentives to support 'good' class actions. Preventing 'good' cases qualifying for the collective action regime because the take up of damages by the claimant class is likely to be high would be perverse and in direct contradiction to the objective of the EU Damages Directive and the principle of effectiveness.[51]

It has long been established that any individual has the right to claim compensation for the breach of EU competition law in the courts of the Member States.[52] Article 3(1) of the EU Damages Directive restates that Member States must ensure that individuals who have suffered harm from breaches of EU competition law are able to claim compensation. While the right to compensation does not require Member States to create a collective action process, the principle of effectiveness requires that access to compensation is not unduly hindered. The principle of effectiveness under EU Law is summarised by AG Jääskinen:[53]

> *The principle of effectiveness, or effective judicial protection, obliges Member State courts to ensure that national remedies and procedural rules do not render claims based on EU law impossible in practice or excessively difficult to enforce.*

The Damages Directive, which is now binding on the UK,[54] essentially enshrines AG Jääskinen's statement in UK law by way of Art 4:

> *In accordance with the principle of effectiveness, Member States shall ensure that all national rules and procedures relating to the exercise of claims for damages are designed and applied in such a way that they do not render practically impossible or excessively difficult the exercise of the Union right to full compensation for harm caused by an infringement of competition law.*

If section 47C(6) and CAT Rule 93(4) are construed to limit the reimbursement of costs and fees to the post-distribution stage, they would discourage the bringing of collective

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[51] *Directive 2014/104/EU of the European Parliament and of the Council on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union* [2014] OJ L 349/1 ('Damages Directive').

[52] Case C-453/99 *Courage Ltd v Bernard Crehan*, ECLI:EU:C:2001:465 [2001] ECR I-6297; Case C-295/04 *Vincenzo Manfredi v Lloyd Adriatico Assicurazioni SpA*, ECLI:EU:C:2006:461 [2006] ECR I-6619.

[53] Case C-536/11 *Bundeswettbewerbsbehörde v Donau Chemie AG*, ECLI:EU:C:2013:366.

[54] Art. 21.1 of the Damages Directive. See also *The Claims in respect of Loss or Damage arising from Competition Infringements (Competition Act 1998 and Other Enactments (Amendment)) Regulations 2017*.

actions in scenarios where class members could be (almost) fully compensated (because no funds are left over for the funder). However, cost arrangements creating incentives not to bring a case that could achieve full compensation are likely to be contrary to the principle of effectiveness as expressed by AG Jääskinen and in the Directive.

D. Criticisms

In this section we will briefly address some counter-arguments to our reading of section 47C(6) and Rule 93(4).

Class Representative's Powers

It could perhaps be argued that the class representative has no power to commit class members to payments of costs prior to distribution, thereby reducing class members' recovery. This argument is somewhat based on Rule 98 which does not allow cost to be awarded for or against individual class members. However, there is no support for such a proposition in the legislation, the CAT Rules or the guidance.[55] Furthermore, the proposition misunderstands the role of the class representative and the role of the CAT – it is not the class representative who binds the class, it is the CAT that issues the orders that bind the class, under the statutory powers granted to it under the Consumer Rights Act.[56]

Once the CAT has granted class certification, the class representative is able to bind the class within the remit of the CAT's approval. If the class representative could not bind the class (following certification) to paying the costs of the litigation, it would breach the principles set out by the CAT in *Merricks*, and it would be the only thing that the class representative could *not* do. The class representative clearly has authority on behalf of the class to: (i) instruct lawyers to pursue the claim and to agree the funding arrangements; (ii) enter into a funding agreement and the 'consideration' to be paid to funders; (iii) instruct other professionals, e.g. economists, accountants and other specialists to support the case and to agree their fees; (iv) agree ATE insurance and the premium payable; and perhaps most importantly (v) agree the timing and quantum of a settlement.

Indeed during oral argument in the Merricks CPO application, Justice Roth said that the CAT's oversight of the LFA is to protect the class before the CAT binds the class to the LFA:

> *The traditional, or perhaps as you say not traditional because it is too new, but the usual arrangement is, well, of course, the party being funded makes the agreement with the funder. … The difference here being that the class being funded by its very nature is not involved in making the agreement. … That is why all these restrictions apply, including settlements having to be approved because normally the client decides whether the settlement is a good one or not. Here there is an absent class which has to be protected. That is why all*

[55] See our analysis above.
[56] Section 47B(12).

these protections come into play and that is why the usual funding agreement is just not possible.[57]

None of the powers limit the contractual terms that might be negotiated between the class representative and the third party concerned. Class members have the opportunity not to participate in the collective action by opting out under Rule 82(1)(b), but if they fail to opt-out within the time period specified by the CPO they become bound by the contractual terms agreed with third parties by the class representative and so ordered by the CAT.

No Right to an Opt-Out Remedy

There is no inherent right to seek remedy of a dispute through the opt-out regime - for example uneconomic 'good' cases could be pursued through regulatory channels, an opt-in or group claim, representative action or by individual action.[58] The opt-out regime must therefore be viewed in the overall context of the range of options available to a claimant, or group of claimants.

It could be argued that the opt-out regime is designed for cases where the class cannot be identified without recourse to advertising, and that the example given in the first part of this article, where the majority of damages can be distributed, might be inappropriate in an opt-out regime – perhaps an opt-in group action would be more appropriate. Our argument that the statutory purpose would be defeated if payments could not be made pre-distribution could evoke the response that an opt-in action could be brought and would be more appropriate.

In many cases, however, the opt-out regime is the only way that a remedy can be achieved. In the Consultation, the Government expressed frustration that there has been only one deemed unsuccessful opt-in case, the replica football shirt case.[59] The Consumer Association (now Which?) settled an opt-in case against JJB Sports for their participation in price fixing of replica football shirts. The settlement was agreed in 2009 – eight years after the infringement had ended. The Consumer Association had found it difficult to identify and convince victims to sign up for the claim. The limited pay-out and, thus, effect highlighted the difficulties of opt-in claims. History has demonstrated the limited success of the opt-in action. The lack of cases brought thereafter invalidates the purported counter-argument that other procedures would be equally effective in compensating claimants. The opt-out collective regime was brought in specifically because other methods of claim aggregation had failed to deliver compensation to harmed individuals.[60]

Indeed, *Mobility Scooters* itself would provide an example of circumstances where claimants would be unlikely to sign-up. Claimants were elderly and/or disabled, and therefore the opt-out regime is likely the only way that a claim could have been brought. There are many reasons why those with a claim do not sue and the theoretical availability of other avenues would therefore seem a poor argument not to follow the

[57] *Walter Hugh Merricks CBE v Mastercard Inc,* Transcript of CPO Application Hearing (Day 3) Transcript of 20 January 2017, p. 22.
[58] For example, the Civil Procedure Rules provide for a group litigation order in CPR 19.10-19.15 and a representative action in CPR 19.6.
[59] Government Consultation at [3.14].
[60] Government Consultation at [3.11-3.15].

intentions of the legislature. If cases were dismissed on this policy ground, for which there is no justification in the *travaux preparatoires*, market inefficiencies and illegal behaviour will not be eradicated. Such a policy level approach would therefore achieve a perverse outcome.

E. Conclusions

In this paper we have addressed a crucial aspect of opt-out collective action funding in the UK. We have demonstrated that any concerns about the non-recoverability of funders' fees and costs due to the lack of unclaimed funds are misplaced. We have made numerous arguments to support the view that costs can be recovered pre-distribution. The arguments to support the contrary view are weak, and require a selective reading of the *travaux preparatoires*.

Section 47C(6) and CAT Rule 93(4) have caused some confusion. Our analysis shows that section 47C(6) was inserted in the Consumer Rights Bill to provide costs recovery for *pro bono* representation. It is somewhat frustrating that in *Merricks* the references to Hansard were limited to the House of Commons debate, and they did not refer to the more insightful House of Lords debate. Only the latter makes it clear beyond doubt that section 47C(6) addresses the specific problem of *pro bono* representation but is not meant to limit fee recovery in commercially funded collective actions.

If post-distribution recovery is the only way that costs can be recovered, it would create perverse incentives. Collective actions with the potential to fully compensate class members would not be brought whereas collective claims with a good chance of substantial undistributed funds will be more likely to attract funding. In addition to the perverse incentives, limiting fee recovery to post-distribution would also create a conflict between the class representative's interests and those of the class. There is an incentive to design a distribution model that is 'less than optimal' in order to ensure that there are sufficient undistributed damages.[61]

Class actions do not always involve millions of consumers and hundreds of millions of damages. In other jurisdictions, class actions are not limited to competition damages so the comparison is not perfect but other jurisdictions can have a class size of a few dozen members – for example, teachers at a given school, civil rights violations, and victims of environmental torts, where distribution would be close to 100%.

In essence, a narrow reading of Rule 93(4) means that good cases will not be brought and less effective compensation cases will be encouraged. Legal teams would have to walk a tightrope to find the balance between the very good cases which are uneconomic and the bad cases that are economic but may not get class certification, because distribution is difficult and may lead to a low take up of damages. It seems perverse that a system designed to create more efficiency by enabling recovery for damages for competition violations would actually increase inefficiencies.

[61] This is far from a theoretical concern. Given the widely (although not universally) held belief that Rule 93(4) is the only way that success fees can be recovered the need for substantial undistributed damages is an expectation.

On a policy level it must surely be the case that providing another procedure for claimants to recover their losses should be encouraged, especially given the government's frustration at the lack of previous cases.[62] Indeed, there is a very good argument that being able to identify class members is exactly what the regime is created for. In this sense, the 'perfect case' where there are clear competition violations and where damages can be put directly into the hands of those who have suffered harm is 'perfect', but under the Rule 93(4) single route to costs recovery, the perfect case would be *too good to fund*.

[62] Government Consultation at [3.14].