EXTENSION OF THE RTA PI SCHEME: PROPOSALS ON FIXED RECOVERABLE COSTS

A response by the Association of Personal Injury Lawyers

January 2013

The Association of Personal Injury Lawyers (APIL) is a not-for-profit organisation with a 20-year history of working to help injured people gain access to justice they need and deserve. We have around 4,500 committed to supporting the association's aims and all of which sign up to APIL's code of conduct and consumer charter. Membership comprises mostly solicitors, along with barristers, legal executives and academics.

APIL has a long history of liaison with other stakeholders, consumer representatives, governments and devolved assemblies across the UK with a view to achieving the association's aims, which are:

- To promote full and just compensation for all types of personal injury;
- To promote and develop expertise in the practice of personal injury law;
- To promote wider redress for personal injury in the legal system;
- To campaign for improvements in personal injury law;
- To promote safety and alert the public to hazards wherever they arise;
- To provide a communication network for members.

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APIL supports legal reform where it produces efficiencies in process and delivers the appropriate level of compensation to the injured person. Fixing costs without fixing the process will not achieve this. Without ensuring that fixed costs are linked to a fixed process and fixed for both sides of the industry to reflect the work carried out, difficult but meritorious cases will not be brought and access to justice will be seriously impeded for those injured through no fault of their own.

Introduction

APIL remains gravely concerned about the lawfulness of the proposed extension of the Road Traffic Act personal injury scheme. We have continually sought reassurances from the Government that the aggressive timetable that is being insisted upon is revised to allow for proper consultation on protocols, forms and other accompanying rules. Sufficient time should be allowed for data collection and independent analysis by an academic and proper procurement process of a new IT system. Whilst we welcome the CPRC consultation on the protocols, in our view this is only a small part of the exercise that must be completed.

The unrealistic deadline being imposed for these major reforms will have a serious impact on the injured person's ability to receive independent legal advice and appropriate compensation. Practitioners are also being exposed to significant uncertainty as the implementation deadline approaches. The process is still unclear; the fixed fees are only just being consulted upon and they are unable to set budgets and plan their businesses for 2013.

In the haste for reform the Government is failing to comply with their own procedure set out in its response to the Solving Disputes in the County Court consultation where it clearly outlined what procedure it would follow before coming to a decision. For the extension of the RTA scheme to cases up to £25,000 the Government stated, "consideration will be given to the timing of the extension, following a full evaluation of the existing RTA PI Scheme, following which we will publish our final impact assessment of the proposed extension."[1] In respect of the extension of the scheme to incorporate employers' liability (EL) and public liability (PL) cases up to £25,000 it said "while we plan to introduce a scheme for such claims, further consultation with key stakeholders will be required to agree the detail."[2]

The decision to reduce the recoverable fees for RTA claims between £1,000 and £10,000 was made without proper consultation, data or evaluation. The decision was reached by Government at a summit with the insurance industry. It is unfair to conduct reform in this manner when this amounts simply to a cost fixing exercise at the request of insurers intent on reducing the number and cost of lower value claims.

No full evaluation has been undertaken and therefore the full impact of these reforms, both on a victim's ability to bring a claim, the level of compensation actually received by the victim and in respect of the profession, has not been properly considered. An impact assessment should have been conducted before timing for implementation was confirmed; instead an implementation date was set. Without such a review serious issues regarding equality and diversity will be over looked.

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[1] The Government response to the Solving Disputes in the County Court, paragraph 15

[2] Ibid paragraph 16

An early evaluation of the RTA low value PI scheme conducted by independent academic Professor Paul Fenn raises a number of concerns that have not been properly taken into account by the Government before deciding whether or not to extend the scheme. The report "Evaluating the low value Road Traffic Accident process" July 2012 raises a number of concerns. First, Fenn found that there had been around a six per cent reduction in the level of damages. Further because approximately 50 per cent of cases exit the portal it is likely that the reduction in damages is driven by only 50 per cent of claims meaning that the reduction could be substantially more in real terms[3]. The latest figures from the Portal co suggest that the exit rate are now even higher, namely some 65 per cent[4]. The Governments stated aim of the scheme when developed was to simplify the claims procedure and reduced cost, it was not to reduce damages and this concerning trend has simply been ignored.

It should be noted that the high drop-out rate is due to insurance industry behaviour with *"around half of all notifications ... exiting the process due to denial of liability or non-response"* [5]; both of these factors being solely at the discretion of insurers.

Finally, Professor Fenn's report is caveated by the fact that the data used for the analysis is only for the first year of operation of the scheme, when the scheme had a number of teething problems (including duplicate claim notification forms [CNFs] being registered). Furthermore, the more complex and difficult cases have not yet finished and have not been included in the information which was analysed; the data therefore only reflects the straight-forward and easy cases. Indeed Prof. Fenn states that "[i]*t could be argued that this is too short a time period to make firm conclusions about the impact of the process, particularly those more complex, higher value claims that are settled within stage 3 of the process"* [6]. This again highlights the fact that the report does not represent the promised full evaluation of the scheme.

In his recent presentation entitled "The future of the RTA Portal: How successful has it been to date, and is it too soon to extend its remit?" at a Post Magazine event on 28 November 2012. Professor Fenn said as follows:

"Of course, my report has to some extent been overtaken by events as the government has announced its intention to extend the Portal from April 2013, and has released both the draft protocols for the extended scheme and the proposed set of fixed costs. Consequently I will finish with some comments on the government's plans in the light of my findings and recommendations."

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[3] It should be noted that the high drop-out rate is due to insurance industry behaviour with *"around half of all notifications ... exiting the process due to denial of liability or non-response"* [3]; both of these factors being solely at the discretion of insurers. 'Evaluating the low value Road Traffic Accident process' Professor Paul Fenn (Ministry of Justice Research Series 13/12, July 2012), page 23
[5]Ibid page 27

[4] Based on the cumulative figures from 20 April 2010 to 30 November 2012, portal management information shows that of the 1,493,398 CNFs which have concluded (i.e. are not still in the system), 972,004 left at stage 1, stage 2 or via the exit function without agreement; this equates to an approximate 65% drop-out rate.

Later in the presentation he said:

"To my knowledge the MoJ hasn't made any formal response to my report, so I have to infer their views on these from the actions they've taken in recent weeks.

Need for a further review before implementation of the Portal extension: it appears that they are committed to implementation in April 2013 without any further review of the existing scheme, and they have not as yet announced arrangements for reviewing the proposed extension. I believe some kind of review is planned, but details are sparse. Without a proper benchmark of the current system including longer lasting claims, and because the current set of proposed fixed costs are not evidence-based, a one-off review will in my view be rather limited in its scope and objectives."

In addition to all this the Government has recently launched a consultation "Reducing the number and costs of whiplash claims, a consultation on arrangements concerning whiplash injuries in England and Wales." We question the logic of consulting on RTA PI scheme fees when an increase in the small claims limit, even for whiplash only cases, would seriously reduce the number of RTA proceeding through the portal. It is impossible and irrational even to begin discussions on the fixed fee when it is not clear what cases are being costed for inclusion in this scheme.

If the small claims court limit is raised even for a limited category of cases the basis on which the claims process is being developed will be fundamentally flawed. The basket of cases within the process and the fixed costs set for that basket of cases will need to be entirely reworked to accurately reflect the level of work involved.

Whilst we understand the desire to reduce car insurance premiums, preventing access to justice for those who have been injured and cutting access to independent legal advice is not the way to achieve this. In fact APIL would question the suitability of justifying the current changes due to the perceived high level of motor insurance premiums. To place recent levels of motor insurance premiums in perspective, Otto Thorensen (ABI director general) indicated that "[i]*n real terms, the 2010 average premium, taking into account inflation, is still 26% below what drivers were paying in 2000."*[7] The insurance industry has already made significant savings from these reforms, at least £26 million a year[8].

These savings are only now coming through as *"the combined effect of information and reporting lags can result in a loss ratio which is related to loss shocks from the past two years as well as the current loss shock"*[9] essentially current premiums are based on data from up to two years previously. This combined with other factors, such as the number of insurers entering and leaving the market and changes in reserve levels, potentially explains why premiums are actually going down. For example, according to car insurance comparison website www.Tiger.co.uk *"the last six months have seen a significant drop in prices, from May 2012 to October a fall of over 8% has occurred*[10]." This reduction has occurred even though none of the proposed changes have been implemented yet. Further,

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[7] ABI Motor Conference - Tuesday 22nd November 2011, speech by ABI Director General Otto Thoresen; see http://www.abi.org.uk/Media/Articles_and_Speeches/59730.pdf)

[8] Appendix 1

[9] 'Cycles in insurance underwriting profits: dynamic panel data results' Fenn & Vencappa (June 2004)

[10] http://www.insurancedaily.co.uk/2012/10/18/car-insurance-premiums-hit-two-year-low/

there are to be significant savings to the insurance industry from the change to none-recoverability of success fees and ATE premiums in almost all personal injury claims (mesothelioma claims being excepted) from April 2013.

Referral fees v cost of acquiring business

The Government continues to draw conclusions about the link between referral fees and lawyers' costs which are illogical and flawed. The link appears to be based upon the premise that the abolition of referral fees contained within Legal Aid Sentencing and Punishment of Offenders Act 2012 (LASPO) provides a costs saving, a benefit, to the business models of claimant representatives. This is wrong for the following reasons:

1. Not all solicitors pay referral fees. In fact less than 50 per cent of personal injury firms pay referral fees[11]. This is supported by research conducted by the Legal Services Consumer Panel[12]. Those that currently do so will have to shift business models come April 2013 in any event.
2. Solicitors are free to obtain business in many different ways. This is the nature of a competitive market. All cases have an acquisition cost, in just the same way as insurers advertise to attract new customers for their insurance products. If the logic of the Government's belief as to the effect of the abolition of referral fees on insurance premiums were applied to the insurers themselves, the Government should make it illegal for insurers to advertise for customers thus saving them a considerable cost which would be reflected in lower premiums.
3. Abolishing referral fees does not prevent firms needing to market in other ways.
4. All marketing costs money.
5. No other profession is prevented from attracting customers by marketing which is essentially what reducing the level of fees by £700 seeks to do.
6. The effect of the drastic reduction in costs payable by defendants is to require one of two things (or a mixture of the two): a reduction in what claimant representatives receive for doing the work; or a reduction in the level of compensation received by the injured person as the injured person will have to contribute to the costs out of their damages.
7. It is simply wrong that the abolition of referral fees in LASPO will result in the removal of the need for claimant representatives who currently acquire work by way of referral fees to spend the equivalent on marketing, thus justifying a reduction in the fees payable by defendants. And clearly the LASPO ban on referral fees will have no beneficial effect on those who currently do not pay referral fees.

The SRA is currently consulting on the referral fee ban. In their latest consultation they recognises that whilst firms will have to reconsider their marketing/ advertising costs as a result of the referral fee ban, they do not envisaged that the cost of marketing/advertising will be substantially higher than the referral fees paid at the moment[13].

[11] Law Society Strategic research unit. REGIS figures 2010/2011
[12] Legal Services Board Consumer Panel. Referral arrangements, May 2012, page 13
[13] Solicitors Regulation Authority, consultation on the ban on referral fees in personal injury cases. Issued 23 October 2012. Paragraph 35

Data gained from APIL members who do not pay referral fees illustrates the current level of case acquisition costs incurred:

Table 1: Average level of case acquisition costs for non-referral fee paying firms

Case type and value	No. of respondents	Mean	Median	Mode
RTA (£1k - £10K)	n = 50	£444.22	£550	£550
RTA (£10k - £25k)	n = 50	£450.22	£550	£550
EL Accident (£1k - £10K)	n = 52	£442.90	£550	£550
EL Accident (£10k - £25k)	n = 52	£446.75	£550	£550
EL Disease (£1k - £10K)	n = 15	£359.07	£250	£200
EL Disease (£10k - £25k)	n = 14	£327.57	£229	£200
PL (£1k - £10K)	n = 51	£448.25	£550	£550
PL (£10k - £25k)	n = 51	£451.20	£550	£550

The above figures indicate that the cost of acquiring cases is not substantially different from the speculated level of referral fees. In fact in some cases the figures are substantially lower than the proposed referral fee reduction - e.g. employment liability disease cases. The approximate £700 reduction would therefore significantly adversely affect non-referral businesses, even though the reduction is meant to directly target those firms paying referral fees.

A further demonstration of the misunderstanding of referral fees is provided in Appendix 2 in a short paper written by Otterburn Legal Consulting. This shows that with the proposed reduction in fees plus the need for firms to still market their businesses to obtain work cases will become uneconomic to run.

The proposed portal RTA fixed fee for cases valued between £1,000 and £10,000 have been reduced by £700. We assume this amount is intended to reflect the forthcoming ban on referral fees. We question how the £700 referral fee figure was arrived at. The fixed fee table intended for RTA, EL and PL cases outside of the portal fees appear to have been reduced by around £550 to £600; again it is unclear how this figure has been arrived at. There has been no evidence or reasoning produced by the Government to support this assertion and therefore no rational basis to support this reduction. Full details of how these figures are arrived at and the methodology adopted by the Government should be provided. The two fixed fee models must not be looked at in isolation. The two are inextricably linked given that current dropout rates in the portal are around 65 per cent [14]. It is wrong to look solely at portal cases and assume so simple a calculation as the Government is doing in its proposals. Portal cases are the **minority** of cases, not the **majority.**

[14] Based on the cumulative figures from 20 April 2010 to 30 November 2012, portal management information shows that of the 1,493,398 CNFs which have concluded (i.e. are not still in the system), 972,004 left at stage 1, stage 2 or via the exit function without agreement; this equates to an approximate 65% drop-out rate.

At the same Post Magazine event 28 November 2012 Professor Fenn made the point that *"Need for an integrated approach to fixed costs for all claims, with and without admission of liability: the proposed fixed costs for the Portal extension are flat rate within the Portal, and proportional outside. They are also significantly below current costs due to an ad hoc reduction of £700 to take account of the presumed savings from the banning of referral fees (but unsupported by evidence on these presumed savings). Clearly the marked reduction in the flat rate costs inside the Portal should reduce the incentive for defendants to exit the Portal with low value claims. However, the lack of integration remains a problem. From a situation where the defendant's reward for admission of liability is too low for most claims, there will now be a situation where the defendant's reward for admission of liability is too high for most claims (that is, relative to the observed savings in solicitors' costs from early admission of liability). It follows that, if many more claims have liability admitted, even where the claimant's case is not strong, then we may move to something that looks very much like a de facto no-fault scheme, particularly if claimant solicitors are less inclined to take on risky cases due to low recoverable costs. No-fault schemes have advantages and disadvantages; they may reduce costs for both sides as liability is not disputed, but they may increase the number of claims and they may increase the number of accidents (evidence on this is available from a number of North American studies). No doubt the MoJ will be considering the evidence on these risks in their impact assessment for the proposed extension."*

Fixed recoverable costs for claims within the RTA, EL, PL protocols

Access to independent advice

The Government seems happy to let independent legal advice be eroded to the detriment of the injured person. Insurers must not be allowed to settle claims directly. We know from the Financial Services Authority that where an insurer directly captures a claim, and deals directly with the injured person who does not have independent advice, offers are only rejected in three per cent of cases despite the fact that when injured people are independently represented by a lawyer they are awarded 274.95 per cent or £1,003.07[15] more than the first offer.

To illustrate the detrimental effect the changes will have on injured people's ability to be able to access independent legal advice, APIL asked its members about their future plans:

If the Government's proposals remain unchanged, as a FIRM, will you continue to do PI work under £25k? (n = 155)	
Yes	30% (47)
No	15% (24)
Unsure	54% (84)

Nearly one in six firms which responded to APIL's survey indicated that they are likely to pull out of personal injury (PI) work under £25,000, while a further 50 per cent indicated that they were unsure about what they were going to do. It is therefore a possibility that nearly 70 per cent of firms may decide to pull out of PI work below £25,000 in the near future. This will

[15] Financial Service Authority third party capture risk report 2009

significantly restrict access to solicitors potentially leading to access to justice gaps in certain personal injury fields. This is particularly concerning for people with special needs who may not be able to deal with a claim simply over the phone and/or the internet; it is likely to adversely affect the most vulnerable members of society.

If the Government's proposals remain unchanged, do you anticipate the need to reduce staff numbers in the near future? (n = 155)	
Yes	76% (118)
No	9% (14)
Unsure	15% (23)

The figures also indicate that nearly three quarters of firms are likely to be making staff redundant. In the current economic climate, this is of particular concern as the number of PI practices to which they would normally apply for a new job are unlikely to be hiring new staff.

Approximately, by what percentage, do you think your business will shrink by in terms of current staff numbers?					
	Band A (n = 117)	Band B (n = 93)	Band C (n = 96)	Band D (n = 92)	Other (n = 75)
None	24	12	9	11	5
1% to 20%	48	17	17	12	12
21% to 40%	20	32	34	15	34
41% to 60%	11	13	17	32	13
61% to 80%	3	2	3	6	3
81% to 99%	1	1	5	3	3
All of them	10	16	11	13	5

APIL members also indicate that their businesses are likely to shrink up to 40 per cent in terms of Band A, B and C fee earners, while the number of Band D fee earners is likely to shrink between 41 per cent and 60 per cent. This will have serious implications on access to independent advice in all geographical areas.

The impact of the introduction of alternative business structures also needs to be evaluated and clearly understood. These appear to enable insurers to continue to enjoy at least some of the benefits of referral fees, whilst in a position of conflict of interest or potential conflict of interest, whilst preventing fair competition. This aspect needs to be carefully examined by the Office of Fair Trading and/or the Competition Commission. The impact on access to justice and fair competition is grave.

Access to the Bar

So far the Government has failed to confirm their position on access to the Bar for cases within the RTA PI scheme. It is essential that their position is confirmed as soon as possible. Counsel's advice is essential to ensure a claimant has access to independent advice on quantum if required. The attack on the levels of fees in this type of work further could result in a reduction in the quality of service, quality of case handlers and potentially result in a reduction in damages. This is something already borne out in the evidence produced by

Professor Fenn in his report to the Government in July this year[16]. The reason why the levels of damages have reduced needs to be clearly understood. One possible reason put forward by Professor Fenn is that the fixed costs regime does not link costs to the specific level of damages. Other possible reasons include the increased incidence of insurers making offers without any medical evidence and direct intervention by insurers to seek to settle claims quickly and cheaply. The possible reasons need to be carefully examined and understood before action is taken.

We have proposed before that for RTA cases under £10,000, the disbursement for counsel's fee would only become payable on the basis of an "added value trigger", namely if the quantum advice received from counsel produces a higher settlement on negotiation or award at stage three than the insurer's initial offer.

For all EL and PL cases and for RTA cases over £10,000 the trigger should be where the difference between the claimant's and defendant's offer is five per cent or more. The appropriate fixed fees for the disbursement could be agreed with the Personal Injury Bar Association (PIBA).

Irreducible minimum amount of work

It seems to have been forgotten, or ignored, that there is an irreducible minimum amount of work that is required in all cases. The Solicitors Regulation Authority requires lawyers to: know their client; take instructions, investigate funding options, provide advice on funding; carry out checks such as money laundering, ID, conflict of interest, bankruptcy. There is also a duty on the solicitor to manage client's expectations throughout the life of the claim, updating them on the progress of their claim throughout. All this is in addition to advising the client on the merits of the claim and the value of compensation they can expect to receive, and gathering the evidence necessary to make their claim.

Setting the fees payable by defendants according to Guideline Hourly Rates (GHR) and the amount of work required ensured that solicitors have the appropriate levels of income from this work to constantly engage in the training of staff to the required level of proficiency, carry out file audits, staff reviews, maintain up to the minute case management and telephone systems, have in place the requisite compliance procedures and checks and employ a finance department to deal with the accounting issues. Firms will be unable to run successful practices advising claimants on pursuing claims for minor injuries. Many will withdraw from the market leaving injured people either reliant on non qualified advisers or without representation, both of which result in restrictions in access to justice, a rise in litigants in person and the likelihood of under settlement of claims. There is a real probability that Claims Management Companies, no longer able to refer claims because of the forthcoming ban on referral fees, will move to running the claims themselves. These CMCs will be unregulated in the advice they give to claimants when compared to lawyers regulated by the Solicitors Regulatory Authority. They will get a lower level of service, advice and consumer protection.

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[16] Evaluating the low value Road Traffic Accident process Professor Paul Fenn, July 2012, page 28 "The reduction in damages found in this study (around 6%) was not part of the intended consequences of the RTA process"

If only the largest of firms with the greatest economies of scale can afford to do the work at the level of fees proposed this will fundamentally change the personally injury market and drastically reduce consumer choice.

RTA cases valued between £1,000 and £10,000

No evidence has actually been produced by Government to suggest that the figures originally agreed by both sides of the industry are too high. The fees were agreed by insurers and claimant representatives following negotiation facilitated by the CJC. Simply to reduce these to reflect the forthcoming ban on referral fees is illogical. Leading academic professor Paul Fenn was asked about the reduction in fees at the Post Magazine event on 28 November 2012, he said “my feeling is that that is a very dramatic reduction in those costs that are being recovered. I am wary about the impact of this.” A clear indication in our view, that this is not a rational way to fix costs and independent analysis should have been carried out.

The process followed last time which resulted in industry agreed fees was: once the prescribed process had been confirmed it was costed from the bottom up. An average amount of time taken to reasonably deal with each element of the fixed process was costed according to the appropriate level of fee earner needed to conduct the work. The GHR for the appropriate level of fee earner was then averaged out and applied to the amount of work involved. The rates applicable at the time of the exercise were applied, namely the rates for 2009. Additional time was then built in for supervision by an appropriate level of fee earner, and this was costed in the same way according to the applicable GHR. There was also an agreement to annually review these costs which has not been honored.

The claimant group consisting of APIL, The Law Society, MASS and Trade Unions, cross referenced figures arrived at by examining 50 detailed bills of costs in RTA matters, where the general damages were under £10,000 and where liability was admitted or agreed on a contributory basis but damages could not be agreed, meaning that the matters were ultimately outside the provisions of CPR45 Section II. None of the cases examined proceeded to a final hearing and all litigation costs (the issuing of proceedings, attendance at court, with counsel and with the client in respect of the same) were discounted from the calculations. Bills were selected from large/medium sized solicitor firms which operated systemised processes but which did not record time generically.

Claimant representatives’ and defendant representatives’ were asked to submit figures to the MoJ, which were mediated and the figures in CPR 45.29 were agreed. The figures were also considered by independent academic Professor Paul Fenn. In advance of the mediation he produced data on RTA cases valued £1,000 to £10,000, which could be used as a benchmark for the costs in the scheme.

With the benefit of hindsight, to fix the costs at that stage was premature. Whilst the process had been largely drafted, the forms had not been drawn up and the work involved in completing those could not be, and was not, costed. In addition, the use of counsel had not been properly considered.

Whilst the defendants sought to argue that the fees should be in the region of £850 for stage one and two to take into account £600 to £700 referral fee this was not accepted and the final figures did not take into account a referral fee or marketing spend. To reduce the fees to

reflect a ban in this area now is unsound. GHR were used against the time actually taken to complete the work. GHR were used on the basis that they include an element for marketing spend as a permitted overhead along with all other overheads including salaries, property rental, training/professional development and professional indemnity insurance.

The Advisory Committee on Civil Costs (ACCC) examined GHR and referral fees in 2009-2010 at the request of the MoJ as it said it wanted to investigate the reasons for the alleged 20 to 35 per cent difference between the hourly rates of claimant and defendant solicitors in personal injury and clinical negligence cases. The ABI had argued then that claimant fees should be reduced to the level of defendant fees because of referral fees and marketing spend. The ACCC found that there was no evidence to suggest that GHR should be reduced to the same level of fees that defendant solicitors charge and whilst marketing costs are high in PI cases, it was no surprise that PI lawyers spend more on marketing than employment or divorce lawyers because such marketing can generate more new cases than in those other fields of law.

APIL looked at a representative sample of data obtained from members in early 2012. The figures showed that for RTA cases valued up to £10,000, the number of hours to complete the work was between six and 14 depending on the complexity of the case. The average number of hours was ten. We know that an incidence of pre-medical offers is high, anecdotal evidence suggests that 25 per cent of cases within the portal settle without a medical report. APIL recommends that this practice is prevented altogether. Ensuring a claimant is examined in every case would go some way to preventing fraud in lower value RTA cases, something both insurers and claimant lawyers want to tackle.

The data also showed that the profit on a current portal case is around 14 per cent. This calculation includes the 12.5 per cent that is currently recoverable from the losing party for success fee. If the 12.5 per cent success fee is not recovered from claimant damages as the Government intends, this will reduce in a further loss of income to the lawyer, reducing profit to just four per cent on the basis that fees stay the same. Reducing them further still as proposed in annex A renders RTA claims under £10,000 unprofitable thus eradicating access to justice for victims with cases valued below £10,000. Undoubtedly some firms with application to application case management software will complete portal cases more quickly, but there is only so far this efficiency can be driven and it is essential that there remains diversity in the market and the market cannot be monopolised by just one or two major firms. The data suggests that the current fees are not too high.

RTA cases valued over £10,000 and EL and PL cases valued between £1,000 and £25,000

The Government has failed to provide the methodology for the figures arrived at for these cases. Indeed we are surprised that figures are even being consulted upon at this stage given that the protocols are not agreed and the forms have not been consulted upon. It is impossible to know how much work will be required for cases that fall within these sections of the scheme until that element of the process has been finalised. Setting fees for an unfinished process and an unknown amount of work is both irrational and unreasonable. It is impossible to collect meaningful data based on the “unknown.”

In order to illustrate the current level of work involved in these cases, APIL member provided data on the average time taken for these types of cases and average level of fee earner undertaking the majority (50 per cent plus) of the work:

Table 2:

			Level of fee earner undertaking the majority of the work (50%+)			
Case type and value	No. of respondents	Average hours per case	Band A	Band B	Band C	Band D
EL accident - £10k to £25k	n = 58	38	72%	23%	5%	0%
EL accident - £1k to £10k	n = 73	25	45%	26%	26%	3%
EL disease - £10k to £25k	n = 10	37	90%	10%	0%	0%
EL disease - £1k to £10k	n = 10	40	30%	50%	20%	0%
PL - £10k to £25k	n = 24	41	75%	21%	4%	0%
PL - £1k to £10k	n = 57	24	46%	26%	23%	5%
RTA - £10k to £25k	n = 49	32	54%	35%	8%	2%
RTA - £1k to £10k	n = 73	16	22%	14%	34%	30%

As already mentioned these figures are not based on a fixed process - which would be needed under a portal scheme - rather they reflect the current amount of work needed.

The Government must urgently review its approach to this work to ensure data is not collected and analysed until meaningful conclusions can be made. We would also urge the Government to involve an independent academic in this work to independently cost the process based on data sets produced by claimants and compensators to ensure there is sound methodology and force in any final fees produced.

In addition, the Government appears to have completely ignored the recommendations following the evaluation of the existing scheme by Professor Fenn. He recommended that any extension of the scheme "would need to take into account the extent to which incentives for solicitors to act in their client's interests are diluted with flat rate fixed cost, particularly in relation to the claims where the calculation of quantum is more complex."[17]

Claimant solicitors will need to examine the economics of running complex claims. As has already been stated, claimants may well be expected to fund some of the costs of pursuing claims out of their damages. Solicitors may require that claimants fund a greater amount of costs, if and when their claim becomes complex albeit that it remains a claim within the PI scheme. This will clearly discourage claimants from pursuing the complex and expensive aspects of their case resulting in lower damages being awarded to such claimants or their net recovery of damages, after costs are taken in to account, being reduced. Put simply, the lack of an incentive within the scheme to pursue the complex and costly aspects of these claims, particularly in claims over £10,000, will damage access to justice and the proper and full, or near full, recovery of damages to claimants. This is an inevitable consequence of the

[17] Evaluating the low value Road Traffic Accident process Professor Paul Fenn, July 2012, Page 28

fixed fee regime being proposed and of which there is already evidence from Professor Fenn.

Certainly there has been no explanation as to why Professor Fenn's recommendations have not been followed nor was there consensus from the call for evidence earlier this year: the Minister's letter confirms that views were wide ranging and contradictory.

Fixed recoverable costs for claims outside of the RTA, EL, PL protocol

Fixed costs

APIL does not believe that fixing costs is the solution to managing costs in the fast track; such steps will simply prevent injured people from being able to successfully bring difficult but meritorious cases. Where the costs are fixed but the process is not defined or predictable, the only cost savings are those that are driven by the claimant lawyers in an attempt to remain profitable. Without ensuring that fixed costs are linked to the process, the system is open to defendant abuse. We believe that the incentive on the defendant to narrow the issues in the case is lost where claimant costs are fixed. Compliance with the personal injury protocol by defendants is already a problem; however, if fixed costs were introduced there would be even less of an incentive for defendant insurers to comply.

The assumption has been made that parties' behaviour will not change if the costs payable in successful cases is changed. This is a fundamentally flawed assumption. Claimants' representatives will change their selection criteria as to which cases they are willing and able to take on, when acting under a conditional fee agreement of any sort. Defendants and their insurers can choose, as set out below, to dispute a greater percentage of cases than they do at the moment, knowing that the level of costs that might be awarded against them will be limited.

The inequality of arms that already exists between the corporate insurer and individual injured person will only deepen if the process remains unpredictable but costs are fixed. Insurers are already able to choose to undertake an unlimited amount of work to defend a claim on a point of principle. There can be genuine cases where there are exceptional difficulties on liability, and the case is of modest value, but if the issues arise and the claimant is successful in arguing their position then the costs have to be paid for. By fixing costs a claimant representative would simply not get paid for doing such work, no matter how necessary or fair it may be. This will cause access to justice issues where difficult cases are simply not run because of the cost constraints. And, as already observed above, defendants can choose to make cases more difficult.

The amount of work involved in a case is largely dictated by the defendant. They decide on the issues which the claimant has to prove. Fixing costs therefore does not fix the amount of work involved. All litigation is different; no one case is the same. Cases can involve disputes on liability, causation, quantum and limitation can often be raised. Many cases involve difficulties identifying the correct defendant and there can be apportionment issues in disease cases. They can also involve complex special damages especially in higher value

cases such as difficult care issues, loss of chance claims, claims for disadvantage on the open labour market, future loss of earning calculations and pension loss, to name some of the issues experienced. In addition to that, cases can involve foreign speaking clients, multiple defendants, children and patients, multiple experts, multiple injuries, multiple witnesses and inquests. These issues aside, a case must be proved and this involves time and cost. There is a need for consultation/evaluation of the impact of fixed costs where there is no fixed process, which should include insurer representative behaviours.

If a solicitor is restricted in the amount of work that he can do in order to prove the claimant's case, a claimant will not necessarily get the rehabilitation or compensation he is entitled to. There is a danger with fixing costs and not fixing the process that the commercial incentive for insurers to admit claims and narrow issues is lost. What is clear is that defendant behaviour will certainly change if the drivers against poor behaviour are removed.

If the costs in such a very large basket of cases are fixed, claimant representatives will be able to identify which type of cases can be run profitably with fixed costs and which cannot. The consequence is that solicitors will not take on the unprofitable cases thus denying access to justice to people with those types of cases. Alternatively, injured people with certain types of cases will be charged more by solicitors if and when the fixed fee is insufficient to cover the cost of work done. So access to justice will not only be reduced but also the justice received by many will be reduced justice.

If the Government is intent on implementing fixed costs for claims outside of the RTA, EL, and PL protocols then it is essential that the issues below are addressed.

Value of claim v allocation to a track

It is not clear from the letter whether these fees are proposed for all cases valued between £1,000 and £25,000 or if they are related to cases allocated to the fast track. Value is not the only reason for allocating a claim to a particular track. For fast track cases the civil procedure rules say at part 26.6 (5) that:

"The fast track is the normal track for the claims referred to in paragraph (4) only if the court considers that –

(a) the trial is likely to last for no longer than one day; and

(b) oral expert evidence at trial will be limited to–

(i) one expert per party in relation to any expert field; and

(ii) expert evidence in two expert fields."

It is therefore possible that some cases valued under £25,000 will in fact be allocated to the multi-track thus requiring all the procedural steps necessary to comply with multi-track directions. It would therefore be wholly inappropriate for these cases to attract the fixed fees proposed. More complex cases allocated to the multi-track but valued under £25,000 were not included in the data set used to fix these fees.

For instance, currently, if a defendant alleges that a claim is being brought fraudulently, the case will be allocated to the multi-track. An allegation of fraud, which may lead to a judicial

finding of fraud, is inherently complex. A judicial finding of fraud can lead to an order for contempt of court and, in turn, to imprisonment. This is all true whether the claim is worth £5,000 or £50,000. If the claim were one for £5,000 and the claimant was limited to the proposed fixed costs despite the claim being allocated to the multi-track by reason of fraud, the claimant and their solicitor would be at a huge disadvantage. The solicitor may be forced to refuse to continue to act for the claimant as to do so would be grossly uneconomic; the claimant may be required to fund the extra costs out of their own pocket. Such a costs disadvantage would undoubtedly be exploited by defendants, insurers and their advisors who would raise fraud in any and every case possible.

Further, there are many types of complex personal injury claims where the case is worth less than £25,000. Examples of these include disease cases such as deafness cases and Hand Arm Vibration Syndrome cases. The factual, legal and medical issues in such cases are many and complex. Such cases are currently routinely allocated to the multi track by virtue of their complexity even when the value is below £25,000. As above, if such cases were to be fixed with fixed cases notwithstanding their complexity they would become even more uneconomic to run. This would lead to claimants with such conditions finding it unable to get solicitors to run their cases on a conditional fee type basis as the fees would simply be insufficient to cover the cost of the necessary work.

It is therefore essential that the proposed fixed fees do not apply to cases allocated to the multi-track, irrespective of value. (It is the judiciary who allocate cases to the correct track; it is not the claimant's choice.)

Access to the Bar

Lord Justice Jackson stated that the Bar has a valuable role to play in fast track PI work. He proposed that a lump sum should be added to the costs in every Fast Track case to cover the average cost of solicitors instructing the Bar[18].

At present, in fast track cases, barristers are paid as a disbursement by the losing party. We support the retention of this practice to ensure that claimants have access to the Bar in cases outside of the liability admitted protocol. It is essential that there is further discussion with PIBA and the Bar Council on this matter.

Sanctions

The fees used to develop the fixed fee table include all cases settled on a standard basis. Whilst Lord Justice Jackson recommended that claimants should benefit from 10 per cent increase on general damages where they beat their own offer we believe that the current Part 36 benefits must also be retained. Claimants should not lose the right to indemnity costs and enhanced interest simply because a fixed cost regime is introduced. Part 36.14 in particular should be retained to benefit the claimant who obtained judgment which is equal to, or more advantageous than, the claimants own offer. It is only right that the claimant should get the benefit of making a sensible and realistic Part 36 offer where they have been faced with a stubborn defendant. It is important that claimants have the means to make a sensible offer and be rewarded for doing just that as they are now. A claimant must have the

[18] Lord Justice Jackson, Review of Civil Litigation Costs: Final Report, December 2009, page 159 paragraph 5.10

tools to protect themselves against a defendant who runs up costs and fails to narrow the issues in the same way that the defendant has the benefit where they make an early and sensible part 36 offer that the claimant refuses to accept. This is not a new benefit but is already enshrined in the rules.

Defendants' costs

It would be grossly wrong to fix claimants' costs without fixing defendants costs too. Notwithstanding the introduction of Qualified One Way Costs Shifting (QOCS) there will be circumstances when a claimant is required to pay some or all of the defendant's costs. Defendants' costs should be fixed at a fair level for the work involved and a fair process used for fixing them.

Sir Rupert Jackson in his Final Report also recommended that defendant costs be fixed. He said "I accept APIL's argument that I must consider the costs incurred by defendants.....since in PI litigation defendant costs are significantly lower than claimant costs, it would be disadvantageous to claimant lawyers if fixed costs are set by reference to defendant cost as opposed to the Fenn Data."[19]

Table B on which annex B is based includes claimant data only. As Sir Rupert Jackson acknowledged in his report defendants do less work and their costs are lower[20]. This is because the burden of proof is on the claimant to prove their case. Defendant lawyers get involved at a much later date, usually only after the start of court proceedings, and they have significantly less work to do. They are usually paid on every case by their insurer clients regardless of the outcome of the case.

One of the reasons why Sir Rupert Jackson recommended QOCS was to reduce the cost of ATE insurance to claimants. The level of ATE premiums will be further reduced if the extent of liability for defendant costs is fixed. ATE insurers would very much welcome the certainty that fixed defendant costs would give them. Fixing defendant costs would therefore further the Government's policy intentions as well as being fair to both parties.

We recommend that the Government urgently ask Professor Fenn to analyse defendant costs. A thorough analysis like that conducted for claimants costs is essential if defendant fixed costs are to be fair to all parties.

One circumstance where QOCS protection is lost is when a claimant is awarded less by a court than the defendant's Part 36 offer. This would give rise to a liability to pay the defendant's costs for the period after the making of the offer by the defendant. Therefore, fixed defendant costs will need to be staged to reflect when the defendant made its offer. Account will need to be taken of this requirement when conducting the analysis of defendant costs.

In addition, claimants should not lose the right to indemnity costs and enhanced interest simply because a fixed cost regime is introduced. The fees used to develop the fixed fee table include all cases settled on a standard basis. Therefore current Part 36 benefits must be retained. Part 36.14 in particular should be retained to benefit the claimant who obtained

[19] Ibid page 158 paragraph 5.8
[20] ibid

judgment which is equal to, or more advantageous than, the claimants own offer. It is only right that the claimant should get the benefit of making a sensible and realistic Part 36 offer where they have been faced with a stubborn defendant. It is important that claimants have the means to make a sensible offer and be rewarded for doing just that as they are now. A claimant must have the tools to protect themselves against a defendant who runs up costs and fails to narrow the issues in the same way that the defendant has the benefit where they make an early and sensible part 36 offer that the claimant refuses to accept. This is not a new benefit but is already enshrined in the rules.

Interlocutory applications

Annex B fails to deal with the issue of costs in interlocutory applications. In our view this is an area that needs urgent consideration. There clearly needs to be some form of cost sanction to ensure correct behaviours by all parties. Where genuine interim applications are required there should be a suitable mechanism for rewarding, in costs, the successful party, and punishing the unsuccessful party for the defaulting behaviour that required the making of the application. What must be avoided is a situation where interim applications are routinely issued to get extra fixed costs. There are two possible options for dealing with costs in this area: fix them at an appropriate rate; or, as now, require the court to summarily assess the costs. The advantage of fixing the interlocutory costs is that the parties are aware of what additional costs liability they may be exposed to; the disadvantage is that whilst the costs maybe fixed for both parties defendants would still be free to charge their insurer clients costs in addition to those recoverable inter partes which is grossly unfair. A further disadvantage of fixing the costs is that the level of costs may be set at too low a level thus favouring the defaulting party over the party who has to make the application.

The relationship between fixed recoverable costs in the PI scheme and claims outside of the portal

We are concerned that the data produced in the fixed recoverable costs table annex B has been collated in isolation from the work being done on the PI scheme. Bolting a fixed cost matrix on top of the PI scheme is not comparing like with like.

The draft protocols tightly define which cases the protocol will apply to and those that it will not. For example, abuse cases are excluded as are some disease cases. The data collected by Professor Fenn did not include certain categories of public liability cases. The data obtained was very general data regarding RTA, EL accident and PL accident cases. He did not ask for case types and details of the claim to be provided.

However, it is clearly the intention that some disease cases be included in the PI scheme and therefore the fixed recoverable costs scheme. Fenn's data did not include any disease cases. Currently there is simply no basis upon which the Government can rationally, fairly or properly set fixed fees for disease cases.

At the time the initial work was done for Lord Justice Jackson's final report, the PI scheme was still being developed and there was little regard by Sir Rupert for the process that was being developed.

In fact the data collected by Fenn included a broad basket of cases including both liability admitted and liability disputed cases. The application of this data as is being proposed is

therefore seriously flawed as the liability admitted RTA, EL, PL (as defined by the protocols) should not be included in the data set used for setting fees as those cases have been stripped out by the PI scheme. In addition, Jackson LJ's recommendation for fixed costs in the fast track was for accident cases only. Therefore, there is simply insufficient data available to fix fees for disease cases.

Despite Jackson LJ recommending that referral fees were banned, there was no recommendation for the proposed fees to be reduced to take into account such a ban. When Jackson made his recommendation that the figures in Appendix 5 to his report be used he did so, on the basis that they were part of a package of reforms, including the banning of referral fees. Therefore, to the extent that such a ban is relevant to the setting of fixed fees, account has already been taken of that in Jackson's recommendation of the figures in Appendix 5. For that reason, in addition to the others set out elsewhere in this response, it is wrong and irrational to reduce any such figures by reference to a ban on referral fees.

The data used for annex B in the Minister's letter is therefore seriously flawed as the two processes have not been considered together. There is a clear lack of understanding of the procedure and the complexity of fast track cases. We are concerned that reforms continue to be considered in isolation.

Exceptionality rule

Under the present scheme, either party can simply issue court proceedings, in the event of bad behaviour by the other party. The case then comes out of the fixed cost regime and subject to judicial discretion as to whether or not fixed costs should apply. A fixed cost regime for all Fast Track cases (whether issued or not) removes this safety net and is therefore open to abuse. APIL is concerned that if the wronged party has to prove the case is "exceptional", that may in practice mean that no cases can escape, depending on the definition of the word "exceptional", no matter how justified or deserving the application to escape fixed fees might be. APIL suggests that a defendant can for example string a case out (whether by making numerous requests for additional information, or a number of interlocutory applications, or otherwise) without that necessarily being conduct, which attracts indemnity costs under the rules.

It is essential that CPR 45.12(1) is amended and APIL suggest the amendment should be: *"but only if it considers that there are ~~exceptional circumstances~~ issues of complexity, or conduct by the defendant, which have resulted in a proportionate increase in costs to at least 20% in excess of the fixed fee, thereby making it appropriate to do so."*

Comments on the Fenn data

Road traffic accident data

The original data produced by Professor Fenn, for the purposes of populating the table in annex B of Lord Justice Jackson's final report, did not take into account the work being done on the claims process at that time. The result of this is that the figures for RTA cases under £10,000 are likely to be skewed as all the liability admitted cases are now being dealt with under a different regime. This means that the cases left to be dealt with outside of the portal will, by their very nature, be more time consuming liability disputed cases or cases where

causation is being argued by the defendant. The modelling work undertaken by Professor Fenn could have been substantially affected by these reforms and therefore the existing data sets are unlikely to be a representative sample. It is probable that a high percentage of the cases included in the data set are liability admitted RTA claims with a value of £1,000 to £10,000. Pre-issue data could include high volumes of cases settled under the predictable cost regime. We would argue that these cases do not give a true indication of the amount of work actually undertaken to successfully conclude a claim.

Public liability data

While the data for PL cases came from a variety of sources (local authority, insurer and claimant datasets), the actual definition of what constituted a PL was something which was agreed during the mediation which surrounded the original discussions around the setting of Table B. It is unclear which definition is going to be used in order to define this category of case, yet any deviation from what was previously agreed would make the resulting figures incompatible.

In addition, within the dataset itself, it is unknown whether data is a general PL “book”, including a breadth of PL claims such as slips and trips, product liability, claims involving animals to name a few, or if the data is limited to a certain category of cases. Either way, because of the inconsistency with comparing the PI PL scheme cases with general PI cases, the data is seriously flawed.

Employers’ liability data

The data currently available for EL cases includes both the liability admitted and the complicated liability disputed cases. With the introduction of a protocol of liability admitted EL cases, the liability admitted cases will all be outside of the fixed costs Fenn figures meaning that the figures included in annex B are too low and are unrepresentative for the liability denied cases.

Additionally, Fenn’s data set does not include diseases cases. The draft protocols that were consulted upon included single defendant disease cases. Is it proposed that if these cases fall out of the protocol, costs are then to be dealt with under the EL fixed fees at annex B? If this is so, it is wrong and irrational, as the data never included disease cases and it will mean that lawyers are not properly remunerated for the work required in these cases. EL accident and EL disease cases are very different in nature and will need to be costed separately. If this is not corrected many disease cases will become unprofitable to run and these claimants will suffer most in terms of access to justice. In addition to this, the data collected is based on the law as it is at the moment.

In addition to these reforms, if Clause 61 of the Enterprise and Regulatory Reform Bill is passed it will fundamentally change the way in which EL accident and short tail EL disease cases are run. This clause will prevent claimants from relying upon a breach of statutory duty as giving rise to a claim for compensation. Claimants will need to prove their claims in negligence. The Government’s own impact assessment of the effect of Clause 61 of the Enterprise and Regulatory Reform Bill states that investigating claims in negligence is more

time consuming and expensive[21]. They will become more expensive to investigate and litigate, and failure to take account of this will render the figures even more unreliable with the proposed figures even more irrational.

[21] Enterprise and Regulatory Reform Bill. Impact Assessment, Strict Liability in Health and Safety at Work Legislation page 9, paragraph 33

Appendix 1- Savings to the insurance industry

If we assume that the original estimate of *"almost 80% of all motor personal injury claims"*[22] will be covered by the portal, and that in 2011/12 there were 828,489 motor claims (as reported to the CRU)[23], this means that 662,791 claims should be captured by the RTA portal. However, according to the Portal Co. management information statistics for April 2012, 48% of claims entering the portal leave without resolution[24]. This should leave about 344,651 claims still in the portal.

Now if each claim is saving the insurance industry on average £76.14, based on the difference between the average costs pre-portal and post-portal detailed within *'Evaluating the low value road traffic accident process'* (July 2012)[25], then over a year – based on the 2011/12 claims figures – the insurance industry will directly save approximately £26 million in costs.

Calculation:
Pooled defendant dataset: mean costs by observation period - pre-portal £2,267.52; port-portal £2,191.37 = difference £76.14
Motor insurance claims, compared to all personal injury claims = 80%
No. of motor claims in 2010/11 (as reported to the CRU) = 828,489
80% of 828,489 = 662,791
No. of portal claims which leave the portal without resolution = 48%
52% remain in the portal
6*62,791 x 52% = 344,651*
344,651 x £76.14 = £26,241,727
Current annual saving = £26 million

Please note: It should also be remembered that this savings does not include efficiency savings within the insurance industry due to the automated claims process; therefore the actual savings are going to be even higher. For example, the aforementioned 'Evaluating the low value road traffic accident process' report states "[t]*he reductions in time to settlement found in this study (5-7%) were statistically significant and may reflect* ***in part*** *the administrative benefits of an electronic system by which the parties can communicate with each other" (*emphasis added, p.29). The low value RTA PI Protocol, and the draft extensions vertically and horizontally to it, all place increased onus on the claimant representative to carry out increased activity in a consistent and easily understood format with resultant savings to insurers which should result in lower premiums for the public. The Government must ensure there is a reliable mechanism to monitor that this is achieved.

In addition, Nick Starling (Director of General Insurance and Health, ABI said of the RTA portal that "[t]*here is evidence that it is producing significant consumer benefits and savings. Personal injury claims are dealt with in a matter of hours, rather than what was previously weeks or months, and that's a good thing."*[26]

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[22] http://www.rtapiclaimsprocess.org.uk/DOCs/MOJ%20reforms%20-%20implementation%20ABI%20FINAL%20release.doc
[23] http://www.dwp.gov.uk/other-specialists/compensation-recovery-unit/performance-and-statistics/performance-statistics/
[24] APIL Internal document - N:\RTA claims process\Portal Co meetings\2012 - Under TBE\PORTAL Co BOARD
[25] http://www.justice.gov.uk/publications/research-and-analysis/moj/evaluating-the-low-value-road-traffic-accident-process
[26] Q.107, Ev. 15 - House of Commons Transport Committee 'The Cost of Motor Insurance' Fourth Report of Session 2010-11 Volume 1 (HC591) - http://www.publications.parliament.uk/pa/cm201011/cmselect/cmtran/591/591.pdf

Appendix 2- Personal injury marketing and “referral fees”.

Otterburn legal consulting

APIL

Personal injury marketing and “referral fees”

December 2012

Personal injury marketing and “referral fees”

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Executive Summary

- Over the last year a simple and very powerfully argued proposition has been put forward - that if referral fees are banned, the fees paid to solicitors in respect of fixed fee personal injury cases can be substantially reduced resulting in savings for consumers and taxpayers;

- This short paper seeks to examine this underlying assumption and the potential impact of the proposed change on both the victims of accidents, and on the people who seek to represent them;

- The term "referral fee" has over the last year been applied very widely to embrace both the controversial practices of certain insurance companies and claims management companies, which are to be banned, but also marketing expenditure which is universally accepted as normal in the course of any business, which will not be banned. The use of this generic term has arguably complicated the picture, and made it more difficult to understand the actual issues involved;

- The very broad headline assertion that fixed fees can be cut by the amount saved with the referral fee ban is difficult to support because firms will still need to promote themselves. Such marketing activity is quite normal and occurs in all sectors, not least insurance. All businesses undertake marketing and there is a cost in acquiring all new customers, and in many cases it is substantial;

- Depending on their marketing expertise and ability, firms either undertake their marketing themselves or sub-contract to a third party – a marketing collective or claims management company - which generates the customers on their behalf. It is all marketing – the only difference is that one is done in–house, the other is provided as a service by a third party;

- When the referral fee ban is introduced in 2013 firms will still need to engage in marketing to win new business;

- Unless firms are able to cross-subsidise they will no longer be able to do this work profitably and will have to run down their personal injury departments. The result will be that victims of accidents will not be represented and many firms will be forced to close.

The equation becomes £500 - £700 = a loss of £200 and that is before calculating the actual cost of doing 10 hours work…

- In understanding the issues surrounding referral fees it is important to appreciate the wider issues surrounding insurance company economics and the potential opportunities this proposed change might provide to insurance company owned claims processors as they will have zero acquisition costs;

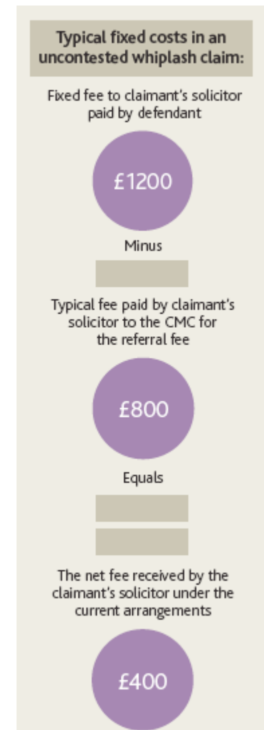
- The relatively high acquisition costs faced by personal injury firms is mirrored in general insurance where as much as 51% of a motor insurance premium can be spent acquiring the customer.

About the author

Andrew Otterburn is an independent law firm management consultant advising firms in the UK and Ireland. A chartered accountant, and initially a senior consultant at Grant Thornton, over the last twenty years he has advised over 250 firms on their strategy, management and profitability, and has provided management skills training for firms in Lisbon, The Hague and Brussels. He has undertaken extensive consultancy work for the Law Society of England & Wales, the Legal Services Commssion and the Ministry of Justice.

He has written a number of books including "Profitability and Law Firm Management" (Law Society 2007) and "From Recession to Upturn - financial management and strategy for law firms" (Law Society 2009). He is co-author of the Law Society of Scotland's annual Survey of Law firms in Scotland. He is Vice Chair of the Executive Committee of the Law Management Section; a founding member of the Law Consultancy Network; and a lead tutor for the MMU Postgraduate Certificate in Legal Practice Management.

Introduction



Over the last year a simple and very powerfully argued proposition has been put forward – illustrated in the box to the right - that if referral fees are banned, the fees paid to solicitors in respect of fixed fee personal injury cases can be substantially reduced resulting in savings for consumers and taxpayers[1]. Indeed, in November 2012, the Ministry of Justice issued proposals to reduce these fixed fees in order to reflect the forthcoming ban on referral fees.

There is an underlying assumption that with the ban on referral fees this expenditure will no longer be required and that fees can be reduced without any further consequences.

It is also apparent that the generic term "referral fee" has been used to describe a range of very different payments. These include the sale of the personal details of accident victims by insurance companies, as highlighted by Jack Straw, to marketing expenditure that is universally accepted as normal in the course of any business. The use of this generic term has arguably complicated the picture, and made it more difficult to understand the actual issues involved.

This short paper seeks to examine this underlying assumption and the potential impact of the proposed change on both the victims of accidents, and on the people who seek to represent them. We were asked to prepare it by APIL in mid December following the Ministry of Justice consultation launched on 19th November. There is very limited published data on the sector so we have instead sought to understand the present position by speaking to a selection of firms of solicitors who currently undertake this work and create a small number of case studies.

[1] Association of British Insurers – Tackling the Compensation Culture – September 2011

Marketing, acquisition cost and referral fees

As indicated above, some care needs to be taken when considering marketing in the context of personal injury solicitors because the generic term "referral fees" has, over the last year, been used very widely.

All businesses undertake marketing activities in order to acquire new business and in all sectors the nature of that marketing has changed radically in recent years, especially due to the internet.

Twenty years ago, most firms of solicitors did very little marketing with most of their work coming from existing clients or client recommendation. For some areas of work, such as private client or family, this continues to be the case, however other areas such as conveyancing and personal injury (PI) have seen radical change in the marketing techniques used to obtain new clients.

In the same way that marketing has changed for lawyers, the insurance sector has also seen huge change, from work being generated via door-to-door salesmen or customers calling into local branches, to being generated mainly from the internet. For example, until relatively recently, Endsleigh Insurance[2] generated most of its work through a local branch network but in 2009 closed 119 of its branches and more than 80% of its enquiries now emanate from the internet.

Personal injury solicitors still receive some work from existing clients, or passing trade, however for most this work source is minimal. Most personal injury business today comes through television advertising, web site optimisation, pay per click or direct marketing. Many firms of solicitors lack in-depth experience of these forms of advertising and an alternative has been to buy leads from a third party – either a marketing consortium or claims management company - who undertake the marketing and sell the subsequent leads generated in return for a fee. In addition, some insurance companies have sold leads to personal injury solicitors.

For many firms these fees are simply another form of marketing, in much the same way as today most (but not all) insurance companies buy work from price comparison websites. They are simply different ways of generating work.

The "cost of acquisition" of new business and the length of time for a new customer to become profitable, has become a huge issue in many sectors, not least the insurance sector, and in particular in recent years due to the growing prominence of price comparison websites.

[2] http://www.moneywise.co.uk/news/2008-07-04/endsleigh-poised-to-close-branch-network

Case studies

Personal injury solicitors now operate in a very different world than just a few years ago. They employ a diverse and complex marketing mix and as with any business sector, different organisations choose to use different methods to capture clients. This mix of different marketing methods is illustrated by these case studies. They illustrate that:

- Not all firms doing PI work buy work in;
- One size does not fit all, with the cost of acquisition differing between:
    - firms and marketing approach;
    - between direct and indirect marketing.

We have included some figures kindly supplied by the case study firms, however we must stress that these figures and calculations are pitched at a very macro level. A more detailed analysis beyond the scope of this paper would be needed to differentiate between the portal/fast track part of the market (cases with compensation awards between £1,000 and £25,000) and multi-track (cases with compensation awards over £25,000). These case studies are intended to simply provide an overview.

Case study summary

The case studies highlight a number of points:

- The one firm selected that undertook no marketing is likely to close its personal injury department next year because work levels are so low;
- The firms that were buying work in (at least in this sample) were smaller practices that lacked in-house marketing expertise;
- Some of the larger firms had highly sophisticated marketing;
- These larger firms are niche PI firms – they are not "general practices". They are specialist PI firms with a strong understanding of the sector and how to generate business;
- The average acquisition cost of a client was approximately £700, with a range from £200 to £900;
- All of these firms (except one) have to rely on marketing to generate their business, and that marketing is expensive. If the fixed fees were reduced in the way that is being proposed this marketing would still be required however the firms would not generate sufficient profit to enable the work to be viable. Instead of earning a fee of £1,200 they would instead, under the MOJ proposal, be paid £500, out of which they would have to pay the marketing cost of winning the client, currently £700, together with the cost of actually doing the work. We understand these types of case typically take 10 hours work, so each case undertaken would lose the firm money.

Case study one – 2 people – no marketing

Staff in firm or PI department	2	Direct marketing	0
PI fees	£96,000	Indirect marketing - work bought from 3rd parties	0
PI fees as a % of the firm's fees	6%	Average acquisition cost	n/a

Firm one operates in a very traditional way - it does not buy work in and does very little marketing. It is part of a general practice in a city centre and relies on referrals from other departments and passing trade. One person is employed in its personal injury department, an experienced solicitor in her late 50's who, together with her secretary, generates fees of approximately £95,000, of which approximately half is in respect of personal injury. The balance relates to other civil litigation. The direct salary costs of the department are approximately £90,000 and once the department is allocated its share of the firm's overheads the department is making a loss.

With the proposed increase in the small claims limit to £5,000 for personal injury cases it is expected that much of the personal injury work will go and it is likely the fee earner will be made redundant. The firm, which acts exclusively for people seeking compensation for accidents, will cease providing this service.

Case study two – 8 people - £305,000 marketing spend

Staff in firm or PI department	8	Direct marketing	£5,000
PI fees	£1m	Indirect marketing - work bought from 3rd parties	£300,000
PI fees as a % of the firm's fees	30%	Average acquisition cost	Range £550 - £750

Firm two is also a general practice and has just 8 people in its PI department generating fees of approximately £1m. They spend approximately £5,000 on marketing but 80% of their work is acquired through a national solicitors collective marketing scheme with whom with which they spend just over £300,000 a year. The average case acquisition cost is in the range £550 - £750.

They have limited in-house marketing expertise but have recently launched a separate PI website although this has not generated any work to date. They have also employed a marketing person to assist with focusing the marketing budget and preparing for the many changes that they face.

The ban on paying referral fees would have a significant effect upon their future marketing commitments, and in the short term their case intake is likely to reduce. However this would be ameliorated by the recruitment of an in house marketing person together with some focused marketing activity.

Case study three – 15 people - £420,000 marketing spend

Staff in firm or PI department	15	Direct marketing	£10,000
PI fees	£1.4m	Indirect marketing - work bought from 3rd parties	£410,000
PI fees as a % of the firm's fees	23%	Average acquisition cost	£535

Firm three has 15 people in its PI department and generates fees of approximately £1.4m. They spent approximately £410,000 acquiring work from a marketing network in their last financial year. The acquisition cost per case is approximately £535.

This firm has also launched a dedicated PI website which is in its early days and has yet to generate very much work – so far approximately 10 leads.

Case study four – 50 people - £1.6m marketing spend

Staff in firm or PI department	50	Direct marketing	£1.4m
PI fees	£3.8m	Indirect marketing - work bought from 3rd parties	£200,000
PI fees as a % of the firm's fees	100%	Average acquisition cost	£850

Firm four employs 50 people and is expected to produce fees of just under £4m in the current year to 29/2/2013.

The firm buys some work from other organisations (£200,000) but spends a further £1.4m on its own marketing. The firm's average cost of opening a case is £850 including all media and other running costs. The firm's marketing approach is based around:

- Direct response television advertising;
- Targeting of most effective times and channels;
- Optimised website with lead capture and live chat option;
- Pay per click being used to support both TV and search engine optimisation.

Case study five – 70 people - £900,000 marketing spend

Staff in firm or PI department	70	Direct marketing	£400,000
PI fees	£7m	Indirect marketing - work bought from 3rd parties	£500,000
PI fees as a % of the firm's fees	100%	Average acquisition cost	£900

Firm five has 70 people and a turnover of just under £7m. In the year to 30th June 2012 it spent:

- £500,000 on buying in work – this generated 2,496 cases – an average cost per case bought of £200;
- £400,000 on direct marketing. This included significant expenditure on raising general brand awareness that did not relate directly to the level of incoming work. A more up to date and relevant figure, which corresponds more directly to the number of cases received, is estimated at £900 per converted case.

The firm provided an analysis of its 2011/12 marketing expenditure:

Pay per click	£136,000
2 x concentrated brand campaigns (micro-site & transvision screens)	£140,000
Other brand building	£24,000
Display ads	£83,000

The firm's online marketing activity can be broken down into:

- Pay Per Click - Sponsored search engine listings based on real-time bidding for various keywords. Can generally control spend however requires a great deal of daily management to work efficiently due to very high level of competition and cost. Primary source of online work generation

- Search Engine Optimisation - Strategy is to appear on the first page of organic search results via the creation of quality online content. A long term project requiring intensive onsite/offsite activity and tangible results may not be seen for several months after work. Secondary source of online work generation

- Display - Offsite banner adverts using a variety of wide targeting methods (location, demographic, activity). Requires a high number of views to drive brand awareness and capture interest of potential clients. Tertiary and supporting source of online work generation

Each of the above broad marketing areas also has major subcomponents. For example, PPC campaigns on Google perform differently to those on Bing; SEO involves web design, page accessibility, social networking; on Display different networks require different formats and styles of ads etc.

Case study six – 100 people - £1.5m marketing spend

Staff in firm or PI department	100	Direct marketing	£1.5m
PI fees	£5m	Indirect marketing - work bought from 3rd parties	0
PI fees as a % of the firm's fees	100%	Average acquisition cost	£550

Firm six employs just over 100 people and had fees in the year to 31st August 2012, of just over £5m. It is a niche PI firm and all its work is for claimants. It spent £1.5m on marketing and generated 2,790 cases – an average acquisition cost of £550 a case.

The firm itself made some useful observations about these figures:

"In understanding the average case acquisition cost it is important to realise that this relates to 'signed up clients' or 'retained cases' after we've been through a process of looking at leads, deciding which ones we want, telling the clients that and then getting them to retain us. After that point, we do not win 39-40% of our cases, it's what I suppose in the business world you would call 'churn'. That's why there is a difference in case acquisition fee from £550.00 to acquire a signed up case, to £1000 being the cost of the ones that you acquire and win on average. That doesn't mean that we would lose that many at trial although that certainly happens particularly on public liability cases, but after appropriate investigation, often after a disclosure application or getting disclosure at the end of a protocol period or getting medical records and looking over them or investigate it with witnesses, we realise we can no longer win and tell the client we can't continue further on a CFA. On those cases, we clearly write off an enormous amount of Work in Progress or costs and sometimes absorb small disbursements or if it's bigger disbursements, claim from an after the event insurer.

This doesn't mean we're bad at picking cases, it means that it is not clear in about a third of the personal injury cases that you look at, whether you're going to win or lost at the outset. **In very rough terms, one third you know you're going to win, one third you know you're not going to win but for a vast swathe of the injured public, the third in the middle you need to investigate which costs money and effort and that was the basis of the whole 'no win no fee' system with success fees recovered from the other side post Access to Justice Act 1999 replacing Legal Aid**.

The other obvious point to make is that the real problem with the proposed Table B fees or whatever proposed fixed-type costs you have once PL, EL and OL's have fallen out of any portal, is that **once you fix the costs, there is absolutely no incentive driving**

insurers to behave reasonably and deal pragmatically, efficiently and quickly with cases. There is, of course, a direct obvious financial incentive for insurers and other defendants to seek to frustrate and delay and string out in order that claimants run out of available budget and therefore can't pursue their claims as ably, if at all. Every claimant insurer knows that is precisely what they will do."

Case study seven – 200 people - £900k marketing spend

Staff in firm or PI department	200	Direct marketing	£900,000
PI fees	£15m	Indirect marketing - work bought from 3rd parties	0
PI fees as a % of the firm's fees	100%	Average acquisition cost	£729

Firm seven employs just over 200 people and has an annual turnover of approximately £15m. They undertake all of their own marketing and do not buy work in, instead spending, in the year to 31st March 2012, just over £900,000 on marketing. The firm only undertakes personal injury and it acts exclusively for claimants. Their advertising for last year and this year to date is summarised below:

	12 months to 31st March 2012	8 months to 30th November 2012
Marketing spend	£929,768	£438,877
Number of cases generated	1,164	602
Average cost per case	£799	£729

The marketing is primarily advertising on radio and television, signage, and internet based advertising. The firm also employ sales staff that are primarily dealing with insurance brokers, insurance intermediates, fleets, dealerships/repairers.

Case study eight – 300 people - £3.2m marketing spend

Staff in firm or PI department	300	Direct marketing	£3.2m
PI fees	£23m	Indirect marketing - work bought from 3rd parties	£100,000
PI fees as a % of the firm's fees	100%	Average acquisition cost	£888

Firm eight employs approximately 300 people and has a turnover of £23m. In the year to April 2012 they spent £3.2m on marketing and £100,000 on buying in work. One third of the marketing spend was allocated to printed press and directories, one third to TV and Internet, and one third to practice development.

The marketing spend generated 3,600 cases giving an average acquisition cost of £888.

Other sectors

As indicated already, all organisations undertake marketing activity and have a cost associated with the acquisition of a new client.

Considered in isolation, the costs indicated by the eight firms to acquire a new case may appear high, however interestingly other sectors experience similar high new business acquisition costs. The key is often the relationship between that cost and the income it generates and how long it takes to move into profit. For example:

- Research in the US suggests the cost of a new cell phone customer is $350, comprising commissions, phone subsidies and marketing. A customer paying $59.99 a month becomes profitable after month 8 and a $39.99 a month customer after month 11 (www.myrateplan.com);

- A regional UK accountancy practice estimate their marketing budget at £68,000, being £18,000 on a limited amount of advertising, their seminar programme, and a client newsletter, and a further £50,000 on sponsorship, a total of £68,000. Each year they might acquire 15 new clients, so the average acquisition cost per client is £4,500. Average fees for these new clients are £13,000, so the acquisition cost represents just over 33% of the first year's fees. The £18,000 direct marketing expenditure represents 1% of their fees[3].

[3] confidential research as part of this project

The insurance sector

There are very close parallels between personal injury and the insurance sector in terms of work processes – both have become highly commoditised with extensive use of technology, and both use very similar and sophisticated marketing methods.

Research published in 2011[4] indicated the relatively high acquisition costs insurers had to pay for motor insurance customers:

Channel	Acquisition cost per customer
Internet banners	£151.55
Cold list direct mail	£130.51
Television	£125.24
Directories	£103.82
Sponsored online searches	£88.13
Price comparison sites	£39.29
Recommendation and word of mouth	£11.82
Overall average	£78.48

The mean premium per customer was £294 for those acquired through traditional media and £381 from those recruited via price comparison sites. The latter are higher because price comparison sites attract customers whose premiums are typically higher than the general insurance market – they are often younger with higher risk profiles.

The mean premium income per customer (the profit earned) was £44 and £38 respectively – low margins which would only be helped if the volume of claims was substantially reduced through action by Government to make personal injury unviable. It is predicted that the growth of comparison web sites will serve to further erode insurance company profitability and threaten their current business model. Not only are premiums lower through these sites (in order to attract the business) but customer retention rates are significantly reduced – 34% compared to 69% through traditional channels.

It appears from this analysis that an insurance company might be paying as much as 51% of the premium in acquisition costs, and with an overall average of 27%.

[4] Robertshaw, Gary, An examination of the profitability of customers acquired through price comparison sites: implications for the UK Insurance Industry. Journal of Direct, Data and Digital Marketing Practice. Much of the analysis was based on unpublished data in respect of a FTSE 100 insurance company.

It is important to put the discussions surrounding referral fees in the wider context of these challenges facing the insurance industry. In particular, the 2011 research paper examined the implications of this changed market, especially in terms of acquisition costs and retention rates for the insurance company economic model. It did this via a hypothetical profitability model, as set out below:

Hypothetical profitability model

	Price comparison site	**Traditional channels**
Total customers acquired	1,000	1,000
Acquisition cost per customer	£40	£80
Total acquisition cost	£40,000	£80,000
Mean premium per customer	£381	£294
Mean premium income per customer	£38	£44
Total premium income	£38,000	£44,000
Retention rate	34%	69%
Cumulative profit/loss (year 1)	(£2,000)	(£36,000)
Cumulative profit/loss (year 2)	£10,920	(£5,640)
Cumulative profit/loss (year 3)	£15,313	£15,308
Cumulative profit/loss (year 4)	£16,807	£29,762
Cumulative profit/loss (year 5)	£17,315	£39,736

The research indicates the lower profitability of business generated via comparison websites, and in particular the issue of falling retention rates and insurance company brand loyalty. It raises serious questions about the ability of insurers to maintain their current economic model in the face of this challenge to their markets. It may well be tempting for some of these companies, no longer allowed to sell the details of their policy holders involved in accidents, instead simply to transfer the leads, for no referral fee, to an in house legal provider. This in-house service would deal with the claim, in a way which might appear to be much the same as personal injury solicitors do today. albeit probably un-regulated. The key advantage the insurance industry would have is that their acquisition cost would be zero.

Conclusion and summary

A number of important points emerge from this paper:

- The term "referral fee" has been applied very widely to embrace both the controversial practices of certain insurance companies and claims management companies, which are to be banned, but also marketing expenditure which is universally accepted as normal in the course of any business, which will not be banned. The use of this generic term has arguably complicated the picture, and made it more difficult to understand the actual issues involved;

- The very broad headline assertion that fixed fees can be cut by the amount saved with the referral fee ban is difficult to support because firms will still need to promote themselves;

- Such marketing activity is quite normal and occurs in all sectors, not least insurance. All businesses undertake marketing and there is a cost in acquiring all new customers, and in many cases it is substantial;

- Depending on their marketing expertise and ability, firms either undertake their marketing themselves or sub-contract to a third party – a marketing collective or claims management company - which generates the customers on their behalf. It is all marketing – the only difference is that one is done in–house, the other is provided as a service by a third party;

- When the referral fee ban is introduced in 2013 firms will still need to engage in marketing to win new business;

- Unless firms are able to cross-subsidise they will no longer be able to do this work profitably and, as in the case of case study one, will have to run down their departments. It might be possible to charge clients an amount in addition to their "recoverable" fee however clients may be unwilling to pay this. The result will be that victims of accidents will not be represented and many firms will be forced to close.

The equation becomes £500 - £700 = a loss of £200 and that is before calculating the actual cost of doing 10 hours work…

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