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Changes in EU Legal Landscape Offer a Leadership Opportunity for In-house Counsel

Litigation and Dispute Resolution

Skills and Professional Development

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The litigation risk environment in Europe is increasing, which brings challenges for businesses but simultaneously offers leadership opportunities for in-house counsel who can help their organization identify and address those challenges.

These changes offer corporate in-house counsel a golden opportunity to embellish their credentials as critical business partners in the boardroom and on corporate leadership teams. By moving beyond a narrow transactional role and scanning the legal landscape for potential legal risks and exposure, assessing those risks and providing pragmatic strategies to mitigate them, in-house counsel can bring significant added value to C-suite meetings. The significant legal and regulatory changes going on in the European Union and United Kingdom offer in-house counsel an ideal opportunity to enhance their leadership role in this respect.

Increased risk of class actions

The most acute area of increased risk is in class actions. Europe is seeing a sharp increase in these

types of claims: 121 were filed in 2022 compared to 55 in 2018, equating to 130 percent growth in that period (see CMS European Class Actions Report 2023). This growth is being driven by a number of factors including new procedural mechanisms being made available at domestic level, increasing capital availability from litigation funders and specialist plaintiff law firms including, but not restricted to, US plaintiff firms setting up in Europe.

The increase in class actions are even before the EU Representative Actions Directive (RAD) comes into effect. The RAD will empower “qualified representatives” to bring collective actions and seek damages on behalf of groups of claimants harmed by unlawful practices that breach a wide range of EU laws, including consumer protection law and product liability law.

The RAD introduces a set of minimum procedural standards which Member States must make available for these claims. The RAD will not standardize class action mechanisms across Europe as its provisions act as a “floor,” and Member States are permitted to introduce procedures which go beyond those required by the RAD with yet greater risk for businesses. EU Member States were required to comply with RAD by 25 June 2023. Many countries have missed this deadline, but several are likely to introduce new class action mechanisms in the coming months. Thus, the recent increases in class actions in Europe are even before RAD has had an impact.

ESG risks, creative plaintiff tactics, and more challenges

Other dynamics that are increasing class action and litigation risk, and which are making those risks more challenging for corporations to address include:

- Increasing risks of ESG claims, many of which bring reputational risk which can bring settlement pressure irrespective of the substantive merits of the case;
- More active and creative tactics by plaintiff lawyers and collaboration with NGOs to use litigation and – connected to the point above – reputational risk to impose settlement pressure;
- Proliferation risk both within specific jurisdictions, but also cross-border where a claim in one country encourages claims to be filed elsewhere;
- Increasingly assertive enforcement by regulatory authorities that lead to follow-on class actions;
- Use of technology, including social media, to seek potential claimants to bring claims;
- Digital business models and ongoing digitisation across all sectors that create new risks for class actions in relation to the use and protection of vast customer data sets; and last but not least,
- Class actions are also being driven by third-party litigation funders (TPLF) that use litigation as a business model. TPLF is a growing industry across the European Union, whereby financial firms (such as investment firms running “hedge funds”) invest money to bring lawsuits in exchange for a percentage of the settlement or judgment if the case is successful. As the name states, these funders are third parties and usually have no relation to the claim; rather, their primary incentive is to make a profit.

Access to justice is a key element of a functioning democracy, but it is worth noting that according to a 2018 study by the Institute for Legal Reform, in 87 percent of class actions in the United States, claimants got nothing and when claimants did receive payment from a class action, it was typically about US$32, while claimants' lawyers earned an average of US$1 million per settled case.

Notwithstanding the significant question mark over whether these claims materially benefit consumers, European legislatures are increasingly passing legislation that not only brings clear regulatory obligations but also is intended to make it easier for claimants to sue. Thus, it is not only changes to procedural law, such as is required by RAD, but changes in substantive law which can materially increase litigation risk in Europe. In-house counsel should be aware of developing legislation in their sector where it will materially increase risk of litigation.

Examples of new and proposed legislation which increase litigation risk are:

The proposed Product Liability Directive (PLD) and AI Liability Directive (AILD)

Elements of the proposed legislation which materially increases litigation risk are:

- Expansion of scope of damage to include immaterial harms such as "medically recognised harm to psychological health" and "loss or corruption of data";
- Introduction of vague and subjective criteria in the test for defectiveness;
- Possibility of reversal of burden of proof in certain loosely defined situations;
- Far-reaching proposals for disclosure of pre-trial evidence and introduction of presumptions in favour of the claimant with a weakening of the protections for sensitive documents or trade secrets and of other rights of defence;
- Removal of minimum thresholds for bringing a claim;
- Additional complexity and confusion with other regimes such as Product Safety regulations and possible usurping of role of Regulatory Authorities in the safety field.

The proposed Corporate Sustainability Due Diligence Directive (CS3D)

Elements of the proposed legislation which materially increases litigation risk are as follows:

- Very broad scope of companies' responsibility over what is termed the "value chain" that includes both upstream and downstream business partners;

- Lack of alignment with existing human rights and environmental due diligence frameworks such as OECD and ILO Guidelines and other EU reporting requirements;
- Overly formalized rules and lack of risk-based or flexible approach for companies to use in their due diligence;
- Possible liability for damages caused even by an indirect partner;
- Need for significant investments by companies in extra resources, funding and capabilities to implement the new measures and ensure compliance.

The Digital Services Act brings very significant regulatory changes for digital services providers, but in addition to these regulatory obligations, Article 54 of the DAS gives persons a direct right to sue providers of intermediary services for compensation "*in respect of any damage or loss suffered due to an infringement by those providers of their obligations under [the DSA]*."

The PLD, AILD, and CS3D proposals are still going through the complex EU legislative process and are subject to modification before they are finally adopted. The above comments are based on the proposed texts as currently available.

Even though several of the legislative proposals are not yet adopted, it is clear that the legal framework within which companies operate in the European Union is becoming more complex including, inter alia, through the introduction in non-common law jurisdictions of common law-based tools such as discovery procedures in collective actions, overlapping private/public enforcement decisions by national Courts and Member State national competent authorities, forum-shopping by claimants as well as parallel, follow-on and cross-border claims.

Overall, it is likely that the volume of claims being brought against companies is likely to grow significantly and the size of the claims will also increase and the chances of claimants winning will also be higher. Many EU countries operate cost shifting rules which are intended to deter frivolous claims, but often the amount which can be awarded in adverse costs is capped at a low level. This capping can deter frivolous low value claims, but they do little to deter high value frivolous claims as the sum in issue vastly exceeds the cap on adverse costs risk.

The changes described above will increase costs and risks for companies doing business in Europe. In-house legal functions will face increased demands, especially if they are hit with high profile litigation which draws attention from the board. Those claims will demand highly sophisticated, expensive and carefully managed defence strategies. Proactive senior in-house lawyers will assist their business partners by identifying the risks brought by specific legislation and preparing accordingly. Those senior lawyers are uniquely qualified to identify, understand and interpret the complex legal changes and to mitigate the risks by introducing pragmatic and tailored solutions at their companies.

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Kenny Henderson is an experienced litigator who represents sophisticated and blue-chip clients in high stakes disputes, frequently with a cross border element. He is particularly experienced in strategically significant litigation such as class actions, competition litigation and litigation in regulated industries. He also advises clients in identifying developing areas of strategic risk and implementing mitigation strategies.