Justice Committee

Civil Litigation (Expenses and Group Proceedings) (Scotland) Bill

Written submission from the Forum of Insurance Lawyers

1. The Forum of Insurance Lawyers (FOIL) exists to provide a forum for communication and the exchange of information between lawyers acting predominantly or exclusively for insurance clients within firms of solicitors, as Counsel, or as in-house lawyers for insurers or self-insurers. FOIL is an active lobbying organisation on matters concerning insurance litigation and seeks to advance a reforming agenda for a more transparent and proportionate claims environment benefiting claimants and insurers alike.

2. FOIL represents over 8,000 members. It is the only organisation which represents solicitors who act for defenders in civil proceedings. This submission was drafted following consultation with the FOIL membership in Scotland.

3. The comments in this submission are restricted to the subject of personal injury claims, but (except where otherwise stated) should not be read as applying to clinical negligence claims where we accept different considerations might apply.

4. Our comments follow the same structure as the Call for Evidence.

Whether the Bill will achieve the policy aim of improving access to justice by creating a more accessible, affordable and equitable civil justice system

Introduction

5. FOIL supports the broad policy aims of the Bill. However, our concerns are that the Bill, as currently drafted, might not only fail to achieve those aims, but that the unintended consequences of the Bill could be seriously detrimental to those aims.

6. In Scottish litigation the usual rule is that the loser pays the winner's legal expenses. That rule has the effect of encouraging both parties to settle, instead of wasting court time and racking up legal costs. It is important that any changes to that rule maintain the same incentive to settle those claims which ought to be settled and do not cause wasted court time and expense.

7. The Bill will introduce qualified one-way costs shifting (QOCS), which means that in personal injury claims a pursuer who loses their case will no longer (in general) be liable for the defender's legal expenses. That will remove a very significant incentive for a pursuer to settle a claim, and will likewise remove a major disincentive against making a dishonest or fraudulent claim. We do not believe there is any current evidence that would support the introduction of QOCS in Scotland. If QOCS is brought in to Scotland, then it must be accompanied by rules which safeguard the interests of society as a whole: dishonest claims must be discouraged, and parties must be incentivised to settle claims.

The market for personal injury claims

8. The pursuer personal injury market contains a number of different models. Some claims are simple and direct: an injured person contacts a solicitor in order to obtain the compensation they are entitled to. In other claims however the route to market is more complex, and involves networks of accident management companies, claims management companies and other enablers buying and selling referral information and encouraging reluctant claimants to proceed with (or manufacture) a claim. This is known as "claims farming" and often involves the use of texts or unsolicited telephone calls to generate claims. Claims are assets that are bought and sold because they provide a ready stream of work with good margins. In its most extreme case this involves claims which are not genuine, either opportunistically or as part of an organised fraud perpetrated by criminal gangs.

9. In the foreword to the Taylor Report, the learned author stated:

   In the three year period between 1 April 2008 and 31 March 2011, the number of claims registered by the Compensation Recovery Unit in England increased from 728,164 to 892,463, an increase of 23 per cent. In the same period, the number of claims registered in Scotland increased from 36,417 to 38,819, an increase of only 7 per cent.

10. There are a number of factors to consider in order to understand the background to this comparison, and how trends in personal injury litigation have changed since that data was compiled in March 2011.

The effect of change in England and Wales

11. They key difference is that structural changes in England and Wales since 2011 have made Scotland a much more attractive jurisdiction for injury claims.

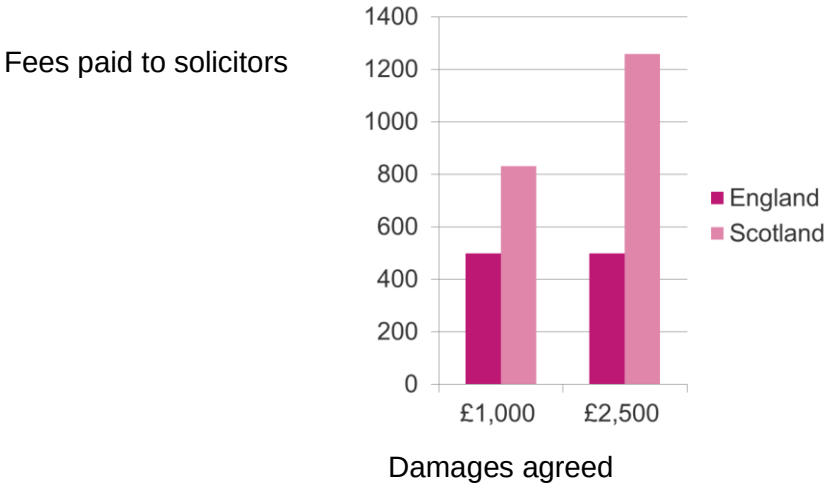
12. The statistics in the Taylor Report are taken from a period of time prior to the enactment of the Legal Aid, Sentencing, and Punishment of Offenders Act 2012 (LASPO) in England and Wales. Prior to 2012, solicitors' costs were higher in England than in Scotland. As claimant solicitor firms and claims management companies operate on a risk/reward model, it was hardly surprising that in England, where the risk was the same but the reward was greater, there was a higher incentive to make a claim, and more claims were made as a result. Prior to LASPO, significant economic drivers were in place to support a growing claims environment in England.

13. To compare claims data without a detailed appreciation of the operating model of accident management companies and English claimant solicitor firms risks obscuring the causal factors which lie behind those numbers. This is not a like for like comparison. Two significant changes have occurred in England and Wales since the Taylor Report:

    (i) As of 1 April 2013, referral fees have been banned in England and Wales. The ban on referral fees in England removed one incentive for claims to be generated or "farmed".

(ii) Claimant solicitors' costs in England are now capped and are lower than the equivalent judicial expenses in Scotland. That means that Scotland is now a much more attractive destination for claims farmers:

Table 1: Comparison of pursuer's solicitors fees for pre-action settlements in Scotland and in England



14. It is obvious that Scotland is now a much more profitable jurisdiction, in particular for claims management companies, both from the perspective of higher solicitor fees generated per claim, and because of the additional income stream derived from selling referrals.

The position in Scotland since 2011

15. Due to the passage of time, the data relied upon in the Taylor Report is now considerably out of date. From data we have obtained from the DWP, the period between 2011 and 2016 saw the number of injury claims in England and Wales decrease by 4%, whereas there was a corresponding 16% increase in Scottish injury claims[1]. The decrease in England and Wales (and increase in Scotland) corresponds broadly with LASPO coming into force in England and Wales. One conclusion from this data is that accident management companies which have seen their business model disrupted by LASPO in England and Wales have moved their activities to Scotland where the rewards are greater, and they can operate free from regulation.

16. In only seven years (2008/9 to 2015/6) there has been a 43% per cent increase in the number of personal injury claims in Scotland without QOCS[2]. Over the same period there has been a 25% increase in the number of personal injury court actions raised in Scotland[3].

[1] Source: FOI response from DWP dated 12 April 2016
[2] Source: 36,417 in 2008/09 per the Taylor report; 52,104 in 2015/16 per DWP FOI response dated 12 April 2016.
[3] Source: Civil Justice statistics in Scotland 2015/16: http://www.gov.scot/Publications/2017/03/5915/downloads

17. Although the argument for QOCS in Scotland is based on access to justice, the experience of FOIL members is that the vast majority of claims management companies and pursuers' solicitors will underwrite any adverse award of expenses, with the result that the pursuer rarely if ever requires to meet them personally. Indeed, there are pursuer solicitors and claims management companies which advertise for new clients on the basis that "you won't have to pay a thing". There is no current evidence to support the proposition that genuine personal injury claimants are deterred from making claims, or raising court actions, in Scotland. That being so, if QOCS is implemented without appropriate safeguards, there will be significant adverse consequences including increase in nuisance calls, increase in fraudulent claims and higher insurance premiums all as more fully outlined below.

The specific provisions in the Bill which:

(i) regulate success fee agreements (sometimes called 'no win, no fee' agreements) in personal injury and other civil actions, including by allowing for a cap on any fee payable under such agreements

18. The level of the success fee must be based on an assessment of the risks inherent in the case.

19. To safeguard pursuers we strongly support an overall cap on the success fee. The Scottish Government will require to collect and publish data on the share of damages currently taken from pursuers under speculative fee agreements in order to determine the appropriate level for the cap. That will be an ongoing task to ensure the level of the cap remains appropriate. The cap will also have to be policed with sanctions for its breach. Any contract which includes a deduction in excess of the cap should be void.

20. It is essential that future losses (for example, cost of care and loss of future earnings) are ring-fenced from the calculation. Future losses in catastrophic cases (such as those involving paraplegia, tetraplegia, or cerebral palsy) are carefully calculated to ensure severely injured pursuers have the care, accommodation and equipment they need for the rest of their lives.

21. To apply a crude percentage deduction from such huge sums could result in an enormous windfall for the solicitor and a funding gap (and significant anxiety) for the injured pursuer, who in most cases has no source of income. The Bill proposes at section 6 a complex mechanism for dealing with that situation. In our submission that complex mechanism is unnecessary, and can be avoided entirely by ring-fencing future losses and making them exempt from the DBA/SFA.

22. If the concern with that approach is that solicitors will be under-paid, it will be remembered that the pursuer's solicitor will be allowed to apply a DBA to past losses, and (as is currently the case) will in addition recover judicial expenses from the defenders, including in many cases an increase in those expenses (known as an "additional fee", which can be a multiple of three or four times the judicial expenses) from the defenders. FOIL members have reported a couple of very recent examples:

- Damages of £1m: pursuer's solicitor's account settled at £105,500 inclusive of additional fee.

- Damages of £730,000: pursuer's solicitor's account settled at £98,500 inclusive of additional fee. The solicitor's fee was approximately £47,000 excluding VAT.

23. DBAs will allow a pursuer's solicitor to receive an extra payment (on top of the fees paid by defenders shown above) from the pursuer.

24. In our view damages for future losses should stay where they are meant to stay: with the injured pursuer, and not in the hands of lawyers.

(ii) allow solicitors to enforce damages based agreements (a form of 'no win, no fee' agreement, where the fee is calculated as a percentage of the damages recovered)

25. The Bill treats all success fee agreements in the same way, although agreements in which the success fee is assessed as a percentage of expenses, and agreements in which the success fee is assessed as a percentage of damages are very different. In England and Wales, under damages based agreements, a claimant representative will require to offset costs recovered against the success fee, rather than recovering both. Under the proposals in Scotland, a pursuer's representative will be entitled to both recovered expenses and a fixed percentage of damages unrelated to the work undertaken.

26. In success fee agreements where the success fee is a percentage of costs, a mathematical calculation enables a success fee to be calculated based on the prospects of success in the case, thereby providing some protection to the consumer. It is much harder to link the success fee to prospects of success in a damages based agreement. It seems likely that, if the cap is the same for success fee agreements with a success fee based on a percentage of expenses or costs, as recommend by Principal Sheriff Taylor, damages based agreements will become the most common form of success fee agreements as they will always allow the maximum success fee to be recovered, expressed as a percentage of damages, regardless of the amount of work undertaken.

27. We consider it essential that a cap on damages-based agreements (DBAs) is set. The Scottish legal marketplace does not contain enough pursuer firms to generate sufficient competition to allow the cap to settle at a level that ensures pursuers' interests are safeguarded. Our comments above in relation to success fees apply equally here.

28. We do not agree that under a DBA a pursuer's solicitor should be entitled to recover and retain expenses recovered in civil proceedings in addition to the success fee. In some cases the success fee will be very substantial and the pursuer should be given allowance for recovered expenses.

(iii) introduce 'qualified one way costs shifting', which means that a pursuer who acts appropriately in bringing a personal injury action or appeal will not have to pay the defender's legal expenses even if the action is unsuccessful

29. As we have already set out, there has been a very substantial increase in injury claims in Scotland in recent years. That does not justify bringing QOCS into Scotland. Unless QOCS is balanced by further reforms it will create a series of financial and risk-based incentives which will lead to a substantial increase in claims, increased risk of fraud, substantial costs to the taxpayer and a corresponding increases in insurance premiums.

QOCS - the English experience

30. QOCS was implemented in England as part of a package of measures designed to reform the personal injury market. In addition to QOCS, the following reforms were introduced at the same time:

- A ban on referral fees
- Regulation of accident management companies
- Significant reduction in the legal costs which claimant solicitors can recover

31. The result of that balanced package of reform has been that meritorious claimants can still pursue their claim without fear of an adverse award of costs, while those behind frivolous or fraudulent claims are discouraged by lower rewards (in the form of reduced costs awards) and by stringent regulation. By contrast, in Scotland there are at present no provisions in the Bill which would prohibit referral fees, regulate accident management companies, or reduce recoverable legal costs.

Unintended consequences of QOCS in Scotland

32. If QOCS is introduced in Scotland as presently envisaged, the risk/reward balance which governs much of the pursuer market will be weighted significantly in favour of reward. We have already seen claim volumes increase significantly in Scotland without QOCS. The business model of accident management companies is such that they will inevitably move their operations to where the profit margins are best. Claim volumes will inevitably increase if the Bill is enacted (indeed this is appears to be what QOCS is designed to do).

33. The claims spend of insurers, self-insured businesses and the public sector will rise as the number and cost of claims both increase. The effects of the increase in the number and cost of claims include:

- An increase in nuisance cold calls and texts in Scotland, targeting in particular the most vulnerable– something the Scottish Government's Nuisance Calls Commission is trying to address;

- An increase in fraudulent claims (often connected to organised crime), again targeting the most vulnerable. The "LASPO effect" has already seen an increase in fraud in Scotland. FOIL members report an increase in cases that are fraudulent or have suspected fraud elements from 2% in 2015 to 11% in 2017. FOIL members have also identified a number of organised fraud rings operating in Scotland; and

- The significant risk of higher insurance premiums in Scotland due to the increased per capita cost of providing insurance cover in this jurisdiction. As well as being a cost on business, this makes it harder for the young to obtain motor insurance (particularly a concern in rural areas) and can only increase the number of uninsured motorists.

QOCS as part of a balanced package

34. In our submission it would be dangerous to introduce QOCS in Scotland without other measures which would constitute a more balanced package of reform. Those other measures are: reduction of pursuer's judicial expenses for low value claims; a ban on referral fees; and regulation of claims management companies. This was done successfully in England. None of these would impact on a pursuer's ability to conduct litigation without fear of an adverse costs order, and none of them would impact on access to justice.

Expenses for low value injury claims

35. Table 1 above demonstrated the relatively high level of costs recovery in Scotland compared to England and Wales, in pre-action settlements. FOIL members report the following information for average settlements in litigated cases:

Table 2: Comparison between damages paid to the pursuer and expenses paid to pursuer's solicitor

Damages	**Average expenses paid to the pursuer's solicitor (including VAT and disbursements)**
£3,000	£4,000 to £6,000
£10,000	£6,0000 to £11,000
£25,000	£13,000 to £18,000
£100,000	£25,000 to £42,000
£500,000 plus	£50,000 plus

36. It will be seen that, especially in lower value claims, the level of expenses recovery is already significant. This is the "reward" side of the risk/reward matrix. As QOCS reduces the risk then, unless reward is also reduced, there are significant incentives for a substantial increase in claims.

Referral fees

37. The ban on referral fees in England and Wales has had an obvious effect on the Scottish marketplace. Scottish claims are now, relatively, much more attractive to generate and sell. This has changed and will continue to change the profile of accident management companies in Scotland. According to records at Companies House, at least 15 new accident management companies have incorporated in Scotland over the last 18 months. Of course, very many accident management businesses will not structure themselves as a limited company. The fact that they are unregulated (see below) means it is impossible to know how many claims management companies operate in Scotland. To ensure a level playing field, and that the Scottish consumer is not penalised compared to the consumer in England and Wales, we support a ban on referral fees in Scotland.

Regulation of claims management companies

38. Claims Management Companies are regulated, throughout England and Wales, by the Claims Management Regulator[4]. That system involves a strict code of conduct, authorisation, audits, and inspections. The challenges of regulating Claims Management Companies have proved so significant that, under the proposed Westminster Financial Guidance and Claims Bill, regulation will pass to the FCA, with a view to a tougher regime being imposed. As long ago as 2012, the Govan Law Centre commented on the risks inherent in the absence of claims management regulation in Scotland.[5] In September 2013, the Taylor Report recommended that a regulator of claims management companies be established in Scotland[6]. The Nuisance Calls Commission has highlighted the absence of regulation of claims management companies in Scotland as a "*gap in the regulatory environment*"[7].

39. We understand that the regulation of claims management companies in Scotland is now being considered as part of the independent Review of the Regulation of Legal Services. However, that Review is not expected to report to Ministers until June 2018. It will be some years later before any legislation recommended by the Review comes into force. It is essential that regulation of claims management companies is implemented now, especially given the Bill's clear and obvious effect on the operating risk/reward incentive model of claims management companies. Scottish consumers will not be protected unless regulation of claims management companies is effected immediately (most likely via the Financial Guidance and Claims Bill at Westminster).

Equality of arms: not all defenders are insured

40. The purpose of QOCS is to address the perceived David v Goliath situation where a private individual cannot afford to fund litigation against an insured defender. The principle of equality of arms must be properly understood and properly applied,

[4] https://www.gov.uk/government/groups/claims-management-regulator
[5] http://www.moneysavingexpert.com/news/reclaim/2012/08/why-no-claims-management-arbitrator-in-scotland
[6] Taylor Report, recommendation 85.
[7] https://beta.gov.scot/publications/nuisance-calls-commission-minutes-march-2017/Nuisance%20Calls%20Commission%20-%20Paper%203%20-%20Regulatory%20environment%20-%20March%202017.pdf?inline=true

however, not all defenders are insured. Many pursuers enjoy the support of a well-funded accident management company or solicitors' firm standing behind them, acting on a no-win no-fee basis. In, for example, a public liability claim, a well-funded pursuer who benefits from financial support could pursue a private individual who has no insurance. In that situation, there is already an inequality of arms in favour of the pursuer. QOCS will only increase that further.

41. We therefore propose that section 8 should be amended as follows:

- QOCS should only apply where the defender is a public body, or is insured in respect of the claim; and

- QOCS should not apply where a pursuer enjoys the benefit of third party financial support, such as before the event insurance or support from a claims management company or credit hire organisation, or where the pursuer's liability for the defender's expenses are underwritten by his or her solicitor.

Restrictions on QOCS

42. Section 8(4) sets out circumstances in which a pursuer will lose the benefit of QOCS. It is essential that these are designed to support genuine claims and deter dishonest claims:

- "Fraudulent representation" is too high a test and, to be effective, may require production of evidence of actual fraudulent activity. We suggest that any claimant found to be "fundamentally dishonest" ought to be exempt from QOCS, which mirrors the approach taken in England and Wales. As that test is well established this would have the benefit of avoiding satellite litigation.

- Most personal injury claims do not result in litigation, but the structure of rules and costs for litigated claims has a significant bearing on how pre-litigation claims are conducted. At present there is no disincentive to discourage a claimant from making a fraudulent representation prior to litigation. To instil good practices both pre- and post-litigation, section 8(4) (a) should be amended to include a fraudulent representation made in connection with "*the claim or proceedings"* (rather than simply "*the proceedings*").

- It should also be made clear that any fraudulent misrepresentation in respect of any part of the claim will mean a pursuer loses the benefit of QOCS.

- A finding of fraud or fundamental dishonesty in relation to any aspect of the claim should result in the action being dismissed, as is the case in England and Wales. A genuine pursuer has nothing to fear from that proposal but it will deter the unmeritorious pursuer (and any entity providing support to that pursuer).

Encouraging early settlement

43. We do not consider that it is equitable for QOCS to apply where a pursuer is awarded less than any formal offer made by the defender (known as a tender). To encourage early resolution of cases, a pursuer who fails to beat a tender should meet the whole

of the defender's post-tender expenses. Anything less than that means a dilution of the current incentive to resolve cases early to the benefit of both parties and the court system. Whilst this issue may be addressed in detail in the rules, there is the danger that the prohibition against costs orders in Section 8(2) may make it impossible to allow a defender making a reasonable offer to recover any costs from an unreasonable pursuer.

(iv) give the courts the power to order that a payment be made to a charity where expenses are awarded to a party represented for free

44. FOIL supports this proposal.

(v) require a party to disclose the identity of any third party funder and provide the courts with the power to award expenses against that third party

45. FOIL supports the general purpose behind this provision. The Financial Memorandum states at para 67: "*This would include success fee agreements provided by claims management companies*". This should be reflected clearly in the Bill. It should be made clear that any third party which enters into a success fee agreement or a DBA with the pursuer is both providing "financial assistance" and has a "financial interest" in the proceedings. For the avoidance of doubt "financial assistance" should be defined to include deferring payment of a fee, agreeing not to charge a fee if the claim is unsuccessful, or upfront payment of any outlays (which in effect are a loan to the pursuer). All of these constitute a third party providing financial assistance to a pursuer. Where a pursuer is backed by a third party in this way, and a defender is backed by an insurance company, it is not equitable or proportionate for one party to enjoy the benefit of QOCS while the other does not.

46. In addition to being included in the Bill as a stand-alone provision, third party funding should be an exception to QOCS and part of section 8, rather than a matter left to the court's discretion (which will in any event only lead to satellite litigation). There is no reason in principle why a claims management company or a credit hire organisation should enjoy the benefit of QOCS. In the absence of David v Goliath, the usual rules on expenses should apply i.e. the losing party pays.

(vi) make legal representatives personally liable for any costs caused by a serious breach of their duty to the court

47. FOIL supports this proposal.

(vii) enable auditors (who are responsible for determining the amount of expenses due by one party in litigation to another) to become salaried posts within the Scottish Courts and Tribunals Service

48. FOIL supports this proposal.

(viii) allow for the introduction of a group procedure in Scotland, which would enable people with similar claims to bring a joint action

49. FOIL supports this proposal. We would also support the extension of this procedure to the Sheriff Court.

Any other matters relating to the Bill, such as any financial impacts or whether there are other provisions which should be included

Cost to the public purse

50. It is surprising that the cost to the public purse has not been calculated in the Financial Memorandum. Introducing QOCS without also introducing the measures we have recommended will increase the volume of claims significantly, in an environment where claims are already increasing. Many claims will not be litigated but the burden will fall on Scottish policyholders and on Scottish taxpayers. We set out a projection of some of these costs at Appendix 1.

Legal aid

51. With the legal aid budget under increasing pressure, legal aid should not be available for personal injury claims (other than clinical negligence) unless the applicant can demonstrate that they have attempted to obtain representation from a firm offering success fees or DBAs and such a firm has refused to accept their claim. It is not in the public interest for legal aid to be expended supporting a personal injury claim which could be funded by alternative means. This would allow more legal aid funding to be directed to areas of greater need such as cases involving children, housing rights, family law etc.

Forum of Insurance Lawyers
18 August 2017

Appendix 1

1. FOIL members report that the average cost of handling the defence of an average personal injury claim (including non-litigated and litigated claims, whether or not the defender handles the claim in house or instructs a solicitor) is £2217. That sum is simply the average cost of defending an average claim and does not include (for example) any damages or expenses paid to the pursuer or their solicitor. (It also does not include the court costs, borne by the Scottish Courts service, of administering such claims when they are litigated.)

2. In 2015/16 there were 52,104 personal injury claims in Scotland[8]. The public sector in Scotland accounts for 38% of the Scottish economy[9]. Using that percentage as an indication of the proportion of injury claims which fall to be defended by the public sector, for the purposes of this illustration, 38% of 52,104 is 19,800.

3. In the table below we illustrate how a projection of an increase in injury claims is likely to impact on the public sector in financial terms.

Annual increase in claims	**New claims per annum**	**Per annum additional handling cost**
1%	198	£438,966
2%	396	£877,932
5%	990	£2,194,830
10%	1,980	£4,389,660
25%	4,950	£10,974,150

4. Since 2008/09, in the absence of QOCS, there has been a 43% increase in personal injury claims in Scotland.

5. Using the same methodology as the table above, another increase of that magnitude would produce an increased handling cost of £**18,875,538** per annum to be borne by the public sector.

[8] Source: DWP FOI response dated 12 April 2016.
[9] http://www.parliament.scot/ResearchBriefingsAndFactsheets/S3/SB_10-88.pdf