Ministry of Justice
Scottish Government
The Personal Injury Discount Rate
How it should be set in future

A response by the Association of Personal Injury Lawyers
10 May 2017

The Association of Personal Injury Lawyers (APIL) is a not-for-profit organisation with a 25-year history of working to help injured people gain access to justice they need and deserve. We have around 3,700 members, committed to supporting the association's aims and all of whom 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.

Any enquiries in respect of this response should be addressed, in the first instance, to:

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Executive Summary

Q 1

- The legal parameters of the discount rate should remain as they are, as stated in *Well v Wells*[1]. The most important principle when assessing appropriate solutions should be certainty and security of investment for the claimant. Forcing the claimant to expose their lump sum award to market risk will lead to damages being diminished, claimants being undercompensated and having to turn to the state for financial assistance to cater for their needs when their compensation is exhausted.

Q2

- It is impossible to know whether a claimant has been under or over-compensated until the claimant's death. In our experience, claimants start from a position of compromise: their legal representatives set out everything the client needs in the schedule of loss, but rarely will they receive the full amount.

Q3

- Claimants obtain the advice of an independent financial expert who will provide investment advice once the sum has been awarded. During the negotiations, in claims involving larger sums the claimant will usually instruct a financial expert who will advise on the advantages and disadvantages and investment risks of a lump sum/periodical payment order combination.

Q4 and Q5

- Our members tell us that they have never come across a claimant who has been advised to invest 100 per cent of their award in ILGS or any other single asset class. Under the 2.5 per cent discount rate regime an investment solely in ILGS would have generated insufficient income to offset the effects of the discount rate and the claimant would risk running out of funds before the end of their life, leaving them to rely upon the State for their long term care needs. Even now that the discount rate has changed, it would not be good practice to put all of the claimants investment 'eggs' in one basket.
- The availability of Index-Linked Government Stock (ILGS) enables the Court to consider a theoretical framework within which a claimant could invest.

Q6

- There are various instances where PPOs are not and could not be made available. APIL surveyed its Damages Special Interest Group members to ask them about this. Their responses were useful and provide consistent evidence of the instances, which are set out in detail in our answer to this question.

[1] [2008] EWHC 919

Q7

- In most cases a claimant will want both a lump sum to meet immediate expenses and a PPO to provide the security of annual payments for life to pay for care and therapies.
- Claimants look to their solicitors to advise them. A PPO offers safety and means that they are unlikely to run out of funds, which would leave them reliant on the State for their care at a future date. Solicitors are always going to recommend that a PPO is considered for at least part of the claim, because of this safety aspect.

Q8

- APIL surveyed its members who reported that while the discount rate has been leading to under-settlement with lump sum only awards, there has been an increasing trend to accept a PPO where the client has suffered serious injuries.
- There are several factors driving changes in the popularity of PPOs which are set out in detail in our response to this question.

Q9

- All claimants should receive investment advice about lump sums, PPOs or combinations of the two.
- There remains a significant proportion of consumers with low levels of financial capability.
- APIL surveyed its members and asked them about the type of financial advice they offered to their seriously injured clients.

Q10

- We believe that the legal parameters of the discount rate should remain as they are, as stated in *Well v Wells*. The most important principle when assessing appropriate solutions should be certainty and security of investment for the claimant. Forcing claimants to expose their lump sum award to market risk will lead to damages being diminished, claimants being undercompensated and having to turn to the state for financial assistance to cater for their needs when their compensation is exhausted.

Q11

- We do not think the law should be changed.

Q12

- We consider that for the purposes of setting the discount rate the assumed investment risk profile of the claimant should be assumed to be very risk averse or “risk free” as set out in *Wells v Wells*.
- It is safe to assume that in the majority of cases, the injury suffered by the claimant will have been the worst thing ever to happen to them. They should be allowed to be a risk averse, safe investor, so that they do not have to worry about the possibility that their funds may run out before their life is over, leaving them at the mercy of the State for their care.
- We know that third party insurers – those who pay damages on behalf of the insured defendant – object to the claimant being in the position of a risk-free investor. They

suggest that at the very least, the claimant should be assumed to be a low risk investor with a mixed portfolio.

- If the government seeks to overturn *Wells v Wells*, and the adoption of option b or c (which we vehemently oppose) then management of such funds will effectively become compulsory.
- In these circumstances the additional costs of investment and investment management must to be met by the tortfeasor.

Q13

- The availability of periodical payment orders should work (as it does now) alongside and independent of the discount rate. They are different solutions for different issues (as we have discussed above) and invariably a well advised claimant will accept a settlement which combines the two.
- Refusal to take a PPO is not an indicator of an increased appetite for risk.

Q14

- We do not agree that the discount rate should be set on the basis that claimants opting for a lump sum should be assumed to be willing to take some risk.
- The claimant has no choice in the matter – any outcome is likely to be as a result of compromise and not choice.
- There are a number of reasons why a claimant might opt for a lump sum over a PPO, on the basis that it best meets their expenditure needs, none of which should expose the claimant to any additional risk. We set out those reasons in detail.

Q15 and Q16

- There should not be different rates for different types of cases.
- *Roberts v Johnstone*, which relates to a head of damage (rather than a type of case) is an exception.
- There remain problems, regardless of the level of discount rate, where a disabled claimant needs specially adapted or designed property: here the collision between the discount rate and the *Roberts v Johnstone* calculation creates particular problems. We set them out in detail.

Q17 – 19

- In our view the court should retain its power to apply a different rate from the specified rate where it is appropriate to do so within the current constraints set out in the Damages Act 1996, section 1(2).

Q20

- We agree that the law should be changed so that the discount rate has to be reviewed on occasions specified in legislation.
- It is an unfortunate truth that had the Lord Chancellor, in 2011, exercised his power to review the discount rate in a timely manner, the ‘shock’ which the insurers now claim to be suffering would have been greatly lessened: sixteen years is too long to leave the rate unchanged.

Q21

- This question cannot really be answered until the method of calculating the discount rate is known. The Ministry of Justice is advised to decide on the methodology of calculating the rate and then consult again on review frequency.
- Sixteen years was too long to wait for a review because the discount rate no longer reflected the true rates of return available in the market, and had not done so for many years. But less than five years between reviews is likely to be too frequent, as it will lead to uncertainty in calculating high value claims, stalling tactics by either set of parties as the next review looms all too frequently and will affect the administration of justice in the courts as outlined above.

Q22

- The review should commence in the second quarter of the year so that the announcement to set the rate can be made to coincide with the publication of the Annual Survey of Hours and Earnings (ASHE) figures in the final quarter of the year.

Q23

- We do not agree that the rate should be reviewed at intervals determined by the movement of relevant investment returns. The claimant is not an ordinary investor and the invested damages award must be protected – not used to play the stock market.
- A rate triggered by and set at review intervals determined by the movement of relevant investment returns would be distorted by the volatility of the market, and it is clear that volatile movements should not trigger a review for that reason.

Q24

- In order to ensure there is certainty in the conduct of personal injury claims affected by the discount rate, review dates or review periods should be left intact once they have been included in legislation and implemented. An orderly method, free from options for arbitrary triggers which can be pulled by any interested parties, at any time, must be implemented.

Q25

- While we can see that some parties might argue that there should transitional provisions when a new rate is commenced, in practice, transitional provisions are likely to cause litigation headaches for all concerned.

Q26

- Setting the discount rate should be depoliticised. There should be a panel of experts which sets the rate. The panel should be independent of government and should be empowered to review the rate and then implement the revised rate. It should not, as was the case with the most recent review, simply advise the Lord

Chancellor or other Minister of State and leave it to the Lord Chancellor’s discretion as to whether to amend the rate and if so, by how much.

Q.27, Q.28, Q.29, Q.30

- The current law relating to PPOs should not be changed by creating a presumption that if a secure PPO is available it should be awarded by the court. The claimant should not be forced to accept a PPO against his or her wishes and/or regardless of the claimant’s professional financial advice. We know that the drivers towards acceptance of PPOs by both claimants and defendant insurers are working: now that the discount rate has been reduced they are more attractive to both parties. There is no need to further *legislate* to enforce their provision in this way.
- There are, however, a few *non-legislative* changes which would further promote the use of PPOs where they are most appropriate.
- There is a market for a new, government backed PPO product: to offer a financial product to certain classes of claimant so that they can purchase a suitable property without the need for a large lump sum award, allowing the PPO to include repayments for a mortgaged purchase instead. We urge the government to explore this idea.
- In Scotland the Court rules do not cater for PPOs and they are only available if both parties put them forward. The rules should mirror those in England and Wales.

Q34

- Impact assessment: it is clear that removing the risk-free assumption as the basis for full compensation will have a detrimental effect on those with protected characteristics: those who benefit from awards which are affected by the discount rate are by their very nature disabled, young, old and infirm. Children and mothers injured as a result of birth negligence are injured by reason of pregnancy and maternity: they are also protected characteristics

Criticisms of the law

Criticism of the way in which the law provides for the discount rate to be calculated comes from those who, as the wrongdoer and cause of the claimant's injuries, are obliged to pay compensation. It is inevitable that these individuals and organisations will complain that the law in unfair: their shareholders' dividends and the bonuses of their staff and directors are affected when the discount rate is calculated in such a way as to ensure that previously under-compensated claimants are properly compensated instead. In this article: *Ogden: a very human cost*, the author describes the 'human cost' of the altered discount rate in terms of lost bonuses which will lead to insurance company staff having to cancel a planned holiday or postpone building an extension on their home.[2]

As Lord Scarman said in *Lim Poh Choo v Islington Area Health Authority*[3] "There is no room here for considering the consequences of a high award upon the wrongdoer or those who finance him. And, if there were room for any such consideration, upon what principle, or by what criterion, is the judge to determine the extent to which he is to diminish upon this ground the compensation payable?"

Criticism based on the effects of the discount rate upon the wrongdoer should be discounted as being the complaints of those who are obliged by law to put the injured person – harmed through no fault of their own – back in the position that they would have been in, but for the wrong committed against them (Lord Blackburn in *Livingstone v Rawyards Coal*, 1880).

Two notes on this response:

- Some of the questions in the consultation run on and into one another. For this reason, we have grouped some of the questions to avoid repetition.
- We are disappointed that the Government allowed a very short consultation period. The consultation asks 36 questions. Many of those questions explicitly require the provision of evidence on an issue that is complex and requires detailed analysis. APIL has gathered as much relevant evidence as is possible to maximise the utility of its consultation response within the restrictive timescale imposed. Despite that time constraint, it is hoped that this response will enable the Ministry of Justice to reach an informed decision on the personal injury discount rate. We have written to the Ministry of Justice to outline our concerns in more detail.

[2] *Ogden: a very human cost*, https://www.consumerintelligence.com/articles/ogden-a-very-human-cost and Appendix page 2

[3] Lim Poh Choo v Islington Area Health Authority [1980] Ac 174

Q 1 Do you consider that the present law on setting the discount rate is defective? If so, give reasons.

1. A note on the commentary to this question at paragraph 29: the class of personal injury claimants in receipt of awards to which the discount rate is applied ***will always be*** seriously injured. The discount rate is applied to future losses which will accumulate for every year that the claimant remains alive and injured. PPOs in particular are not so common in cases worth £1m or less.[4] Such losses are not incurred by those who are not seriously injured and for whom recovery is likely.

2. APIL welcomes the opportunity to respond to this consultation on the discount rate. We believe that the legal parameters of the discount rate should remain as they are, as stated in *Well v Wells*[5]*.* The most important principle when assessing appropriate solutions should be certainty and security of investment for the claimant. Forcing the claimant to expose their lump sum award to market risk will lead to damages being diminished, claimants being undercompensated and having to turn to the state for financial assistance to cater for their needs when their compensation is exhausted.

3. APIL is concerned that this consultation is pre-occupied with changing the legal parameters governing the way in which the discount rate is set for the wrong reasons. We hope that the Ministry of Justice has not been influenced by the insurer lobby assertion that 'a reduction in the [discount] rate could cost the insurance industry billions of pounds.'[6]

4. Not only is this assertion made without any supporting evidence, but in fact the rate of return on ILGS yields has, for the past ten years, been sliding in a downwards direction and has stayed significantly below the current discount rate. For example, the average yield for the 36 months leading up to November 2010 was only 0.84 per cent and has continued to fall steadily since then.

5. This means that defendants were quietly reaping the financial benefits of the 2.5 per cent discount rate for years until it was changed in March 2017.

[4] Institute and Faculty of Actuaries Periodical Payment Orders Working Party Update, GIRO 2015 Update Report by the Periodical Payment Orders Working Party: http://bit.ly/2pBE68z

[5] [2008] EWHC 919

[6] See Insurance discount rate debate: A fundamentally flawed decision that could cost the sector billions by James Dalton, City AM: http://www.cityam.com/259541/fundamentally-flawed-decision-could-mean-insurance-costs (See appendix page 4)

Q2 Please provide evidence as to how the application of the discount rate creates under or over-compensation and the reasons it does so.

6. It is impossible to know whether a claimant has been under or over-compensated until the claimant's death. Several of our members act as professional deputies and in their experience, they say that in claims where, for example, the claimant has died prematurely (i.e. before the expiry of the calculated life expectancy) there is usually very little left of the compensation which falls to be included in their estate.

7. In our experience, claimants start from a position of compromise: their legal representatives set out everything the client needs in the schedule of loss, but rarely will they receive the full amount.

8. So, while the claimant is entitled to 100 per cent compensation, more often than not, once the joint settlement meeting (JSM) takes place (this is a formal meeting convened by the parties, to try to settle the claim. It usually takes place at a relatively late stage in the claim and can be a very effective method of negotiation), the advisors will give clear advice to the client to concentrate on the most important aspects of the claim and compromise, if required, on others.

Q3 Please provide evidence as to how during settlement negotiations claimants are advised to invest lump sum awards of damages and the reasons for doing so.

9. Claimants obtain the advice of an independent financial expert who will provide investment advice once the sum has been awarded. It is unlikely that advice about investment of the lump sum will be sought during the negotiations, although at that stage, claimants with larger claims (those where the sums under discussion are £1m or more in particular) will inevitably instruct a financial expert who will advise on the advantages and disadvantages and investment risks of a lump sum/periodical payment order combination (where available) if not the actual investment strategy. [7]

[7] See paragraph 23 of Paul Rosson's report at Appendix page 21 and paragraph 38 of Mark Holt's report at Appendix page 62.

Q4 and Q5

Q4 Please provide evidence of how claimants actually invest their compensation and their reasons for doing so.

Q5 Are claimants or other investors routinely advised to invest 100% of their capital in ILGS or any other asset class? Please explain your answer. What risks would this strategy involve and could these be addressed by pursuing a more diverse investment strategy?

10. Our members tell us that they have never come across a claimant who has been advised to invest 100 per cent of their award in ILGS or any other single asset class. Under the 2.5 per cent discount rate regime an investment solely in ILGS would have generated insufficient income to offset the effects of the discount rate and the claimant would risk running out of funds before the end of their life, leaving them to rely upon the State for their long term care needs.[8]

11. Even now that the discount rate has changed, it would not be good practice to put all of the claimants investment 'eggs' in one basket: it is right that the very low risk is spread across a range of investments. It is rather early to say what claimants will now do as cases under the new rate are only just starting to settle. Claimants will still have a need to stay ahead of inflation, which is not easy without investing to some degree, and will need a home for cash which is secure and within FSCS limits. The values of long dated ILGs have fluctuated significantly in recent years although short dated ones less so and there is a real risk of capital loss to claimants if, for example, they had to sell some of their ILGs to meet a need for income which was greater than the yield from those, or to meet a capital need when values of ILGs were suppressed. Clients are not advised to place all of their eggs into one basket.

12. In their report to the Lord Chancellor, the expert panel explain why ILGS are used as benchmark when calculating the sums due:

13. "The availability of Index-Linked Government Stock (ILGS) enabled the Court to consider a theoretical framework within which a claimant could invest in a portfolio of

[8] See paragraphs 71 – 73 of Paul Rosson's report, Appendix page 31. See also section 4 of Mark Holt's report at Appendix page 62.

ILGS which, if held to redemption in an adequately structured portfolio, would provide for the future losses or costs as they fell due, without risk of erosion through inflation (to the extent the loss in future would have moved from current levels in line with the RPI, the basis of indexation of ILGS), or loss of capital. The availability of ILGS then provided the most accurate way of assessing the value of future losses in real terms (at least relative to RPI inflation)."[9]

14. "… from an actuarial perspective, the valuation of personal injury compensation falls into the matching framework of discounting practice. This is a market consistent approach and in these circumstances ***the nature of the assets held in respect of the liability is not considered relevant. Risk free term dependant discount rates should generally be used irrespective of the underlying assets held in respect of the liability.***

15. 'When valuing compensation payments fixed in nominal terms this would support use of nominal discount rates measured by market yields on conventional gilts or longer term swaps. When considering inflation linked compensation the corresponding investment class providing market related risk free real rates of return would be ILGS …. It is notable that essentially the same principles were adopted in Wells -v-Wells, their Lordships anticipating subsequent developments in actuarial practice. ***The risk free rate was used and the actual assets subsequently invested in by the claimant were not considered relevant*.**"[10] (Our emphasis).

Q6 Are there cases where PPOs are not and could not be made available? Are there cases where a PPO could be available but a PPO is offered and refused or sought and refused?

Please provide evidence of the reasons for this and the cases when this occurs.

16. There are various instances where PPOs are not and could not be made available. APIL surveyed its Damages Special Interest Group members to ask them about this. Their responses were useful and provide consistent evidence of the instances:

[9] The Discount Rate: A report for the Ministry of Justice prepared by Paul Cox, Richard Cropper, Ian Gunn & John Pollock 7 October 2015, Paragraph 1.7

[10] Ibid paragraph 2.11

- **Mutual/self insured defendants**

17 This is a particular issue: insurers which are Lloyds syndicates (particularly those which pre-date 1st January 2004) and medical insurers (which are mutuals) are not considered to be a ‘secure provider.’ Our members’ examples of this:

- o A defendant GP backed by the Medical Defence Union (MDU): a PPO would not be deemed ‘secure’ (because the MDU is not covered by the UK Financial Services Compensation Scheme (FSCS);
- o Other claims against medics such as student doctors, doctors in training and hospital doctors insured by the Medical Protection Society (MPS) which is not considered a “secure provider;”
- o A claim against a local authority which was self-insured and did not meet the criteria for a PPO;
- o Also claims where the defendant RTA insurer is a Lloyds syndicate will not be considered a "secure provider."

- **Insufficient insured indemnity cover**

18. Members report that this is an issue where the limit of indemnity on the defendant’s insurance policy (either an employers’ liability(EL) or public liability (PL) policy) or where there is a fixed indemnity limit of £10m. One member whose client was in this situation reported that if his client had taken a PPO, the fund could not have provided enough to fund payments beyond the age of 55 (and the client’s life expectancy was longer) so the claimant opted for a lump sum instead.

- o An APIL member described one of his current claims: “I have a current claim where the employers’ liability (EL) insurance indemnity limit, commonly £10m, will be insufficient to fund a care PPO for life even at a discount rate of 2.5% and allow for a lump sum and the payment of costs. The claimant is 22 years old and has a normal life expectancy. With the current discount rate, EL policies will have to move to higher or unlimited cover. Or smaller employers will risk going bust where cover is insufficient.”

- **Fatal/terminal cases**

19. In fatal accident dependency claims PPOs are not available because the original victim is already dead and the period for which the lump sum for future losses is calculated

depends on a theoretical calculation of how long the deceased would have lived but for their fatal disease or accident.

20. Similarly, claimants who have asbestos induced disease: PPOs are not suitable as the claimant's condition is usually terminal.

- **Scotland**

21. PPOs are not routinely available or offered in Scotland. The problems include a lack of legislative framework or court rules to facilitate them. Generally, when PPOs are (rarely) used, it tends to be in cases against a government body. One of our Scottish members told us: “PPOs are the exception in Scotland at the moment. I have only used a PPO on one occasion.”

- **Foreign insurers**

22. Claims against insurers based overseas are not considered ‘secure’ for the purposes of PPOs because they are not covered by the UK Financial Services Compensation Scheme (FSCS). This includes claims against P&I Clubs for shipping related accidents. In such claims, which can include RTAs abroad (including Europe) aviation claims and other non-domestic accidents, PPOs are simply not an available option.

- **Defendant attitude**

23. Our members also report that insurers are often reluctant to offer PPOs to settle the claim. This is understandable from their point of view: insurers work on the basis that the claim is paid and the ‘book’ is closed. Offering a PPO goes against this working practice: the ‘book’ has to remain open for the duration of the PPO, with long term administration costs and an ongoing balance sheet liability.

24. Ironically, the defendant attitude changes when the claimant does not have capacity: in those cases (children, brain injured claimants and other patients lacking mental capacity) the settlement requires court approval and the court will want to know why a PPO has not been offered. APIL members report that in such cases, insurers are more likely to offer a PPO as part of the settlement package.

25. Our members have provided detail when surveyed on this point. They say:

- “In quite a few cases (against an insurer) it has been made absolutely plain at the outset of a joint settlement meeting (JSM) that the claimant’s desire for some of their future losses will not be met with a PPO and in fact so much so that all recent attempts to get a PPO have failed. In these circumstances clients simply do not want to keep going with their litigation to trial just for the chance of getting the court to award them a PPO.”
- “Often, compensators will say that they are unwilling to agree a PPO and the claimant would have to go to trial to get one.”
- “The defendant insurers were not willing to make offers with PPO elements but the claimant wished to settle. The client needed financial advice in relation to the premium reasonably required to buy off the PPO.”
- “On three occasions in the last 18 months defendants have refused to settle using a PPO despite this being the claimant's preferred option and instead they have offered an enhanced lump sum.”
- “On the case I settled at the end of November 2016 the defendant argued that PPOS were not required or necessary until right at the end of the case; it had been going for about five years.”

- **Contributory negligence**

26. Where there are high levels of contributory negligence involved in the claim, the claimant usually finds it very difficult to make a PPO ‘work’. For example, a £100,000 claim subject to 50 per cent contributory negligence would make it difficult for the claimant to find enough to fund a proper level of periodical payments for care. The claimant would need to capitalise the lump sum in order to pay for a proper care regime.

    - A member provided the example of a case where the claimant recovered 45 per cent of damages and the defendant would not entertain the idea of a PPO.

    - Another member described a claim where the client required 24 hour care. However, owing to issues of contributory negligence the defendant would not agree to a PPO.

- **Other novel aspects**

27. Members also provided details of other claims where a PPO was not offered or available:

    - “A claim for damages for wrongful conception leading to birth of severely disabled child, as the mothers claim for cost of bringing up child it is not a personal injury claim and so does not qualify for PPO - although we are trying to persuade the NHSLA otherwise!”

    - “A dependency claim under the Fatal Accidents Act for two adult sons who would not have usually qualified for such a claim but for the fact they have learning difficulties and so were unusually dependent upon their father at the time of his death.”

Q7 Please provide evidence as to the reasons why claimants choose either a lump sum or a PPO, including where both a lump sum and a PPO are included in a settlement.

28. In most cases a claimant will want both a lump sum to meet immediate expenses and a PPO to provide the security of annual payments for life to pay for care and therapies.

29. Where some of the future heads of loss which would otherwise be the subject of a PPO are needed to augment the lump sum received, (which may have been reduced by a percentage to reflect the litigation risk of contributory negligence), to ensure that the claimant's needs are satisfied, those portions can be used and added to the basic lump sum and the balance can be paid as a PPO.

30. Claimants look to their solicitors to advise them as to what to do for the best. A PPO (when available and suitable) offers safety and means that they are unlikely to run out of funds, which would leave them reliant on the State for their care at a future date. Solicitors are always going to recommend that a PPO is considered for at least part of the claim, because of this safety aspect.

31. We surveyed our members who provided illustrative detail. Here are representative examples:

- “An ongoing cerebral palsy case where there is a significant dispute over likely life expectancy. PPOs linked to ASHE[11] for care costs will give security for the family of knowing that the claimant’s care needs can be met however long she lives and will keep pace with any increase in hourly care rates. However a lump sum for other heads of loss will give maximum flexibility re providing optimum therapy and equipment needs as and when these needs arise in practice.”

- “Brain injured man in his 20s who will not work again and has hemiparesis. He has good communication skills although lacks capacity to manage his financial affairs. A lump sum enabled his deputy to purchase and adapt a property to enable easy wheelchair access within the home. A PPO provides life-long security and provides for an increase in rate at age 60 when care needs will increase.”

- “Child aged 9: life expectancy to age 70. Parents in their 40s. So there is a need for care for rest of the child’s life. Parents' priority is (1) to provide accommodation and (2) for their child to be cared for, for rest of the child’s life. A PPO offered reassurance for the parents that their child would have income to pay for care after they were dead. The lump sum element meant that a house could be bought/adapted and child would always have somewhere to live.”

- “Most of cases settle on a lump sum and PPO basis which gives the claimant a sum of money to purchase a property and have a bit of a buffer and then the PPO to pay for annual care costs. They then don't have to worry about finding enough money to pay for care as it raises in accordance with ASHE 6115[12].”

- “Claimant suffered a spinal cord injury. He was in his early 40s, rendered tetraplegic. He was single and lived alone: was unable to work or care for himself. He has a relatively long life expectancy and it is important that his future care will be paid for - a PPO was perfect for this need. The claimant also needed a new home as his current accommodation was entirely unsuitable. A lump sum has allowed him to move into a more suitable home.”

[11] Annual Survey of Hours and Earnings (ASHE) figures (which are used to calculate future nursing care costs. *Thameside & Glossop v Thompstone* [2008] 1 WLR 2207 confirmed that ASHE (6115) was the correct measure for the indexation of future care costs.
[12] ibid.

Q8 How has the number of PPOs changed over time? What has driven this? What types of claims are most likely to settle via a PPO?

32. Just over half of our members surveyed (57.14 per cent) indicate that in their view, the number of PPOs offered/accepted has not changed over time. While the discount rate has been leading to under-settlement with lump sum only awards, though, there has been an increasing trend to accept a PPO where the client has suffered serious injuries. 26.32 per cent of our surveyed members indicated this increasing trend, while 12 per cent noted that insurers have, during the same time, been making more PPO offers to their clients. Longer life expectancies in particular, and improvements in medical treatment/care outcomes both mean that more severely injured claimants are surviving and then living for longer.

33. Only seven per cent of our members indicated that in their view, PPOs have become less popular with seriously injured clients.

34. The latest available GIRO report[13] produced by the Institute and Faculty of Actuaries indicates that demand for PPOs had fallen by 2015, (date of latest data available) but acknowledges that insurers' anticipation of the impending discount rate change had affected that demand. As the discount rate had become increasingly out of kilter, PPOs became less attractive to insurers for the bigger claims which were more likely to benefit from them. Conversely, now that the rate has changed, we expect to see PPOs become offered more widely. See below.

What is driving any change? What types of claims are most likely to settle via a PPO?

35. Ironically, the change in the discount rate since March 2017 has been one of the main drivers for changes in defendant insurers' attitudes towards PPOs. They effectively offer a '0% discount rate' and can prove less expensive than a lump sum calculated under the new rate. By adjusting the rate to the correct market position, PPOs have become an attractive proposition for both claimants and defendants[14].

36. As to what else is driving the change (where appropriate) and which claims are likely to settle with a PPO, it again depends on the circumstances:

[13] Institute and Faculty of Actuaries Periodical Payment Orders Working Party Update, GIRO 2015 Update Report by the Periodical Payment Orders Working Party: http://bit.ly/2pBE68z
[14] See for example paragraphs 23 - 25 of Mark Holt's report at Appendix page 57.

- **Foreign insurers – no change**

37. There can be no real change here, unless the foreign insurers are backed by the equivalent of the FSCS or MIB in their own jurisdiction.

- **NHSLA – increasingly popular**

38. APIL members report that the NHSLA/NHS Resolution now is keen to include more heads of loss in a PPO following the discount rate change. Our members' comments illustrate this:

    - "The NHS tends to offer PPOs. Insurers tend to prefer to offer a premium on the lump sum to buy off the PPO. In my view this is down to the financial uncertainty of a PPO having a negative impact on the insurer's balance sheet."

    - "In Northern Ireland medical negligence claims are usually dealt with by PPO if the claim has a potential value of over £1m."

    - "Only the NHSLA seem happy to routinely consider PPOs. I am not yet sure how the current new discount rate will cause a change of heart with insurers."

- **Long term needs security – more popular**

39. For claimants with long term needs, PPOs offer financial security & stability, particularly when they are index linked to ASHE 6115 for care costs.

40. Our members also report that there is increasingly an understanding on the part of some insurers that a settlement for a person who lacks capacity will only be approved by the court on the basis of a PPO, as mentioned above (see para 24 above and 44-46 below) and so that encourages insurers to offer PPOs to these claimant types. Members' comments add more detail:

    - "Taking the guess-work out of managing awards to secure future care is a key factor for many clients but even with PPOs, care is needed in relation to expenditure on care and case management and economies need to be made where possible."

- “My clients like having a guarantee annual income, reducing the risk that they could be caught short. Perhaps my clients are quite risk adverse so do not have the confidence their lump sum will benefit them. If there was not so much risk and / or there was a better return in lump sum payments, then the need for PPOs would reduce.”

- “There has been a sea change since the change in the discount rate in insurers’ attitudes [towards PPOs] and since then PPOs have become more available. I had found that PPOs were unpopular with defendants prior to this and they preferred lump sum settlements. Clients like the certainty of PPOs as they provide the reassurance that they are financially covered for life for their [ongoing] needs.”

- “Simply the certainty in terms of longevity and cost (expense) from a PPO has meant nearly all clients to whom it was offered preferred that option. If the discount rate [change] has done anything, it has given such clients another option.”

- **Life expectancy – more popular**

41. In cases where life expectation is uncertain, PPOs are usually preferable and clients like the reassurance of knowing that the PPO will continue for life, however long that may be. Young claimants are more likely to want a PPO for losses such as care where they have a long life expectancy and want the certainty of knowing the compensation will last.

42. In our view, claimants are less willing to settle for a lump-sum-only award, where a full liability settlement has been achieved, given the issues on life expectancy, when they can have the certainty of care needs being met for the remainder of their life.

43. Our members comment:

    - “Cases where there will be a need for life long care and/or an increase in care needs as the claimant ages are suitable for PPOs. They give security to claimant and family. They know that they will receive a yearly payment for the rest of the claimant's life to pay for care and case management (and other future loss if required). It also ensures that if the claimant lives beyond the anticipated life expectancy; this tax free sum continues until they die and is RPI linked. With a lump-sum-only award the money could run out as life expectancy is a statistical calculation and may not reflect the actual life expectancy achieved."

- **Defendant behaviour**

44. Where the major part of the claim is care and case management and the settlement will require court approval due to a lack of claimant capacity, (who is either a child or has suffered brain damage) then defendant insurers know that they cannot deny a PPO: it is hard for claimant counsel to recommend a lump-sum-only settlement, especially on the old 2.5 per cent discount rate. The courts, in turn, are likely to view a lump-sum-only settlement as inappropriate, especially if they see advice from an independent financial advisor (IFA).

45. Unfortunately, it is those cases where court approval hearings are not required, (where the claimant *does have* capacity) in which insurers have historically put far more pressure on claimants to settle without a PPO.

46. APIL members' comments add more detail to this:

    - "Insurers do not want an open book and all seem to prefer final damages on a lump sum basis even if this is more than they might have to pay if there was a PPO."

    - "The NHSLA and some insurers are happy to offer PPOs. However, most insurers dislike them (presumably due to reserving issues). Proceedings often need to be issued and a trial date arranged before defendants will pay up. Some defendants even refuse to make PPOs without the court ordering them (for an example of this, see the decision in *Farrugia*[15])."

    - "I think claimants want to be in control of their own funds and destiny. I believe that they lack trust in insurance companies and many financial institutions, especially since the problems back in 2008/2009."

[15] *Jack Farrugia v (1) Steven Burtenshaw (2) Motor Insurers Bureau (3) Quinn Insurance Ltd* [2014] EWHC 1036 (QB) Periodical payments for future care amounting to £255,109 per annum were awarded to a 22-year old man who had suffered severe brain damage in a road traffic accident: http://www.bailii.org/ew/cases/EWHC/QB/2014/1036.html

- “Some insurers are more attuned to offering PPOs, others do not offer them, preferring lump sum offers. For example, Ageas and Acromas have historically been more willing to put PPOs forward.”

- **Claimant behaviour**

47. Claimants also have their reasons for accepting or not accepting a PPO as part of their award. Some claimants do not want the wrong-doing defendant to be in control of their damages and may want to be in control of their own funds and destiny, preferring to have the freedom to use their award as they see fit by accepting a lump sum payment.

48. But this often changes once claimants have been given good financial advice. “Claimants can see the significant benefit of PPO's and I always fight for PPO where the IFA confirms they can be afforded” says one of our members.

- **Need to purchase adapted accommodation**

49. There is, however, the thorny issue of the cost of adapted accommodation. Particularly in London and the South East of England where property is so expensive, clients may need the purchasing power of a lump sum to help them sort out their accommodation needs. See our comments on the effects of *Roberts v Johnstone* below (see Q.15 and Q.16 paras 81-87 and appendix page 7).

- **Lower discount rate since March 2017**

50. PPOs have become more popular with defendants since the discount rate change. It was more expensive for defendants to pay PPOs before discount rate change when compared with paying a lump sum settlement. That has now changed (see Q.8, para 35 above).

51. With PPOs now offering a '0%' discount rate these are a more attractive option and insurers are now seeking ways to find solutions for other heads of loss where historically they had no interest with the rate at 2.5 per cent.

52. If the recent discount rate change has done anything, it has given clients another option in more cases.

Q9 Do claimants receive investment advice about lump sums, PPOs and combinations of the two? If so, is the advice adequate? If not, how do you think the situation could be improved? Please provide evidence in support of your views.

53. All claimants should receive investment advice about lump sums, PPOs or combinations of the two. A failure to provide investment advice is unacceptable. The Financial Conduct Authority reports in its business plan that "there remains a significant proportion of consumers with low levels of financial capability. Consumer behaviours and biases will always exist in financial decision making and are often exacerbated by low financial capability."[16] In our view, this contributes to the risk that the seriously injured claimant or the claimant's family (where the claimant lacks capacity, for example) takes the view that the most risk averse action they can take is to make a cash investment with their bank or invest in the only other truly risk free investment (other than ILGS): National Savings and Investments bonds.[17]

54. There is also a risk that claimants might overspend in the early years post-settlement and run the risk of depleting their funds during their lifetime.

55. APIL surveyed its members and asked them about the type of financial advice they offered to their seriously injured clients.

56. Sixty per cent of respondents indicated that their firm offers investment advice either in connection with lump sums, PPOs or both (56%). Only 11.85% of those offered the advice in-house: the majority (77.78%) referred their client to an external financial advisor while the remainder offered both options.

57. We questioned the 40 percent who indicated that their firm did not offer financial advice to these clients to find out what they did instead. The vast majority strongly recommend that the client seeks independent financial advice, and then either refer them on to an IFA or, if it is a Court of Protection case, they may offer the services of an in-house or externally referred Deputy. None of the respondents appeared to leave their clients without either financial advice or a referral on to an IFA or other appropriate professional provider. There is the risk, though, that clients are referred, but do not subsequently take up the offer of advice.

[16] https://www.fca.org.uk/publication/business-plans/business-plan-2017-18.pdf
[17] This is reiterated in the Ministry of Justice's research dated 29 October 2013, "*Revision to Personal Injury Discount Rate Research*" ISBN 978-1-84099-610-4. See page 47-8 for example.

Q10 Do you consider that the present law on how the discount rate is set should be changed? If so, please say how and give reasons.

58. We believe that the legal parameters of the discount rate should remain as they are, as stated in *Well v Wells*[18]*.* The most important principle when assessing appropriate solutions should be certainty and security of investment for the claimant. Forcing claimants to expose their lump sum award to market risk will lead to damages being diminished, claimants being undercompensated and having to turn to the state for financial assistance to cater for their needs when their compensation is exhausted.

59. Changing the legal parameters governing the way in which the discount rate is set would be done for all the wrong reasons. The Ministry of Justice should not be influenced by the insurer lobby assertion that 'a reduction in the [discount] rate could cost the insurance industry billions of pounds.'[19] As we have demonstrated in our answer to question eight above, re-setting the discount rate so that it is in line with the market has already acted as a corrective and is a driver towards encouraging more insurers to offer PPOs, reducing the investment risks faced by claimants, while securing their financial futures.

Q11 If you think the law should be changed, do you agree with the suggested principles for setting the rate and that they will lead to full compensation (not under or over compensation)? Please give reasons.

60. We do not think the law should be changed.

Q12 Do you consider that for the purposes of setting the discount rate the assumed investment risk profile of the claimant should be assumed to be:

(a) Very risk averse or "risk free" (Wells v Wells)

(b) Low risk (a mixed portfolio balancing low risk investments).

(c) An ordinary prudent investor

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[18] [2008] EWHC 919

[19] See Insurance discount rate debate: A fundamentally flawed decision that could cost the sector billions by James Dalton, City AM: http://www.cityam.com/259541/fundamentally-flawed-decision-could-mean-insurance-costs (appendix page 4)

(d) Other.

Please give reasons.

61. We consider that for the purposes of setting the discount rate the assumed investment risk profile of the claimant should be assumed to be very risk averse or "risk free" as set out in *Wells v Wells*.

Very risk averse or "risk free" (Wells v Wells)

62. Claimants whose damages are affected by the discount rate will be, by definition, severely injured: they will have continuing losses which will stretch into the future: losses of earnings due to their reduced or total loss of earning capacity: costs of future care to ensure that they are able to continue to live as independently or a safely as possible, without undue reliance upon the State.

63. The sole purpose of the discount rate is to ensure, as much as possible, that the lump sum awarded will generate in income what the claimant has lost over the period in question - no more and no less - and so put the claimant in the same position he or she would have been in, but for the injury.

64. It is safe to assume that in the majority of cases, the injury suffered by the claimant will have been the worst thing ever to happen to them. They should be allowed to be a risk averse, safe investor, so that they do not have to worry about the possibility that their funds may run out before their life is over, leaving them at the mercy of the State for their care.

65. Adults with care and associated needs may have been reliant on family or other gratuitous care for some time, particularly if there has been a liability dispute and they will be concerned about what might happen if that care is lost (for example, due to ill health of their gratuitous carer – often a spouse). This has a psychological bearing on their willingness to risk their award.

Low risk (a mixed portfolio balancing low risk investment).

66. We know that third party insurers – those who pay damages on behalf of the insured defendant – object to the claimant being in the position of a risk-free investor. They

suggest that at the very least, the claimant should be assumed to be a low risk investor with a mixed portfolio.

67. We also know that as a direct result of the 2.5% discount rate in force until recently, that claimants have had no option but to be low risk investors with a mixed portfolio.[20]

68. Seriously injured people are not investors – they are people who have been given a sum of money which they must protect and 'eke out' for the rest of their life, ensuring that they are housed, cared for and in receipt of appropriate therapies, all of which continually deplete their funds.

69. What safeguards would be put in place to protect claimants? If defendant insurers (and other defendants such as the NHSLA/NHS Resolution) want to save money by urging the Government to follow this approach, then they should bear the costs which will be incurred by the claimant to properly and prudently manage the funds.

70. Claimants are not financial experts. In order to have and manage a low risk balanced portfolio, financial expertise is necessary. To do this, it should to be acknowledged that the cost of managing such a fund ought to be met as part of the settlement. Currently the cost of managing a mixed portfolio is borne by the claimant.

71. There exists a stark unfairness at present: those who suffer a brain injury can claim the costs of a professional deputy (with all the experience the deputy has of managing funds for the seriously injured) with all the expenses that entails built into their award. But if a claimant is left paralysed, but with full mental capacity, there are not costs of financial assistance built into the award. Claimant lawyers do try to build those sums in, but the assumption made by defendants is that the investment advice will pay for itself.

Unacceptable risk inherent in options B and C

72. In our experience the UK economy suffers a boom/bust cycle every 15 years or so and that uncertainty means that if a claimant has to call on funds when the market is 'bust' – it will adversely affect his remaining award, inevitably to its detriment. At worst, leaving the claimant reliant, once more, on the State for future care.

[20] See for example paragraph 64 of Paul Rosson's report, Appendix page 30

73. This volatility creates what is known as 'sequencing risk:' The Government's own expert report describes this in detail:

- "Sequencing risk occurs where one year of below RPI investment returns is immediately followed by another, which is immediately followed by another etc. Poor investment return sequences combine with portfolio withdrawals in a highly destructive way because more fund units need to be enchased [*sic – encashed*] to generate the same annual income. The double erosion of capital following a market fall -the market drop and the drawing an equal income at depressed fund value -is what makes sequencing risk potentially destructive. One of the lessons of the technology boom and bust followed shortly by the financial crisis was the importance of the order, or sequence, of extreme investment returns. If a sequence of market drops means the capital of a fund is 50 per cent lower than planned, a 100 per cent gain is needed to return the fund to where it should be."[21]

- Claimants would need independent financial advice in this type of investment market: in particular, 'smaller' funds, which are usually averse to paying for advice out of the funds due to the risk of eating into the capital, risking fund depletion before the end of the claimant's life. Charges made to manage investments are typically between one and two per cent.[22]

74. If the government seeks to overturn *Wells v Wells*, and the adoption of option b or c (which we vehemently oppose) then management of such funds will effectively become compulsory.

75. In our view, in these circumstances the additional costs of investment and investment management must to be met by the tortfeasor.

76. In his article in a forthcoming edition of the Journal of Personal Injury Law, Edward Tomlinson writes, "any calculation to set a risk discount rate must recognise the cost of investing. In addition to inflation, both the charges and the taxation that will apply to the

[21] *The Discount Rate – a report for the Ministry of Justice prepared by Paul Cox, Richard Cropper, Ian Gunn and John Pollock*, 7 October 2015, Paragraph 4.15. See also Paragraph 4.20 for the downside risk measures used to determine whether an investment portfolio is low risk.
[22] See *The Discount Rate: What Next?* By Edward Tomlinson, 2017 J.P.I.L., Issue 2 (in full in appendix, page 8 onwards) and also *The Discount Rate – a report for the Ministry of Justice prepared by Paul Cox, Richard Cropper, Ian Gunn and John Pollock*, 7 October 2015, Paragraph 4.17 both of which confirm this.

return generated need to be allowed for in the methodology to calculate the discount rate. These figures will not be insignificant and will reduce the discount rate."[23]

Q13 Should the availability of Periodical Payment Orders affect the discount rate? If so, please give reasons. In particular:

- **Should refusal to take a PPO be taken as grounds for assuming a higher risk appetite? If so, how big a difference should this make to the discount rate.**
- **Should this assumption apply in cases where a secure PPO is not available?**

77. The availability of periodical payment orders should work (as it does now) alongside and independent of the discount rate. They are different solutions for different issues (as we have discussed above) and invariably a well advised claimant will accept a settlement which combines the two. Similarly, a well-advised insurer may take the view that a PPO is not an appropriate way to settle the claim.

78. Refusal to take a PPO is not an indicator of an increased appetite for risk.

Q14 Do you agree that the discount rate should be set on the basis that claimants who opt for a lump sum over a PPO should be assumed to be willing to take some risk? If so, how much risk do you think the claimant should be deemed to have accepted? Please also indicate if you consider that any such assumption should apply even if a secure PPO is not available. Please give reasons.

79. No, we do not agree that the discount rate should be set on the basis that claimants opting for a lump sum should be assumed to be willing to take some risk. The question assumes that the claimant has a choice in the matter – in fact, any outcome is likely to be as a result of compromise and not choice. There are a number of reasons why a claimant might opt for a lump sum over a PPO, on the basis that it best meets their expenditure needs, none of which should expose the claimant to any additional risk.

80. Our members have described what these include:

- **Short life expectancy**
  - o "My clients have a fatal condition and therefore prognosis is short."
  - o "Child aged ten with a short life expectancy (to age 19). Claim involved a 'percentage settlement' [contributory negligence] and there was a need for

[23] *The Discount Rate: What Next?* By Edward Tomlinson, 2017 J.P.I.L., Issue 2.

adapted accommodation. A PPO would reduce the amount of the lump sum to a level which would not allow for the purchase and adaptation of property, which was the parents' priority for their child. Therefore a lump sum was the most practical solution."

- **Uncertain life expectancy**
  - "Can be best for claimants with wildly fluctuating needs or an uncertain future."

- **Where contributory negligence which reduces the value of the claim or 'mid-value claims', both making a PPO unviable:**
  - "Usually best in cases worth less than £500K on a capitalised basis."
  - "Cases in which there will be a substantial reduction for contributory negligence or liability risks," where "the PPO would prove insufficient to cover the cost of care."
  - "A case where 2/3 contributory negligence – a pedestrian ran out into the road (a serious head injury for young man) – means that the claimant cannot fund a care regime with only a one-third recovery: the financial adviser says that lump sum is the only option."

- **Where there is capital expenditure such as for housing costs, which has to be met:**
  - "Cases in which a large sum is required in interim payments from the future award to fund housing capital costs"
  - "When you have a claimant with a short life expectancy and there are accommodation needs which have to be met, the client often has to agree to a lump sum as only way to obtain the [suitable/adapted] accommodation, particularly if insurer won't be inventive."

- **Where the cost of care needs in the future cannot be accurately quantified at present, leading to uncertainty as to the calculation of the PPO:**
  - "In a claim for delay in treating hip sepsis, causing the need for hip replacement surgery: the client was aged 16 and would need a full hip revision surgery every 15 years for rest of the client's life – eventually this would result in increasing disability and needs for care, equipment and adapted accommodation. The client's life expectancy was normal and the client preferred the flexibility that a lump sum gave her to plan now for her future care needs, rather than having to

wait for a time in the future when PPOs for care and therapy would become payable. She would be restricted in her options if, for example, those needs arose sooner than anticipated by the medical experts."

- **Where there is the risk of a split liability trial:**
    - o "Child injured with cerebral palsy as a result, allegedly, of medical negligence. However "child" was age 21 years at time of trial. He was in specialist local authority housing with a 24 hour live-in carer which his family were very happy with. Liability in the case was fiercely defended. It was therefore an "all or nothing" split liability trial. A lump sum settlement was offered by the defendant a couple of months before the trial. This was accepted and approved by Court upon Leading Counsel's advice."

- **Fatal dependency claims**
  - o "In a fatal case involving multiple dependants (spouse and minor children) as a matter of practicality the apportionment followed conventional lines with the majority of the lump sum award going to the wife, albeit that much of it would be used for the benefit of the household until the children attained majority. The children would attain majority between two and 14 years post-settlement. It was impractical to further apportion damages to take account of the contrasting dependencies involving (a) the parent and the children and (b) among the children."

Q15 and Q16

Q15 Do you consider that different rates should be set for different cases? Please give reasons. If so please indicate the categories that you think should be created.

Q16 Please also indicate in relation to the categories you have chosen whether there are any special factors that should be taken into account in setting the rate for that category.

81. We take the view that generally, there should not be different rates for different types of cases – the issue of definition would create problems and lead to lawyers attempting creative solutions to gain the best rate for their client. Proper use of the Ogden tables allows the court to precisely calculate the appropriate damages. But,

there is one exception to this, and it relates to a head of damage (rather than a type of case) which is easily defined: property costs.

82. There remain problems, regardless of the level of discount rate, where a disabled claimant needs specially adapted or designed property (usually a bungalow converted/built to specification): here the collision between the discount rate and the *Roberts v Johnstone* [1989] QB 878 calculation (to ascertain the sums required to secure adequate accommodation) creates particular problems.

83. It is generally recognised that the *Roberts v Johnstone* calculation no longer works, particularly when a claimant has a short life expectancy. It is APIL's view that *Roberts v Johnstone* is wrongly decided and should be overturned. It causes great difficulty in cases where the claimant's life expectancy is greatly reduced and/or there is difficulty in quantifying the claimant's life expectancy.

84. In these cases, the *Roberts v Johnstone* calculation only produces a small proportion of the capital required to secure appropriate accommodation and the claimant is forced to 'eat into' the funds allocated for the costs of future care future lost earnings, cuture costs of equipment, transport needs, costs associated with the court of protection and case management, when that duration of that future is limited and/or uncertain.

85. It is our view that the *Roberts v Johnstone* calculation should not apply at all. The claimant should simply be awarded the appropriate extra capital cost without any *Roberts v Johnstone* calculation or provision for recovery. The chances of this providing a windfall for the claimant or the claimant's family are in reality, remote. Awarding the extra capital cost would allow a seriously injured claimant to obtain the best quality of life the tortfeasor's money can provide, and should be a recognisable consequence of negligence.

86. APIL appreciates that this stance, while preferable and the best option for claimants, is unlikely to be considered as a realistic alternative to *Roberts v Johnstone*. APIL believes that if this position is not adopted, it should be enshrined in law that where compensation for accommodation must be calculated, parties and the judiciary must have regard to a range of alternative options, and consider which one is the best in the circumstances. This range of options includes renting property, an interest free loan from the defendant secured by a charge, or periodical payments to pay an interest only mortgage. See also our answer to Q.31 below for more on this.

87. We have produced a worked example of the effects of the discount rate upon this particular head of damage.[24]

Q17, Q18 and Q19

Q17 Should the court retain a power to apply a different rate from the specified rate if persuaded by one of the parties that it would be more appropriate to do so? Please give reasons.

Q18 If the court should have power to apply a different rate, what principles should apply to its exercise?

Q19 Do you consider that there are any specific points of methodology that should be mandatory? Please give details and reasons for your choice.

88. In our view the court should retain its power to apply a different rate from the specified rate where it is appropriate to do so within the current constraints set out in the Damages Act 1996, section 1(2).

89. *Warriner v Warriner*[25] confirms that it is rare for the courts to use this power, but it is right that it should be retained but not extended, to promote certainty for claimants and defendants as well as to avoid constant litigation on the issue, and thereby delaying settlement of claims and increasing litigation costs.

Q20 Do you agree that the law should be changed so that the discount rate has to be reviewed on occasions specified in legislation rather than leaving the timing of the review to the rate setter? If not, please give reasons.

90. We agree that the law should be changed so that the discount rate has to be reviewed on occasions specified in legislation.

91. It is an unfortunate truth that had the Lord Chancellor, in 2011, exercised his power to review the discount rate in a timely manner, the ‘shock’ which the insurers now claim to be suffering would have been greatly lessened: sixteen years is too long to leave the rate unchanged when it is supposed to deal with the rates of return available to

[24] See appendix page 7

[25] [2002] EWCA Civ 81

claimants: rates which now inevitably bear little relation to the financial conditions which existed when the rate was set in 2001.

Q21 Should those occasions be fixed or minimum periods of time? If so, should the fixed or minimum periods be one, three, five, ten or other (please specify) year periods? Please give reasons.

92. This question cannot really be answered until the method of calculating the discount rate is known. The Ministry of Justice is advised to decide on the methodology of calculating the rate and then consult again on review frequency.

93. A feature of the type of claims affected by the discount rate is that they can take years to finalise: the Institute and Faculty of Actuaries GIRO report 2017 indicates that the average delay to settlement of a PPO (from accident date) has remained broadly consistent in the 2010 through 2014 calendar years at between 6 and 6.5 years[26]. If the discount rate is reviewed too frequently, it becomes difficult to calculate losses as the claim progresses during that period of time.

94. If the rate is reviewed too infrequently, then we see the reaction from insurers (but not necessarily the market itself, of course) which claim that the change will adversely affect their business models, along with the consequent probability that seriously injured people will be either under, or over compensated, as the market moves out of kilter with the current rate.

95. Once the methodology for setting the rate is known, then it is possible to work out how long it should be between review dates. It may be that the frequency is expressed as 'not less than… x number of years' rather than fixing a firm time period so that the problems outlined in our answer to **Q25** below, do not become a regular feature of the rate review.

96. For example, if the rate is going to be set using option A above (very low risk investments, as per *Wells v Wells*) then a review every ten years might be appropriate.

97. But if the rate is going to be set using options B or C, then the claimant will be more exposed to the volatility of market movements and the rate is more likely to move out

[26] *Institute & Faculty of Actuaries Periodical Payment Orders Working Party Update GIRO 2015 Report*, 24 August 2016.

of kilter with the market. In which case, the rate may need to reviewed more frequently, but not so frequently that it affects the good administration of justice as cases stall, waiting for the next review, or are all listed for trial if the expected rate review is likely to be less favourable for some types of claimants, for example.

98. In the Lord Chancellor's reasons, dated 27 July 2001, Lord Irvine of Lairg said that, "whilst I will remain ready to review the discount rate whenever I find there is a *significant and established* change in the relevant real rates of return to be expected, I do not propose to tinker with the rate frequently to take account of every transient shift in market conditions" (our emphasis).

99. On 27 February 2017, sixteen years after that review, after completing two consultations, a research project and appointing an expert panel to offer advice, the Lord Chancellor confirmed to the London Stock Exchange that market conditions had shifted sufficiently to justify a change in the discount rate.[27]

100. In our view, 16 years was too long to wait for a review because the discount rate no longer reflected the true rates of return available in the market, and had not done so for many years. But less than five years between reviews is likely to be too frequent, as it will lead to uncertainty in calculating high value claims, stalling tactics by either set of parties as the next review looms all too frequently and will affect the administration of justice in the courts as outlined above.

101. The Ministry of Justice is advised to decide on the methodology of calculating the rate and then consult again on review frequency.

Q22 When in the year do you think the review should take effect? Please give reasons.

102. The review should commence in the second quarter of the year so that the announcement to set the rate can be made to coincide with the publication of the Annual Survey of Hours and Earnings (ASHE) figures (which are used to calculate future nursing care costs[28]) in the final quarter of the year[29].

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[27] Statement from the Lord Chancellor and Secretary of State for Justice to the London Stock Exchange, 27 February 2017, RNS number 8872X.

[28] *Thameside & Glossop v Thompstone* [2008] 1 WLR 2207 confirmed that ASHE (6115) was the correct measure for the indexation of future care costs,

Q23 Do you agree that the rate should be reviewed at intervals determined by the movement of relevant investment returns? If so, should this be in addition to timed intervals or instead of them? What do you think the degree of deviation should trigger the review?

103. No, we do not agree with this suggestion that the rate should be reviewed at intervals determined by the movement of relevant investment returns. The claimant is not an ordinary investor – he or she is a distressed purchaser of investments in order to safeguard future care and other expenses: he or she cannot go out to work to pay for those costs – the invested damages award must be protected – not used to play the stock market.

104. Yields can be volatile over short periods of time. The claimant is not an "ordinary investor" in the sense of being able to wait for long-term returns to materialise, or to ride-out volatility in asset prices. The Lord Chancellor in his 2001 statement (see paragraph 98 above) referred to 'significant *and* established' changes, not volatile trigger events.

105. In APIL's evidence submitted in its Judicial Review of the Lord Chancellor's failure to review the discount rate[30] APIL provided a copy of a report prepared for the Court by Rowland Hogg, dated 20 October 2010 in which he had submitted evidence of ILGS gross redemption yields averages between May 2001 and September 2010 (Fig 1 overleaf).

106. Compare this with the volatility of the FTSE 100 *over the same period* (Fig 2 overleaf). There is an obvious dramatic fall in the stock market in 2003 and immediately after the 2008 financial crisis, with smaller spikes and troughs throughout the period. A rate triggered by and set at review intervals determined by the movement of relevant investment returns would be distorted by the volatility of the market, either at one of its peaks or troughs and it is clear that they ought not to be events which trigger a review for that reason. See also our answer to Q24 below.

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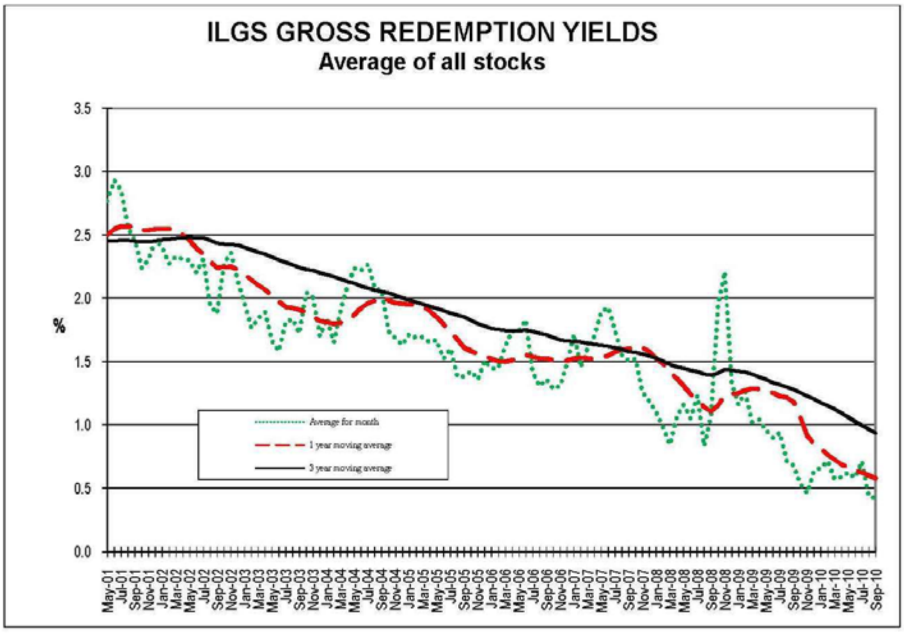
[29] See https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/bulletins/annualsurveyofhoursandearnings/previousReleases for publication dates in the recent past.

[30] *R on the application of The Association of Personal Injury Lawyers v The Lord Chancellor*, issued 1 December 2016, but not served.

Fig. 1. ILGS Gross redemption yields – 2001 - 2010



Month end yields - simple average of all stocks

	May 2001	September 2010
	%	%
Average for month	2.77	0.42
One year averages	2.50	0.58
Three year averages	2.46	0.94

Fig. 2. UK FTSE 100 Stock Market Index 2001 - 2010

Source: http://www.tradingeconomics.com/united-kingdom/stock-market

Q24 Do you agree that there should be a power to set new triggers for when the rate should be reviewed? If not, please give reasons.

107. No, in order to ensure there is certainty in the conduct of personal injury claims affected by the discount rate, we think that the review dates or periods should be left intact once they have been included in legislation and implemented.

108. We also think that allowing the option for additional triggers in the way suggested would allow those with an interest in having the rate reviewed up or down for short term gain to apply pressure to change the rate. Despite (and because) of APIL's own judicial review which it felt compelled to bring to force the Lord Chancellor to conduct the long overdue rate of the review, it is obvious to us that this is no way to conduct the law. As Sir Henry Brooke wrote in his blog, *The origins of the statutory discount rate for lump sum personal injury awards*, "This saga has been redolent of bad government."[31]

109. An orderly method, free from options for arbitrary triggers which can be pulled by any interested parties, at any time, must be implemented.

Q25 Do you consider that there should be transitional provisions when a new rate is commenced? If so, please specify what they should be and give reasons.

110. While we can see that some parties might argue that there should transitional provisions when a new rate is commenced, in practice, transitional provisions are likely to cause litigation headaches for all concerned.

111. It is inevitable that in any event, as soon as it is known that a discount rate review is imminent, that settlement meetings will be postponed, cases will be taken out of court trial lists or more applications for trial will be made (depending on which way the review is likely to take the discount rate) in anticipation of the new rate. We know this from parties' behaviour immediately preceding this most recent review.

112. Introducing transitional provisions will, in our view, simply prolong this behaviour in circumstances where the date of the next review is known in advance. In the weeks or months immediately preceding the known announcement date, and the avoid the

[31] 2nd March 2017 https://sirhenrybrooke.me/2017/03/02/the-origins-of-the-statutory-discount-rate-for-lump-sum-personal-injury-awards/

effects of the transitional provisions which proceed it, financial advisors and solicitors will advise claimants to withdraw part 36 offers to settle and to make applications to take cases out of the courts lists for trial, even earlier than they would in advance of a known discount rate review date. Other financial advisors and solicitors will advise defendants to make Part 36 offers to settle now and make applications for trials to be expedited. The effect will be that settlement of claims will halt for up to six months in anticipation of the review, and the courts will be clogged with additional applications. The closer together the rate reviews are scheduled, the more problematic this would become.

Q26 Do you consider that the discount rate should be set by:

a) A panel of independent experts? If so, please indicate how the panel should be made up.

b) A panel of independent experts subject to agreement of another person? If so, on what terms and whom?

Would your answers to the questions above about a panel differ depending on the extent of the discretion given to the panel? If so, please give details

c) The Lord Chancellor and her counterparts in Scotland or another nominated person following advice from an independent expert panel? If so, on what terms?

d) The Lord Chancellor and her counterparts in Scotland as at present?

e) Someone else? If so, please give details.

113. Setting the discount rate should be depoliticised. There should be a panel of experts which sets the rate. The panel should be independent of government and should be empowered to review the rate and then implement the revised rate. It should not, as was the case with the most recent review, simply advise the Lord Chancellor or other Minister of State and leave it to the Lord Chancellor’s discretion as to whether to amend the rate and if so, by how much.

114. A template for its composition could be the Judicial College or the Civil Justice Council. Overseen by a judge with relevant experience, meeting identified criteria, appointed by

the Master of the Rolls. It should include an IFA, an academic financial expert, an actuary, specialist claimant and defendant solicitors or barristers.

115. In our view, the expert panel for Scotland and Northern Ireland should be set up in the same way as, and match the composition of, the expert panel for England and Wales.

Q.27, Q.28, Q.29, Q.30

Q27 Do you consider that the current law relating to PPOs is satisfactory and does not require change? Please give reasons.

Q28 Do you consider that the current law relating to PPOs requires clarification as to when the court should award a PPO? If so, what clarification do you consider necessary and how would you promulgate it?

Q29 Do you consider that the current law relating to PPOs should be changed by creating a presumption that if a secure PPO is available it should be awarded by the court? If so, how should the presumption be applied and on what grounds could it be rebutted?

Q30 Do you consider that the current law relating to PPOs should be changed by requiring the court to order a PPO if a secure PPO is available? If so, what conditions should apply?

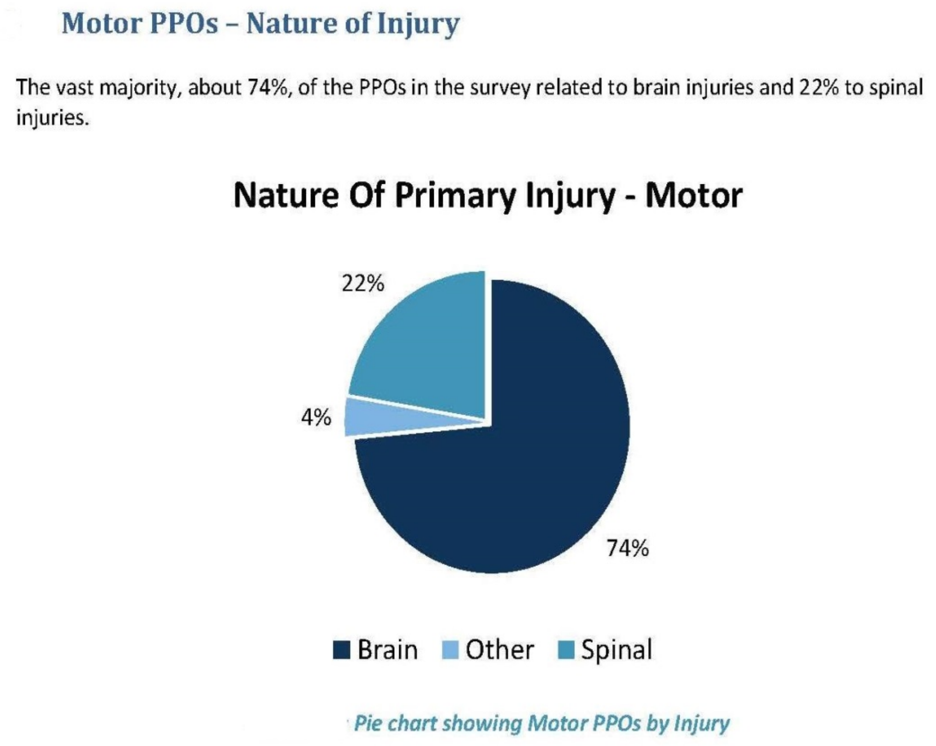
England and Wales

116. The current law relating to PPOs should not be changed by the creation of a presumption that if a secure PPO is available it should be awarded by the court. The claimant should not be forced to accept a PPO against his or her wishes and/or regardless of the claimant's professional financial advice. We know that the drivers towards acceptance of PPOs by both claimants and defendant insurers are working: now that the discount rate has been reduced they are more attractive to both parties. There is no need to further *legislate* to enforce their provision in this way.

117. There are, however, a few *non-legislative* changes which would further promote the use of PPOs where they are most appropriate.

- A Practice Direction, rather than legislation, which stated that defendants and courts should have to consider PPOs should be considered. At present, if the claimant is keen to have a PPO, but the defendant or its insurer will not make one available, the claimant has no option but to go to trial and hope the court will order an PPO. In reality, as our members have already commented above (para 25) claimants prefer not to risk going to trial and defendants encourage this stance by offering enhanced lump sums as an alternative in many cases. As we have also said (see para 24) and which is confirmed by the IFoA PPO Working Party, GIRO 2015 Report pie chart below, claimants without capacity (children, brain injured claimants) are more likely to be in receipt of PPOs because their settlements require court approval.

Fig 3. Relationship of PPO to type of injury



Source: IFoA PPO Working Party, GIRO 2015 Report. Some claimants suffered multiple injuries. This chart represents only the primary injury.

- A set of standard directions for claims valued at £1m or more which required parties to consider the provision of PPOs and provide information at the case management conference. We know that at present, judges are reluctant to deal with the costs of doing this at the costs budgeting stage.

- It should be possible to vary the PPO for reasons other than significant deterioration or improvement in the claimant's condition. For example if and when a gratuitous care provider is no longer able to provide care; if the claimant regains or loses capacity; or where local authority funding stops.

- The average lump sum amount across all PPOs, for both motor and liability policies, is £1.6 million and the average periodic payment is £77,000. For motor PPOs the equivalent figures are £1.7 million and £78,000 respectively.[32] PPOs are problematic in those cases where *Roberts v Johnstone* comes into play, since it is not possible to claim, as part of the PPO, for the cost of the mortgage to purchase an adapted property. For this reason, a lump sum is necessary to purchase the property outright and/or complete property adaptations. This is a market for a new, government backed PPO product: there is an opportunity for the Government to step in and offer a financial product to these types of claimant so that they can purchase a suitable property without the need for a large lump sum award, allowing the PPO to include repayments for a mortgaged purchase instead.

- The key factors would be:
    - PPO linked to indexation against LIBOR;
    - For a percentage of the capital requirement (ie not 100% of the purchase price);
    - Interest only, to avoid capital windfall;
    - Term to be for the claimant’s life plus one year to allow the estate to be dealt with.

118. We urge the government to explore this idea[33].

Scotland:

119. Court rules do not currently cater for PPOs and so they are only available if both parties put them forward. The rules should mirror those in England and Wales.

[32] IFoA PPO Working Party, GIRO 2015 Report

[33] Or at least investigate the very substantial market for investment damages in these cases which represents an opportunity for the Government to attract guaranteed high volumes of secure income.

Q31 Do you consider that the cost of providing PPOs could be reduced? If so, how.

120. This is a question best answered by the insurer respondents to this consultation.

Q32 Please provide details of any costs and benefits that you anticipate would arise as a result of any of the approaches described above.

121. See our answers to Q.27 – Q.30 above.

Q33 Please provide any evidence you may have as to the use or expected use of PPOs in the light of the change in the rate and more generally.

122. See our answers to Q.27 – Q.30 above and in particular our suggestion that a new financial product would be beneficial and, we suggest, very popular with seriously injured claimants.

Impact Assessment

Q34 Do you agree with the impact assessment that accompanies this consultation paper? If not, please give reasons and evidence to support your conclusions.

123. We do not agree with the impact assessment: it is clear that removing the risk-free assumption as the basis for full compensation will have a detrimental effect on those with protected characteristics: those who benefit from awards which are affected by the discount rate are by their very nature disabled, young, old and infirm. Children and mothers injured as a result of birth negligence are injured by reason of pregnancy and maternity: they are also protected characteristics.[34]

Equalities Statement

Q35 Do you think we have correctly identified the range and extent of effects of these proposals on those with protected characteristics under the Equality Act 2010?

124. See our answer to Q.34 above.

[34] S.4 Equality Act 2010.

Q36 If not, are you aware of any evidence that we have not considered as part of our equality analysis? Please supply the evidence. What is the effect of this evidence on our proposals?

125. See our answer to Q.34 above.

Final comments

126. APIL was also sent a questionnaire from the Ministry of Justice's Access to Justice Analytical Services team. The questionnaire was aimed principally at financial experts and required substantial research to obtain detailed evidence which, in the short timescale provided (14 working days), was not possible for APIL to collect.

Appendix

Page number

Ogden: A Very Human Cost.

02/03/17 14:46 / by Ian Hughes

The decision on Monday to change the Ogden rate to -0.75% comes with at least two very human costs.

Before we get in to this I want to make my personal position on this subject really clear so neither side of the debate can criticise. The cost of a personal injury claim is a cost that is borne by the person who caused the injury. The very positive benefit of having insurance is that it covers the individual so that they don't have to pay it from their own pockets. Insurance is, in essence, a hedge that individuals take against the cost of a claim, that insurers price within the legal framework in which they operate and personal injury lawyers do the same. The £3bn issue facing insurers this week has been caused by successive governments of different colours not realising the shifting sands of interest rates also required for the framework to change.

So what about those human costs?

The first is to anyone who has had their claim settled since the rate was set at 2.5% and, more specifically, anyone who has had their long-term claim settled since 2008 when interest rates crashed. If you believe Liz Truss' argument that the only legal level to put discount rate is -0.75% then, put simply, they have received a pay-out that is too low. They will suffer for the rest of their lives.

The second is to the thousands of people who work for insurance companies. The timing of this announcement is particularly cruel for those on profit related bonuses because, at the 59th minute of the 23rd hour of the financial year, profits have been slashed. For those on profit related bonuses that means their bonus has been slashed. Some people will have been relying on those bonuses. Some people will have worked very hard over an extended time to build to this. Some may even have been planning a change in their life or a holiday or an extension or to simply save for retirement. All gone.

Both sides of this debate are sore. Blame can be pointed in many directions, but the truth is that this is a systemic failure. Unlike the Oscars cock-up you can't point a finger and say *"that's the idiot the caused this".*

The only logical solution would seem to be to set the discount rate as a percentage different from a secure interest bearing commodity, be it government gilts or something else. While the price of that commodity may vary by the second the discount rate to the commodity remains fixed. It means that every pay-out for every claim will have a slightly different discount rate because it depends on the rate at the time of the accident.

This might seem maniac as a suggestion, it would require quite a lot of computing power and would also create a need for companies to be able to forecast commodity prices as part of their reserving strategy. It would also mean that when interest rates change then the price of car insurance would also have to change. But the good news is that interest rates are so low that increasing rates are likely to reduce reserving and, therefore, reduce price or increase profit (or both).

This plan might seem like a crazed plan from someone who isn't an actuary and who doesn't understand the nuances of insurer financing. I don't, I freely admit. What I do understand is what it must feel like for those who are injured through no fault of their own and those who have worked hard to have their bonus taken away through no fault of their own.

For the long-term health of the industry and for those we seek to protect we need to do something radically different. We can and we should.

Insurance discount rate debate: A fundamentally flawed decision that could cost the sector billions

James Dalton

James Dalton is director of general insurance policy at the Association of British Insurers [..]

Insurers are eagerly awaiting the decision of justice secretary Liz Truss' decision on discount rates (Source: Getty)

No one can dispute the right of someone seriously injured in an accident to receive compensation.

Where claimants choose to take a lump sum, arriving at the right figure is no easy task as it needs to take into account the long-term cost of care and loss of earnings, among other things. A key component is taking into account how much claimants may earn over time when their lump sum compensation is invested. This adjustment is called the discount rate and, since 2001, it has been set at 2.5 per cent.

In December, after the threat of being judicially reviewed by the Association of Personal Injury Lawyers, the Lord Chancellor, Liz Truss, suddenly announced plans to review the discount rate.

We took the Lord Chancellor to court and, despite the many shortcomings in the process to date, our attempt to prevent her announcing the outcomes of her review without concluding earlier consultations was rejected.

Unintended consequences

As we approach the point of her decision, let's be in no doubt: this decision by the Lord Chancellor risks being fundamentally flawed.

A significant downward change in the discount rate will have unintended knock-on effects across the board, so it is vital for every person in the UK to be aware of this; not just those paying motor insurance.

Thousands of people every year suffer the kind of tragic injuries that mean they will spend the rest of their life receiving medical treatment and care. No amount of financial compensation can make up for that but insurance is there to help people get their lives back on track. The real difference this makes to injured people is one of the things that makes me proud to work for the industry I do.

Take Ben, a 25-year-old sales executive from Lincolnshire who is disabled due to a road traffic accident and cannot work again. He has a degree qualification and it is determined he would have earned £30,000 a year until retirement at 65. Care for the rest of his life is determined to cost £80,000 per year.

Ben has two choices. One option is that he can ask his insurer to invest his damages via a Periodical Payment Order (PPO). Alternatively, he can take a lump sum and ask an independent financial adviser (IFA) to invest it, to produce a return. At the current discount rate of 2.5 per cent, Ben can expect total damages of around £3.2m. If the rate is slashed to minus one per cent, Ben's total lump sum damages suddenly almost treble to around £8.3m. But if Ben's IFA, through cautious investment, in fact receives a one per cent rate of return on that sum, Ben is effectively receiving £88,821 more per annum than he should.

Some might say Ben getting more compensation to compensate him for his injuries is a good thing but it is important to ask who will ultimately be footing the bill? Well, that would be you. And me. And the other 36 million motor policyholders in the UK. The greatest cost increases are likely to be borne by those "just about managing" and those who already pay the highest premiums because of the greater risk they represent, such as younger and much older drivers.

NHS

But it isn't just about motor insurance. Changes to the discount rate will slam other struggling public sector bodies like the NHS, as well as the Ministry of Defence with skyrocketing bills. With clinical negligence claims costing the NHS in England over £1.5bn last year, a change in the discount rate at a time when NHS budgets are already under extreme pressure will have a very serious impact.

All of a sudden, this threatens to become a multi-billion pound problem for everyone and will likely hit the pocket of every person in the UK.

Many businesses buy motor and liability insurance and this will drive up costs at a time of uncertainty in the economy. Some, like bus companies or road hauliers, will be particularly affected. This is not only due to the significant risk they present but because, given the smaller number of insurers selling this insurance, any changes in their appetite for business could have a greater impact on capacity in the market.

The ball is now firmly in the Lord Chancellor’s court. As an industry, we are committed to providing fair compensation to those who need it, but the system needs to work fairly for everyone.

We continue to call on the Ministry of Justice to set a fair rate; one that works for both the victims of life-changing injuries and those insurance premium payers who will ultimately be footing the bill.

City A.M.'s opinion pages are a place for thought-provoking views and debate. These views are not necessarily shared by City A.M.

Source: CityAM accessed 20-04-2017 http://www.cityam.com/259541/fundamentally-flawed-decision-could-mean-insurance-costs

***Roberts v Johnstone* calculation**

The assumption for a *Roberts v Johnstone* calculation is that if the claimant had not spent their money on accommodation, then it would have been invested risk-free.

In *Roberts v Johnstone* [1989] QB 878*,* the Court of Appeal decided that the proper basis for assessing the loss was to apply a rate which would represent a real rate of return on a risk-free investment - which is the discount rate - (and which at the time of *Johnstone* was set at two per cent).

The annual sum calculated using the discount rate is then converted into a capital figure using a multiplier based on the period of anticipated loss.

In this work example, we use the current discount rate of -0.75 per cent, assume that the accomodation costs are anticipated to be £250,000 and that the life expectancy multiplier has been set at 29.6 for a male claimant, aged 30 at the date of trial.

With a discount rate of -0.75%

Accommodation costs

(value of new property – value of current property if there is one)	£250,000
£250,000 x -0.75% x life expectancy multiplier of 29.6	-£55,500
Plus adaptation costs	£150,000
Plus moving costs = £20,000	
Total	£114,500

This leaves the claimant with a shortfall of £135,500, a sum which has to be found by taking funds allocated to other heads of damages, such as future loss of earnings, or part of the costs of care in order to enable the claimant to purchase the adapted accommodation he needs.

The Discount Rate: What Next?

Edward Tomlinson*

keywords to be inserted by the indexer

QUANTUM/ DAMAGES

At 07.00 on the 27 February 2017, an otherwise unremarkable Monday morning, the Lord Chancellor, using her powers as set out in s.1(1) of the Damages Act 1996, changed the discount rate from 2.5 per cent to minus 0.75 per cent. The impact of this change is enormous. Overnight the world of personal injury litigation had changed significantly.

Huw Evans, director general of the Association of British Insurers (ABI), described the change as a "crazy decision" and "a massive own goal [for the Government] that lands the NHS with a likely £1bn hike in compensation when it needs it the least".[1]

In a press release[2] the Association of Personal Injury Lawyers ("APIL") stated:

> "People who suffer severe life-changing injuries can now be assured that the compensation needed to look after them is calculated correctly and is sufficient to provide care for the rest of their lives. It is what they need and deserve and APIL welcomes this recognition from the Lord Chancellor."

Whilst the change in the discount rate was initially seen as good news for claimants and bad news for defendants, what quickly emerged was bad news for all.

> "The Government will review the framework under which I have set the rate today to ensure that it remains fit for purpose in the future. I will bring forward a consultation before Easter that will consider options for reform including: whether the rate should be set in the future by an independent body; whether more frequent reviews would improve predictability and certainty for all parties; and whether the methodology—which in effect assumes that claimants would invest only in index linked gilts—is appropriate for the future. Following the consultation, which will consider whether there is a better or fairer framework for claimants and defendants, the Government will bring forward any necessary legislation at an early stage."[3]

Whilst the promise of a new consultation gave hope to defendants that the discount rate might soon be on its way back up again, the on-going uncertainty and lack of any interim measures, such as a window of certainty to allow claims to settle, was unwelcome to claimants and defendants alike.

Impact of the change

For a 15-year-old female claimant with a normal life expectancy the life multiplier for calculating future losses increases from 33.91 to 104.62[4]; a three-fold increase. A perhaps more striking way of demonstrating the above change, is that for every £10,000pa of future annual losses the 15 year old female claims, the

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1 Julia Bradshaw, "UK insurers hit back at 'crazy' personal injury rate change as share prices tumble" (*The Telegraph*, 27 February 2017), *http://www.telegraph.co.uk/busioness/2017/02/27/uk-insurers-hit-back-crazy-personal-injury-rate-change-share/* [Accessed 7 April 2017].

2 Released 27 February 2017.

3 Ministry of Justice, *Change of personal injury discount rate* (27 February 2017), *www.londonstockexchange.com/exchange/news/market-news/market-news-detail/other/13139570.html* [Accessed 7 April 217].

4 Government's Actuary Department, *Actuarial tables for use in personal injury and fatal accident cases*, 7th edn (The Stationery Office, May 2007), Supplementary Tables.

capitalised lump sum of that loss is now valued at £1,046,200. With care packages for the catastrophically injured regularly assessed at well over £100,000 pa, it is clear that the stakes are high.

Statement of reasons

Like the previous Lord Chancellor, Liz Truss provided a statement of reasons to explain why she had set the discount rate the way she did. From this statement of reasons a number of matters were made clear.

First, this had been a lengthy[5] process that was very thorough:

> "2. In the course of my review, I have considered all the material available to me, including the responses to a Ministry of Justice public consultation in 2012, the report of an expert panel in 2015 (which reached majority and minority conclusions) and the responses of statutory consultees, HM Treasury and the Government Actuary. The process of review has been lengthy, and extraordinarily thorough."

Secondly, claimants should not be expected to take risk:

> "7. I have approached the setting of the discount rate on the basis that the governing principle is as identified by Lord Hope in that case[6]: '[The discount rate] is the rate of interest to be expected where the investment is without risk, there being no question about the availability of the money when the investor requires repayment of the capital and there being no question of loss due to inflation'."

Thirdly, a *no risk* discount rate should be based on the return of index linked gilts ("ILGs"):

> "8. The principles in *Wells v Wells* lead me to base the discount rate on the investment portfolio that offers the least risk to investors in protecting an award of damages against inflation and against market risk. I take the view that a portfolio that contains 100% index-linked gilts ("ILGs") best meets this criterion at the current time."

Fourthly, a *risk* discount rate is not compatible with the principles in *Wells v Wells*:

> "9. … In particular, the case has been made by a number of respondents to the consultation exercises that it might be more appropriate and realistic to use a 'mixed portfolio' approach (in which other securities feature). I acknowledge that those arguments have some merit. However, I am not persuaded by them. I consider that a faithful application of the principles in *Wells v Wells* leads to the 100% ILGs approach as the best way, in the current markets, of ensuring that there is '*no question about the availability of the money when the investor requires repayment of the capital and there being no question of loss due to inflation*.' The mixed portfolio approach in contrast runs counter to these principles by requiring the assumption by the investor of a greater degree of risk."

Knowing that after a lengthy and thorough process, it was found that a claimant should not be expected to take risk and that a no-risk discount rate should be based on the return of ILGs, it is clear that the only way the discount rate will change following the next consultation, is if the principles in *Wells v Wells* are abandoned.

[5] Taking the start date as the response by the Treasury Solicitor to the Association of Personal Injury Lawyers ("APIL") in November 2010 stating that the a review of the discount rate would commence shortly, the time take for the review was six years and three months.

[6] *Wells v Wells* [1999] 1 A.C. 34 HL per Lord Hope of Craighead.

Where next

The clearest indication of where we may be heading came the next day following comments made by Andrew Tyrie MP, Chairman of the Treasury Committee:

> "Under the current legal framework, the Lord Chancellor appears to have had little choice but to reduce the discount rate from 2.5 per cent to minus 0.75 per cent. But the result will be sharp rises in people's insurance premiums, and a big hit to the public finances.
>
> The principle that people should receive full compensation for the losses that they have suffered is a reasonable one. But implementing it in this way is probably not, and has a look of absurdity about it.
>
> Other ways of calculating the discount rate need to be examined, including one that reflects the long-term equilibrium risk-free yield. This is all the more important, given that the gilt markets have been heavily distorted since the financial crash, not least by emergency action to assuage its consequences, including QE.
>
> The Government is now consulting on how the discount rate should be set for the future. This is not before time. If changes to primary legislation are appropriate, controversial though they may be, the Government should consider them."[7]

It is clear that in the new consultation all options will be on the table and this will include abandoning the principles in *Wells v Wells*, which will require primary legislation.

Claimants and risk

It is understood that the claimant is not the "ordinary investor" however it is perhaps less well understood that the majority of claimants would prefer not to take risk. In 2013 Ipsos Mori authored a report[8] *Personal Injury Discount Rate Research* which was published by the Ministry of Justice. Its key findings on investment and consumption behaviour were:

- Stakeholders indicated that claimants are generally cautious in their investment behaviour, and tend to cite their vulnerability as making them more risk averse.
- Responses indicated that claimants tended to take on a mixed portfolio of investments, rather than just relying on ILGS. Claimant investment decisions depended on their risk appetite (with most being uncomfortable with high or even moderate risk); the advice given by their financial advisors; and the level of pressure they felt to meet future needs, regardless of how comfortable they were with risk. Those less satisfied with their compensation tended to be less comfortable with risks, yet sometimes felt under greater pressure to take higher-risk investments than they wanted to.
- Many were unhappy with the rates of return they were achieving on their investments, which increased their concerns about managing their lump sum in the future. This was considered particularly relevant given the decline in recent years in yields on ILGS, on which the current discount rate is based, as the rate assumes a higher rate of return than claimants felt they would be able to achieve in the current economic climate.
- Claimants' initial spending priorities included housing and home adaptations. Claimants felt that their consumption behaviour would have remained largely the same if they had received a larger settlement. However, several felt that with a larger settlement they may

[7] Andrew Tyrie MP, "Chair reduction to discount rate on personal injury lump sum" (UK Parliament, 28 February 2017), *http://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/news-parliament-2015/discount-rate-personal-injury-claim-chairs-statement-16-17/* [Accessed 7 April 2017].

[8] Ipsos MORI Social Research Institute, *Personal Injury Discount Rate Research* (10 September 2013).

> have had more confidence to spend on their immediate needs, such as housing and care. In addition, they felt that they might select less risky investments.

My personal experience of working in this field is that for those with the highest needs, a lump sum settlement can be a burden. It does not make them feel rich; rather it is a constant source of worry that must be managed to ensure that it will be able to meet their needs for the remainder of their lives.

A risk discount rate

If society wants to depart from a no risk discount rate then it is essential that the low risk tolerance of a claimant is reflected. The risk assumptions must be modest and must be achievable by the vast majority of claimants and therefore provides a fair result which does not offend (or least offends) the full compensation principle.

If we expect a claimant to assume some element of risk when they invest their funds, then any calculation to set a risk discount rate must recognise the cost of investing. In addition to inflation, both the charges and the taxation that will apply to the return generated need to be allowed for in the methodology to calculate the discount rate. These figures will not be insignificant and will reduce the discount rate.

Financial advisers in the UK must be authorised and regulated to provide advice by the Financial Conduct Authority ("FCA"). They must adhere to the FCA Code of Conduct and the rules and regulations in the various handbooks. One rule that must be adhered to is the Conduct of Business Sourcebook ("COBS"), Pt 13, Annex 2 Projections 1.1.

> "1.1 A standardised deterministic projection must:
> (1) include a projection of benefits at the lower, intermediate and higher rates of return;
> (2) Be rounded down; and
> (3) show no more than 3 significant figures."

In 2012 the FCA lowered the standardised deterministic projection rates of return to 1.5 per cent, 4.5 per cent and 7.5 per cent.[9] These figures are ultimately a best guess as to what rates of return may be in the future. The figures are taken from an 85 page report[10] from PricewaterhouseCoopers that was commissioned by the Financial Services Authority (FSA who became the FCA) and includes peer review. The figures are regularly reviewed by the FCA to ensure they are fit for purpose.

The standardised deterministic projection rates of return are net of tax but do not include inflation or charges. The current discount rate is net of tax, charges and inflation, and therefore, it is necessary to allow for charges and inflation.

Charges in the financial services industry vary widely between different advisers and different investment solutions. On a very substantial sum of money an overall charge of one per cent per annum would not be uncommon, and could be as high as two per cent per annum once all product charges are taken into account.

Assumptions for inflation are included in COBS 13 Annex 2 Projections and again they are expressed as a lower, intermediate and higher rate. The current rates are 0.5 per cent, 2.5 per cent and 4.5 per cent. In the below table, I have deducted charges and inflation from the rates of return to obtain a net rate. It is the net rate that could be used as a discount rate.

	Low	**Intermediate**	**High**
Projection rate	1.5%	4.5%	7.5%
Less Charges	1%	1%	1%

[9] COBS 13, Annex 2 Projections 2.2.
[10] PricewaterhouseCoopers, *Rates of Return for FSA prescribed projections* (Financial Services Authority, April 2012).

	Low	Intermediate	High
Less Inflation	0.5%	2.5%	4.5%
Net Rate	0%	1%	2%

Whilst this will be a decision for policymakers, knowing that an average claimant is risk averse, then it would seem to me that even the intermediate rate may be too high and therefore a discount rate of between 0 per cent and one per cent would be appropriate.

A discount rate of 2.5 per cent

If we apply the above methodology in reverse to a discount rate of 2.5 per cent, we obtain the nominal required rate of return. Assuming inflation is between two per cent per annum to three per cent per annum (0.5 per cent either side of the intermediate rate), charges are between one per cent per annum to two per cent per annum and that income tax is paid between basic (20 per cent) and higher rates (40 per cent), then the required rate of return is between 6.9 per cent per annum and 12.5 per cent per annum. This is calculated as follows:

Discount rate	2.5%	Discount rate	2.5%
Add Inflation	2%	Add Inflation	3%
Add Charges	1%	Add Charges	2%
Total	5.5%	Total	7.5%
Allow for Tax	20%	Allow for Tax	40%
Required Rate of Return	*6.9%*	*Required Rate of Return*	*12.5%*

To produce a consistent return of 6.9 per cent or more cannot be considered low risk. The FCA consider that 7.5 per cent is high risk. A move to a risk rate would increase the discount rate from minus 0.75 per cent, however it should not increase it back to 2.5 per cent.

Periodical payments

Now that the discount rate has moved to a true risk free rate of minus 0.75 per cent, there is parity between the value of a periodical payment and a lump sum settlement and therefore a claimant is afforded a true choice between the settlement options. Whilst the lump sum will provide flexibility and the potential to provide returns in excess of the discount rate and therefore more funds to the claimant which could meet unforeseen needs, a periodical payment continues to offer the valuable guarantees of transferring life expectancy risk, earnings inflation risk and are tax-free. I therefore believe that the risk averse claimant will still desire to have a proportion of their claim settled by way of a periodical payment.

Summary

The move to a risk-free discount rate will allow claimants with a full lump sum to meet their needs as claimed. If a political decision is made to abandon *Wells v Wells* and move to a risk discount rate then claimants will be required to take risk to meet their needs, those who choose not to take any risk with their settlement will not be able to meet their need. Any new risk discount rate should recognise the risk averse nature of the claimant who is not the ordinary investor and aim to ensure that as many claimants as possible are able to meet their needs.

adroit
Financial Planning

Report on Financial Matters in Respect of the Discount Rate Consultation

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Adroit Reference:	PR/JM/APIL
Date of Report	08 May 2017
Report directed to:	This Report is directed to Helen Blundell – Legal Services Manager of APIL in order to assist with their response the the Governments Consultation on matters in relation to the setting of the Discount Rate.

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INTRODUCTION

1. I, Paul Rosson, am an independent financial adviser and have been advising clients since 1990. I am a recognised expert in Pension Loss calculations, Periodical Payment Order analysis, Personal Injury Trusts and the investment and ongoing management of Damages Awards. I regularly advise on complex Trusts and Court of Protection matters.

2. I have prepared in excess of 500 reports in this field and have acted for both claimants and defendants. I regularly prepare CPR compliant reports in litigation matters and have given written and oral evidence in court within my area of expertise. I regularly train colleagues on all aspects of Pension Loss and PPO's work closely with our team of experts at Adroit. Details of my expertise and experience are provided at Appendix 1.

3. I have been instructed by Helen Blundell of the Association of Personal Injury Lawyers (APIL) to prepare this repose in order to assist with their response to the Governments Consultation on how the Discount Rate should be set in the future.

4. I have been specifically asked to comment upon the typical financial advice given to a Claimant who has received an award for personal injury damages under the previous discount rate of 2.5%, as well as the performance and returns that has been achieved. I have also been asked to consider how the advice would vary based on variables such as contributory negligence or liability compromises, and different life expectancies.

5. I can confirm that I act in this matter as an Independent Financial Adviser, and no conflict of interest will arise in providing my opinion

6. This report has been prepared with regards to the provisions of Part 35 of the Civil Procedural Rules and the attendant Practice Directions. The aims of the report are:

- Provide details of the factors to consider when providing advice to those in receipt of personal injury awards
- Detail the advice process that should be followed when providing financial advice
- Compare the performance achieved in the past from the advice provided taking into account the level of investment risk undertaken.

BACKGROUND & THEORY OF THE DISCOUNT RATE

7. The general principal for the settlement of damages, is *restitutio in integrum* – that the claimant shall be restored as far as possible in monetary terms, to the position that they would have been prior to the incident.

8. The Conventional approach to the award for damages is by way of a lump sum settlement for all heads of damage. The level of damages are quantified by considering the annual loss, and applying actuarially calculated multipliers as provided in the Ogden Tables, based on a given discount rate.

9. Section 1(1) of the Damages Act 1996 empowered the Lord Chancellor to prescribe a rate of return which the court will take into account 'in determining the return to be expected from the investment of a sum awarded as damages for future pecuniary loss in an action for personal injury' – i.e. the discount rate.

10. In addition to the statutory background, the House of Lords set out the principles to be used in setting the discount rate in Wells v Wells [1999]. In that case the House of Lords set the discount rate to be applied by the Courts at 3% largely by reference to a three year average rate of return on ILGS, as it was decided that claimants in personal injury cases were not in the same position as ordinary investors and could not leave the ability to pay for essential losses or which could be furthered by fluctuations in the investment market. In essence it was decided that an investor of monies from an award for damages should be considered to want to invest in the most risk free investment available. Therefore the rate of return on any investments would be limited by the limited appetite for risk. However in prescribing a discount rate, no consideration has to be given to what a claimant would actually do with the award for damages following settlement of the claim.

11. The discount rate was re-assessed in 2001 and was changed and set to 2.5%, based on the same methodology.

12. The Discount Rate remained at 2.5%, until a review commenced in November 2010. A consultation was first issued in 2012, with a response issued in August 2015. The current Lord Chancellor, Ms Elizabeth Truss MP, used these materials as the basis of the decision made in a more recent review.

13. As such, with effect from 20 March 2017, the Discount Rate was changed to -0.75% based on the same methodology i.e. by consideration of the 3 year gross redemption yields on index linked gilts, as a result of the assumption that investors of personal injury awards would look to invest in the most risk free asset available.

14. In her reasoning she referred to the statement laid before Parliament by Lord Irvine in 2001 which recommended that the approach to setting the discount rate should respect the following general principles:

   a. *There should be a single, fixed rate to cover all cases. This accords with the solution adopted by the House of Lords in Wells v Wells. It eliminates argument about the applicable rate at court and avoids the complexity and extra costs that a formula would entail.*

   b. *The rate should be one which is easy for all parties and their lawyers to apply in practice and which reflects the fact that the rate is bound to be applied in a range of different circumstances over a period of time. Given the uncertainties and imprecisions involved in the process of setting the discount rate, a rounded rate is preferable. Accordingly, I have decided to round to the nearest 0.25%. Ogden tables, applied by the courts to adjust awards according to a given discount rate, are currently published for rates at intervals of 0.5%. However, they can readily and swiftly be adapted to an intermediate rate.*

15. Since 2001, the discount rate has been and continues to be (prior to the outcome of this consultation) set as a single discount rate for all personal injury claimants based

on assumed investment into a single asset class which is deemed to be the "most risk free".

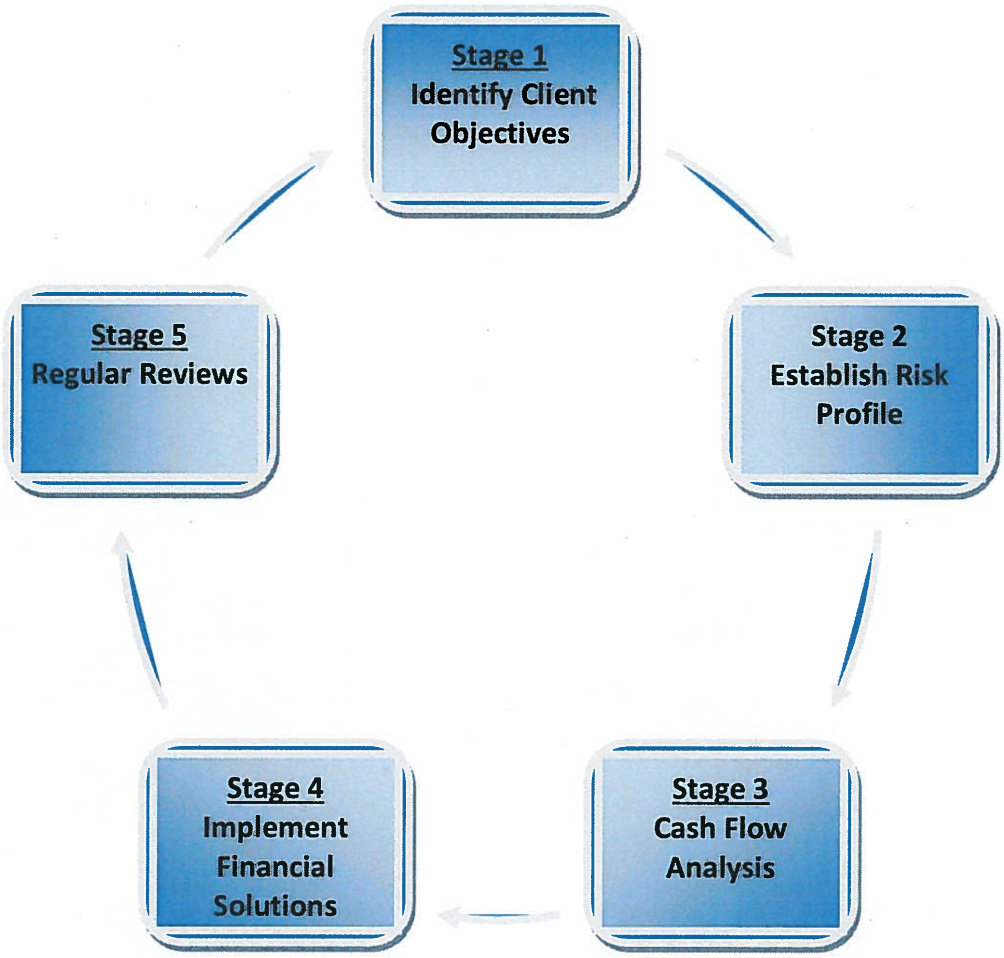
16. No reviews were undertaken until one commenced in November 2010, however no action was taken until 2017 – almost 7 years later.

17. During this time Gilt Yields have declined dramatically, which has meant that if Claimants were investing their monies into a basket of index linked gilts as the theory suggests, they would make a negative real return, and therefore be at risk of exhausting the funds during their lifetime, thus contradicting the 100% compensation principle.

18. The current discount rate of -0.75% now fairly reflects the returns available if Claimants were to invest in a basket of index linked gilts. However as a result of the change, the theory of investing in Index Linked Gilts has now been questioned.

FACTORS TO CONSIDER AND THE FINANCIAL ADVICE PROCESS

19. When providing financial advice, an adviser would follow the advice process, which can be summarised as:



Stage 1 – Identify the Client Objectives

20. It is important that an adviser understands the client's personal and financial circumstances in order to ensure that any advice given meets their specific needs. A financial adviser would therefore look to complete a fact find in order to ascertain details such as the current and anticipated income and expenditure including short term capital expenditure or large future capital expenses, any existing assets and liabilities, and their current tax position.

21. At this stage an adviser would also discuss the investor's future plans for the money in order to consider the time horizon of the investments, to ensure that the advice given is suitable for the client's needs.

22. As such, the investment advice provided to personal injury claimants is often done so following the settlement of their claim, so that the investment amount can be ascertained once all deductions, immediate capital expenditure and a suitable contingency sum (usually 3-5 years of annual expenditure) has been ascertained.

23. During settlement negotiations this is a difficult task as there is little certainty as to what the annual income and expenditure may be. However advisers can consider any shortfall that may occur between income and expenditure based on the Schedule of Loss, and how the settlement could be utilised to fund this.

24. A client's needs can be categorised into four key requirements:

- Income Requirement
- Capital Growth Requirement
- Income & Growth Requirement
- Capital Preservation Requirement

25. The needs can vary dependant on the circumstances of the claim, for example if the Claim involves a liability compromise of 25%, any award for damages is not going to be sufficient to cater for all of the expenditure as claimed for in the Claimant's Schedule of Loss. As such the Claimant automatically has a requirement for capital growth and potentially income too.

26. Essentially they are required to receive a rate of return in excess of inflation, investment charges and tax rates on any income/growth derived from the investments. The Claimants are therefore required to take more risk in order to attempt to achieve a higher annual return in order to ensure that their award can be sustained throughout their lifetime.

Stage 2 – Establish Risk Profile

27. Some of the possible risk factors that an individual may be exposed to when making any financial decision are as follows:

- Inflationary Risk – the risk of inflation increasing at a faster rate than interest/investment returns (net of tax), thus reducing the true value of the investments even if the capital sum is retained. This is a prevalent factor when no action is taken i.e. when funds are held in cash only.
- Capital Risk – the risk of capital losses as a result of a fall in investment markets
- Currency Risk – some investments may be denoted in foreign currencies and are therefore subject to fluctuations in exchange rates. This can work for or against the investor.
- Market Risk – the value of investments are based on supply and demand and determined by market forces or movements. An investor is therefore subjected to the risk of potential capital losses if there is a large swing in the market due to views on the economic outlook, influenced by political or economic factors.
- Liquidity risk – the possibility of not being able to access funds at the time they are required. This is common in investments into the property market.

28. When providing advice, risk forms an important part of the suitability of the recommendations made. In order to ensure that the advice given meets the client's needs and objectives, an adviser must consider:

- The need to take risk – Will the portfolio grow or provide the income that is sufficient to meet current and future needs?

- The ability to withstand risk – what would happen if the portfolio took too much risk and sustained a loss?

- The willingness to take risk – How does the investor feel about risk and how would they feel when the portfolio experiences losses?

29. Part of an investment adviser's role is to consider the required rate of return and the level of investment risk that clients need to take in order to meet their objectives.

30. Defining the relationship between risk and return is important because:

- Taking too much risk could result in higher volatility than is required to meet the needs in questions; and could result in capital losses

- Not taking enough risk could result in not achieving the required returns (or indeed the funds running out)

31. The two main areas that need to be considered are:

Risk Tolerance - An individual's attitude or response driven by their perception of uncertainty

Capacity for Loss – This is the extent to which an individual can afford potential loss before it adversely affects their lifestyle

32. In ascertaining the level of risk required the investor's thoughts and feelings towards taking risk with the monies, an adviser would most likely look to complete a risk questionnaire with the investor and undertake the following risk profiling process:

33. In my experience in providing advice to those who are investing for the benefit of an injured party, child or a protected party, their attitude to risk is often cautious as they understand a level of risk is required in order to keep pace with inflation, however they would be uncomfortable with any large capital losses in the value of the investments.

34. My experience is mainly based on Claimants investing money when the discount rate was at the previous 2.50%, therefore the Claimant's starting requirement in all situations was to attempt to achieve this as a net 'real return' (i.e. the return after inflation, taxes and charges). In more recent times with the Bank of England base rate falling to an all-time low, cash deposit accounts have been providing on average a return of only 1.00% Claimants were forced to take risk with the monies despite potentially having a completely risk averse attitude.

35. The role of the adviser was therefore to manage the level of risk to ensure that they were not over exposed, but at the same time could achieve the required return over the longer term to enable the funds to be sustained for as long as required.

36. The attitude to risk is therefore a critical discussion to have with any investor of personal injury damages as they need to understand why a certain level of risk is required to be taken, without over exposure which may result in capital losses.

37. Even with the current -0.75% discount rate a certain level of risk is still required. I have explained the reasons for this in further detail later in this report.

Stage 3 – Cash Flow Analysis

38. Once an adviser has assessed a client's personal and financial circumstances, needs, objectives, attitude to risk and capacity for loss, they will assess the recommendations made through the use of cash flow models to ensure that they are suitable for the Client. This method also ensures that the client is not taking too little or is over-exposed to risk, for their needs and objective.

Stage 4 – Implement Financial Solutions

39. At this stage an adviser would run through with the client the recommendations made specifically for the client based on their personal and financial circumstances giving regard to the economic environment and outlook at the time the recommendations are made. They would explain the reason for any recommendations and include the reasons why a certain level of risk may be required and the possible risks that they would be exposed to.

40. The adviser would then ask the clients to agree to the implementation. Once all of the relevant documentation is signed, the adviser would then make the necessary arrangements for the monies to be invested.

Stage 5 – Regular Reviews

41. As part of the on-going service a financial adviser will regularly review the client's financial position, needs and objectives as well as the investments made in order to ensure that the financial solutions are performing as expected and are still relevant to the investor's needs and objectives.

THE NEED FOR INVESTMENT RISK TO BE TAKEN

42. The discount rate is essentially the net 'real return' that is assumed to be achieved through investments of a personal injury award in index linked gilts as these are considered to be the most risk free investment available. This means that the rate is the return available once inflation, investment charges and taxation has been accounted for.

43. The two issues with this methodology were that a rate of 2.5% was unavailable via investments into index linked gilts, and secondly, a retail investor found it virtually impossible to invest into gilts on the primary market. This mean they had to invest in them on the secondary market, most likely at a premium, and therefore potentially suffer a capital loss when sold or redeemed.

44. In many cases, investments are made over the long term as the award for damages is required to be sustained for the Claimant's entire life time

45. In addition the expenditure which the award for damages is to be utilised towards is dissimilar from the expenditure of the general population and is therefore subject to differing levels of inflation, often in excess of a 'general basket of household goods'. As such the rates of the Consumer Prices Index (CPI) and to some extent the Retail Prices Index (RPI) is not the most relevant measure. This is supported by the decision in the well-publicised Appeal case of *Tameside and Glossop NHS Trust v Thompstone [2008] EWCA Civ 5* the Court, where it was held that ASHE 6115 was a more relevant index for care and case management costs.

46. From 2001 to 2017 the discount rate was 2.5%. Over a similar time period, the average percentage increase in the 80th percentile of ASHE 6115 was 2.88%, whilst the average percentage increase in RPI was 2.83%. If investment charges were 0.50% per annum, then a gross return (excluding taxation) would equate to 5.83%, which could be rounded up to 6% to account for any tax deductions applicable to achieve this level of return, or differing levels of inflation for different heads of damage. This is simply not achievable in a risk free manner.

47. Therefore when advising personal injury clients there is almost an automatic need to achieve a return of up to 6% even before any shortfall between income and expenditure is considered.

48. To put this into perspective I have attempted to "risk map" the required level of risk in order to achieve this return on an annual basis.

49. At Adroit we use 'Distribution Technology Dynamic Planner' which is a leading risk profiling tool, available to financial advisers. They provide data and expected investment returns based on past performance of a 'typical' asset mix which might be seen for the level of risk taken.

50. The Dynamic Planner risk scale ranges from 1 Lowest Risk to 10 Highest Risk. They provide factsheets for each risk profile, giving details of the example asset allocation that may be seen for each risk profile as well as the inflation adjusted likely returns and the likely volatility.

51. According to their data, to achieve a return of around 6% gross, investments in line with a level 6 – High Medium Risk Profile would need to be taken. The broad asset allocation of this risk profile shows that approximately 71% of the overall portfolio would be in equities, which are considered as a more risky asset class.

52. As detailed in the Factsheets provided at Appendix 2, a portfolio constructed as per the level 6 risk profile example asset allocation has experienced a maximum drawdown of 34.5% since June 2005.

53. With a discount rate of -0.75% the level of risk a claimant is required to take is significantly reduced although it is not completely eliminated. Based on the same assumptions as before, to achieve a rate of -0.75% per annum the claimant is required to seek a gross return of 2.58%. Current bank deposit rates are averaging 1.0% which means a claimant is still required to invest the money.

54. Again using Dynamic Planner the appropriate risk profile would be level 2 – very low risk which has a broad asset allocation of:

Cash	-	41%
Bonds	-	42%
Equity	-	12%
Alternatives	-	5%

55. By comparison, the maximum drawdown of a portfolio constructed in line with the asset allocation of a level 2 risk profile is 4.8% - quite clearly a much more manageable loss in comparison to a level 6 risk profile required to achieve the 2.5% discount rate as an annual real return.

56. This therefore shows that even with a low risk profile, to achieve the required or assumed real rate of return that the discount rate suggests, the Claimant is forced to take a certain level of risk.

57. As stated previously there is no such thing as a risk free investment, therefore in any situation no matter what the discount rate, a Claimant is having to take risk with their money and is therefore always at a chance of suffering or benefitting from over/under compensation.

ADVICE PROVIDED AND PERFORMANCE

58. In this section I have attempted to detail the thought process I have taken when providing financial advice to those in receipt of an award for damages, in line with the advice process as previously detailed.

59. Therefore the first point of call would be to discuss with the claimant and their representatives the income and expenditure relevant to their circumstances. This would entail discussion surrounding the expected expenditure over the short term and longer terms accounting for any capital expenses immediately or envisaged in the future.

60. As briefly described earlier, there are 4 main categories of needs and objectives. However in my experience Claimants, who have not experienced a liability compromise or split, i.e. have recovered 100% of the agreed level of damages, their objective is for capital preservation. Their required rate of return is therefore one which matches the applicable rate of inflation and charges over the required time horizon.

61. For Claimants who have encountered a liability compromise during litigation proceedings, their objective is often for capital growth as they realise that the funds are not sufficient enough to cater for all of their requirements.

62. The required time horizon is another factor that an adviser must consider. In most cases a schedule of loss contains losses which remain for life, although there may be losses which increase in later life. With a lump sum settlement based on a discount rate the capital sum needs to ensure that there are sufficient funds at a time when they are needed the most.

63. Conversely in cases where there is a very short life expectancy investment into certain asset classes or investment vehicles may not be suitable as they are more advantageous if held only over the longer term.

64. As explained previously, under the 2.5% discount rate Claimants were having to take a fairly significant level of investment risk in order to attempt to preserve their capital or achieve capital growth.

65. As an adviser it was my job to ensure the level of risk taken by the Claimants matched their needs.

66. The best way in which to achieve a risk adjusted return is through a well-diversified portfolio which gives exposure to a range of asset classes, industry sectors and geographical locations. It has therefore often been my advice that claimants should look to invest in a discretionary managed portfolio as it can offer greater diversity and is effectively managed to achieve the best outcome in all market conditions, which are ever-changing.

67. There are over 180 different Discretionary Fund Managers all of which would have a number of differing model portfolios or bespoke portfolios specific for a client's circumstances. Their investment strategies would differ dependent upon their beliefs.

68. In my experience some of the best strategies for personal injury claimants are volatility capping solutions, where fund managers look to reduce the downside risk but not necessarily chase a large upside gain. This allows investors to benefit from steady capital growth with little exposure to downside risks and therefore a smaller chance of capital losses which is ideal for those with an objective of capital preservation.

69. I have obtained research from a discretionary fund manager which provides details of their discrete annual returns since 2007, and the associated 3 year and 5 year volatility.

70. To provide an illustration of how the advice which may have been given to personal injury claimants has performed, I have detailed in the following table the performance of a 'typical' multi-asset portfolio along with the mapped risk profile in accordance with Dynamic Planner based on the 5 year volatility, as well as the inflation adjusted return.

Dynamic Planner Mapped Risk Profile *(Asset Allocation provided at Appendix 2)*	2	3	4
Expected Return of Risk Profile (inflation adjusted)	**0.01%**	**0.90%**	**1.90%**
Average Performance of Discretionary Managed Portfolio 2007 - 2016	3.86%*	4.69%	5.13%
Inflation (RPI)	*2.46%**	*2.74%*	*2.74%*
Inflation Adjusted Return	**1.40%**	**1.95%**	**2.39%**

**Please note that data for the lowest risk profile ran from 2008 to 2016 rather than 2007 to 2016 therefore inflation over the same time frame was used.*

71. The above table shows that with low risk investments Claimants have not been able to achieve the required real return of 2.50%, even though they outperformed the expected return as per Dynamic Planner's factsheets.

72. However in my experience most Claimants were unhappy or uncomfortable with having to take more risk than a level 4 risk profile as they were concerned with the possibility of large capital losses causing more hindrance to their financial futures.

73. This quite clearly demonstrates that for many years Claimants have been undercompensated.

74. With a discount rate of -0.75% Claimants are finally able to receive compensation which truly reflects their theoretical returns if invested in Index Linked Gilts, although in practice it remains that a Claimant cannot easily invest into this asset and moreover would not be advised to do so for two reasons:

i) It would be too risky to invest into a single asset class as it offers no diversification against negative returns

ii) it would not be prudent for an adviser to recommend an investment which at the moment would practically guarantee a negative return.

75. However the Claimant is still required to invest the money as cash deposits cannot offer a suitable inflation adjusted return which at least matches the discount rate.

76. Claimants are therefore still forced to take a level of investment risk albeit the amount of risk required is severely reduced.

77. My advice to clients under the -0.75% discount rate still remains the same as I still consider the most appropriate investment to be a well-diversified multi-asset portfolio.

78. In more recent times (last 12 months) the general investment markets have performed better than most expected, therefore as a result of exposure to equities within the diversified portfolios, the performance has exceeded expectations.

79. This however does not mean that Claimants are being over-compensated if choosing to invest the money away from index linked gilts as the theory suggests. This is simply as a result of beneficial positive performance from the most suitable investment available to a retail investor i.e. optimum risk adjusted returns.

80. In summary Claimants are forced to take risk, which will remain regardless of what the discount rate is. By choosing to invest in an option which is most suitable to their personal and financial circumstances based on financial advice provided is not a suggestion that they are choosing to risk the settlement award for a higher return, they are simply looking to optimise the return for the level of risk they are being forced to take.

CONCLUSION

81. The discount rate is currently still based upon the principles as per Wells v Wells in that an investor of an award for damages needs to be considered as wanting to invest in the most risk free asset available to them, which is considered to be a basket of index linked gilts.

82. This theory has been used since 2001 when the rate was set at 2.5%. No reviews occurred until 2010, and even then it was almost 7 years before the rate actually changed although a response to the consultation was published in 2015.

83. Over the same time frame the gross redemption yields on index linked gilts declined, and continued to do so through to negative rates.

84. For personal injury claimants this meant that the theoretical rate of return applied to their damages was overstated meaning they had to be exposed to a greater level of investment risk and look at different investment opportunities simply to be able to sustain the funds to their anticipated life expectancy, if not further. This quite clearly does not represent the principle of 100% compensation.

85. With a change in the discount rate to -0.75% Claimants are finally seeing a fairer reflection of the possible returns achieved through investment in index linked gilts as the theory suggests a claimant would.

86. This theory has now been scrutinised as a result as it would not be prudent for a Claimant to invest the money in an asset which provides a negative return. Although I agree with this statement, I do consider it intriguing that the methods have only been scrutinised now that they offer a fairer award for the Claimant at a larger cost to the Defendant.

87. As stated Claimants were forced to take risk in order to chase a return which could match the discount rate. To do so I have often advised that the best way in which to achieve a risk adjusted return is through a well-diversified multi asset portfolio, as have many of my peers.

88. As detailed in the main body of this report, based on a 2.5% discount rate the Claimants had to take a higher level of risk to attempt to achieve the returns required. In my experience many were uncomfortable with the level of risk required, therefore there was often an under provision of funds to invest. As an adviser I therefore had to consider how the income and expenditure could be adjusted at different stages throughout the Claimant's lifetime, and what State Benefits could be utilised. In essence the 2.5% discount rate did not represent the principle of 100% compensation.

89. With a -0.75% discount rate the Claimant's exposure to investment risk is severely reduced however is not completely eliminated. Claimants are still required to invest the money although they can now do so at a lower risk profile.

90. In recent times the performance of investment markets has exceeded the expectations of many economists. Therefore in recent times, the exposure to equities in a well-diversified multi asset portfolio has been beneficial for Claimants, although this should not be seen as a continuing trend.

91. However it must be borne in mind that the Claimant is practically forced to invest the monies an would therefore look to optimise their return for the level of risk taken. This does not mean they are being over compensated but are simply ensuring the funds can be sustained for as long as possible. In other words they are mitigating the risk of exhausting funds within their lifetime.

92. Within this report I have been asked to comment upon variables such as the inclusion of periodical payments within a settlement. Within the main body I have not referred to this as much simply because a settlement including periodical payments does not have a discount rate for the head of damage they are applied to. For example a PPO of £50,000 per annum for care and case management does not have a capitalised value at the point of settlement. It is simply an award of £50,000 per annum.

93. An award including periodical payments only affects the discount rate as a result of the capital sum attached.

94. In my opinion a capital sum would always be required as part of any settlement to ensure that the Claimant is provided with sufficient financial flexibility.

95. The financial advice provided to those who are in receipt of a PPO does not necessarily differ. Under a 2.5% discount rate they were still required to invest the capital sum to ensure it can be sustained, and the PPO was factored into income and expenditure to see if a shortfall still arose.

96. The advantages of a PPO do not disappear with a change in the discount rate therefore it is my opinion that they have very little bearing on what the discount rate should be and how it should be set.

EXPERT'S DECLARATION

97. I understand that my duty overrides any obligation to the parties who have engaged me. I confirm that I have complied with my duty.

98. My report has been prepared in accordance with the Code of Guidance on Expert Evidence and the requirements of the Civil Procedures Rules and I am aware of the requirements of Part 35, of this practice direction and the Guidance for the Instruction of Experts in Civil Claims.

99. I confirm that I have made clear which facts and matters referred to in this report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matters to which they refer.

100. I have endeavoured to include in my report those matters that I have knowledge of or of which I have been made aware, that might adversely affect the validity of my opinion.

101. I have not without forming an independent view included or excluded anything that has been suggested to me by others (in particular my instructing solicitors).

102. I will notify those instructing me immediately and confirm in writing if for any reason my existing report requires any correction or qualification.

103. I understand that:

a) My report, subject to any corrections before swearing as to its correctness, will form the evidence to be given under oath or affirmation;

b) I may be cross-examined on my report by a cross-examiner assisted by an expert;

c) I am likely to be the subject of public adverse criticism by the judge if the Court concludes that I have not taken reasonable care in trying to meet the standards set out above.

……………………………………

Paul Rosson Dip PFS Cert CII(MP)
Senior Financial Consultant
Adroit Financial Planning

Appendix 1

Profile: Paul Rosson Dip PFS Cert CII(MP)

Senior Financial Consultant
Adroit Financial Planning Limited

I am an independent financial adviser and have been advising clients since 1990. I am a recognised expert in Pension Loss calculations, Periodical Payment Order analysis, Personal Injury Trusts and the investment and ongoing management of Damages Awards. I regularly advise on complex Trusts and Court of Protection matters. I work exclusively in the field of Personal Injury, Clinical Negligence and Criminal Injuries Compensation.

I have prepared in excess of 500 reports in this field and have acted for both claimants and defendants. I regularly prepare CPR compliant reports in litigation matters and have given written and oral evidence in court within my area of expertise. I regularly train colleagues on all aspects of Pension Loss and PPO's work closely with our team of experts at Adroit.

My expert witness pension reports regularly cover Defined Benefit Schemes, Defined Contribution Schemes, Work Based Pension calculations, State Pension and Loss of Dependency.

I have regularly conducted seminars for law firms and barristers' chambers throughout the UK. I have also appeared as a guest speaker at Oxford University and for numerous independent conferences (such as APIL, AvMA and The Law Society) for legal practitioners, litigators and professional groups on the role of an independent financial adviser working alongside the legal profession. These talks focus on the areas of investment, pensions, personal injury work, tax planning and Trustee investment. I have regularly conducted accredited training for APIL, the SRA and the Bar Standards Board.

Prior to joining Adroit, I was a Senior Consult and Head of Litigation Support at Frenkel Topping, where I worked for 7 years. Prior to that I was Director of Financial Services for Cassons Chartered Accountants and Business Advisers, a position I held for 10 years.

Throughout my career I have advised hundreds of individuals and companies on Pensions, setting up schemes for individuals, from small Personal Pensions through to complex SIPP and SSAS arrangements for high net worth clients. He has also advised on and implemented company pensions schemes for many types of employer.

Professional Memberships:

•The Chartered Insurance Institute (CII)
•The Personal Finance Society (PFS)
•The Association of Personal Injury Lawyers (APIL)

Appendix 2

Dynamic Planner Factsheets

Dynamic Planner Quarterly Asset Allocation Factsheet Q4 2016
Risk Profile 2 - Very Low Risk

Expected return
0.01%
pa
(Inflation adjusted)

Expected volatility
3.56%
pa

Profile Description: An investor who is a Risk Profile 2 would be very concerned with the possibility of losing their investment as they have a 'very low' attitude to accepting risk. The level of return would not be expected to rise much more than if they had kept the money in a bank account or other low-risk investment, however this could reduce in value if inflation is high. Preferred investments for such an investor are lower-risk assets such as cash and bonds, with some medium-risk assets in the form of property.

Market Round Up - Q4 2016

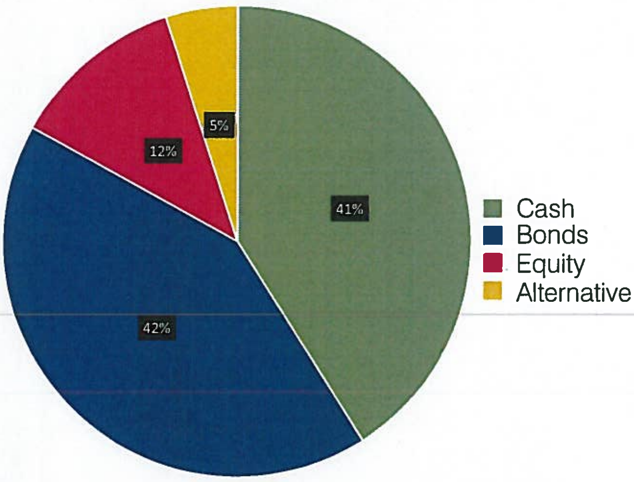
- Bonds - Political uncertainty in the US and Europe, the prospect of expansionary government spending plus another 0.25% rise in US interest rates all contributed to a broad sell-off for Government and (to a lesser extent) investment grade corporate bonds. However, High Yield Global Bonds made headway over the period, spurred by the search for yield and hopes of strengthening corporate balance sheets.

- Equities - Global markets, in general, enjoyed a strong quarter with the key theme being a rotation from defensive towards cyclical growth sectors of the market, referred to as the "reflation trade". Despite the political volatility, expectations for the global economy grew more optimistic, mainly in response to the election promises of Mr Trump. In the Eurozone, the extension of the ECB's quantitative easing programme provided continuing support, whilst UK equities also made progress, particularly financials (beneficiaries of steepening bond yields) and resources stocks. Japanese equities benefited from the further weakness of the yen. In contrast, emerging markets weakened due to continuing US dollar strength and worries over the potential direction of US trade and foreign policy.

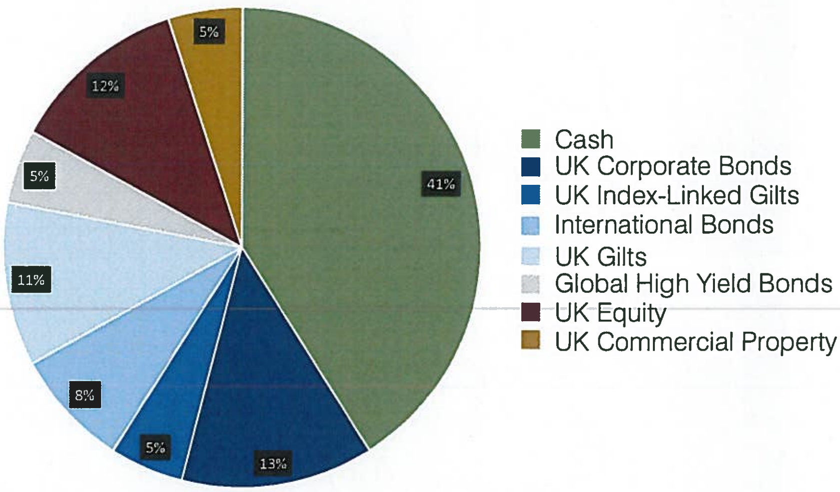
- Alternatives - Commodities performed well given the release of more supportive Chinese economic data and stronger oil prices after OPEC agreed to production cuts. UK commercial property showed a continued recovery in confidence from its post-Brexit woes.

Risk Profile 2: Asset Allocation Breakdown

Broad Asset Classes



Sub Asset Classes



Realised Cumulative Performance (Inflation Adjusted) to 31th December 2016

	1 Year	3 Year	5 Year	Since Inception (June 2005)
Annualised Return	7.2%	3.8%	2.1%	1.5%
Annualised Return (Nominal)	9.9%	5.6%	4.3%	4.5%
Annualised Volatility	4.2%	3.9%	3.4%	3.2%
Maximum Drawdown *[Period]*	*2.2% [Aug 16 - Nov 16]*	*3.3% [Jan 15 - Jun 15]*	*3.3% [Jan 15 - Jun 15]*	*4.8% [Oct 06 - Oct 08]*
Beta	0.3	0.2	0.2	0.1

For more information get in touch: 0333 6000 500 sales@dynamicplanner.com www.dynamicplanner.com

Key Terms

Expected Real Return:

The portfolio's inflation adjusted expected return is based on the current asset allocation and the expected gross returns per asset class.

Expected Volatility:

The portfolio's potential inflation adjusted volatility based on the current asset allocation and the risk and correlation per asset class. This is known as ex-ante volatility.

Realised Volatility:

The dispersion of the portfolio's experienced inflation adjusted returns as measured by standard deviation. This is known as ex-post volatility.

Maximum Drawdown:

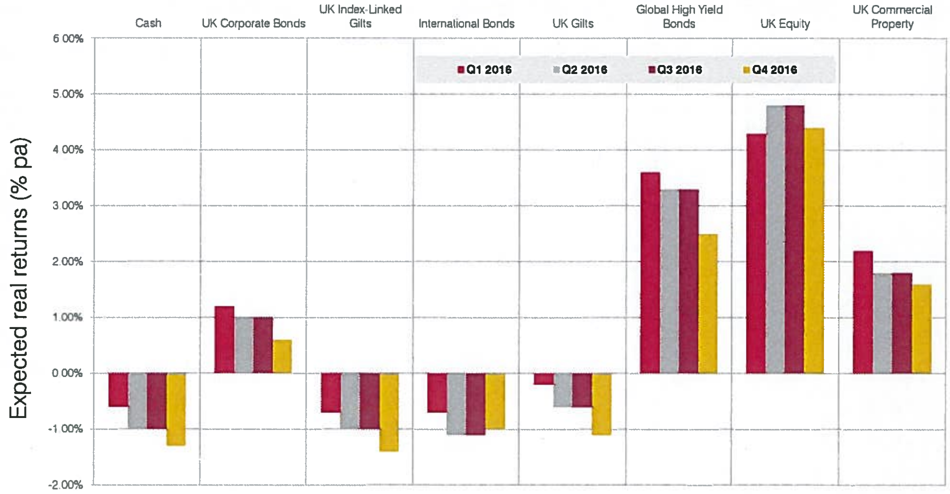
The largest continuous decline in the value of a portfolio for the given period.

Beta:

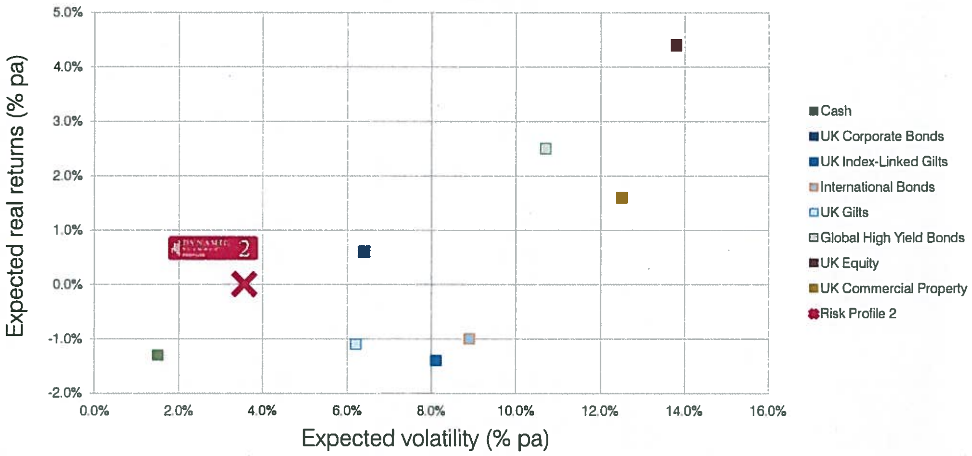
A relative measure of portfolio 'risk' that compares the realised volatility of the portfolio to a common UK equity index.

DYNAMIC PLANNER®

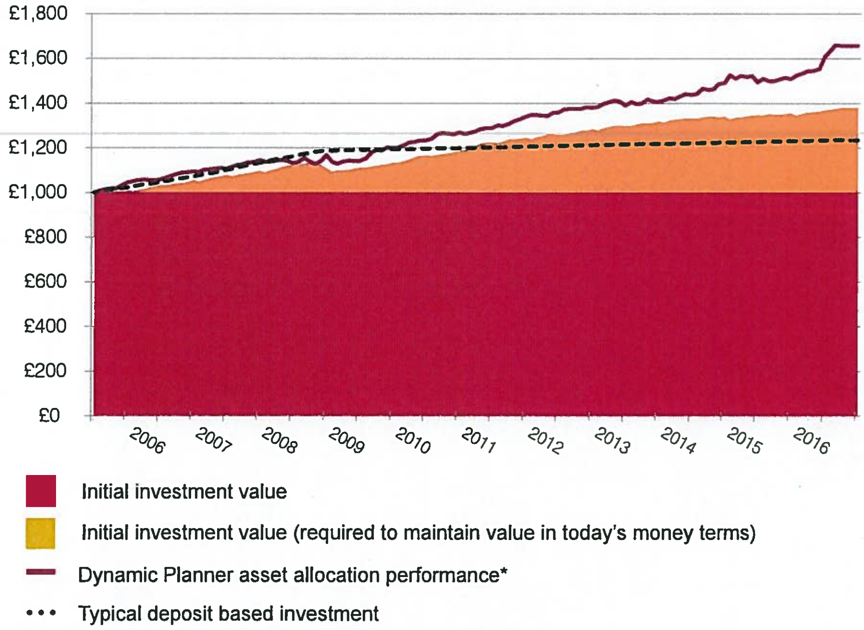
Asset Classes - Quarterly Changes in Expected Returns



Expectations of Asset Classes Used in Dynamic Planner Risk Profile 2



Performance of Dynamic Planner Asset Allocation 2 Since Launch - for £1000 Investment



* Adjusted for typical ongoing investment related fees (OCF's)

Important Information:
All asset allocations, assumptions, forecasts and past performance is calculated based on data live in Dynamic Planner as at the calendar quarter end date.

Dynamic Planner Quarterly Asset Allocation Factsheet Q4 2016
Risk Profile 3 - Low Risk

Expected return
0.9%
pa
(Inflation adjusted)

Expected volatility
5.5%
pa

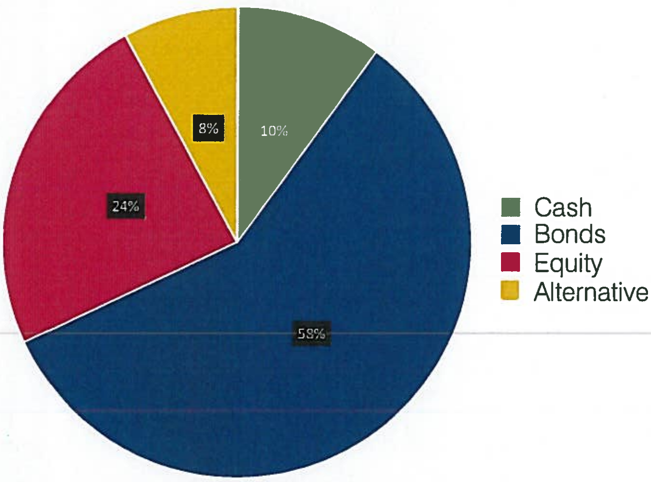
Profile Description: An investor who is a Risk Profile 3 is likely to be concerned about the possibility of losing money on their investments, but does not want to completely ignore the possibility of making higher returns than are offered by bank accounts and low-risk investments. As a result, these investors are willing to sustain very small losses on the amount invested by investing in lower- and medium-risk investments such as cash, bonds and property in order to achieve a higher return.

Market Round Up - Q4 2016

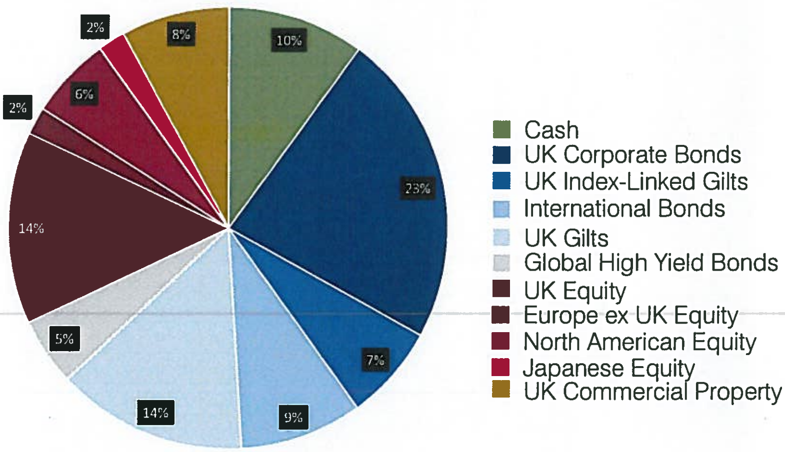
- Bonds - Political uncertainty in the US and Europe, the prospect of expansionary government spending plus another 0.25% rise in US interest rates all contributed to a broad sell-off for Government and (to a lesser extent) investment grade corporate bonds. However, High Yield Global Bonds made headway over the period, spurred by the search for yield and hopes of strengthening corporate balance sheets.
- Equities - Global markets, in general, enjoyed a strong quarter with the key theme being a rotation from defensive towards cyclical growth sectors of the market, referred to as the "reflation trade". Despite the political volatility, expectations for the global economy grew more optimistic, mainly in response to the election promises of Mr Trump. In the Eurozone, the extension of the ECB's quantitative easing programme provided continuing support, whilst UK equities also made progress, particularly financials (beneficiaries of steepening bond yields) and resources stocks. Japanese equities benefited from the further weakness of the yen. In contrast, emerging markets weakened due to continuing US dollar strength and worries over the potential direction of US trade and foreign policy.
- Alternatives - Commodities performed well given the release of more supportive Chinese economic data and stronger oil prices after OPEC agreed to production cuts. UK commercial property showed a continued recovery in confidence from its post-Brexit woes.

Risk Profile 3: Asset Allocation Breakdown

Broad Asset Classes



Sub Asset Classes



Realised Cumulative Performance (Inflation Adjusted) to 31st December 2016

	1 Year	3 Year	5 Year	Since Inception (June 2005)
Annualised Return	12.9%	7.3%	5.5%	3.5%
Annualised Return (Nominal)	15.7%	9.2%	7.8%	6.5%
Annualised Volatility	6.1%	5.6%	5.1%	4.9%
Maximum Drawdown *[Period]*	*2.7% [Aug 16 - Nov 16]*	*4.3% [Jan 15 - Sep 15]*	*4.3% [Jan 15 - Sep 15]*	*11.4% [Oct 06 - Oct 08]*
Beta	0.5	0.3	0.3	0.2

For more information get in touch: 0333 6000 500 sales@dynamicplanner.com www.dynamicplanner.com

Key Terms

Expected Real Return:

The portfolio's inflation adjusted expected return is based on the current asset allocation and the expected gross returns per asset class.

Expected Volatility:

The portfolio's potential inflation adjusted volatility based on the current asset allocation and the risk and correlation per asset class. This is known as ex-ante volatility.

Realised Volatility:

The dispersion of the portfolio's experienced inflation adjusted returns as measured by standard deviation. This is known as ex-post volatility.

Maximum Drawdown:

The largest continuous decline in the value of a portfolio for the given period.

Beta:

A relative measure of portfolio 'risk' that compares the realised volatility of the portfolio to a common UK equity index.

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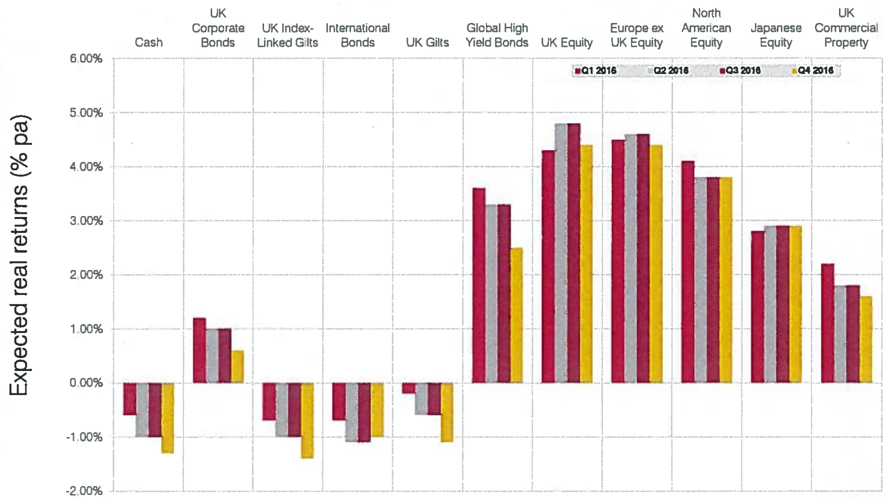
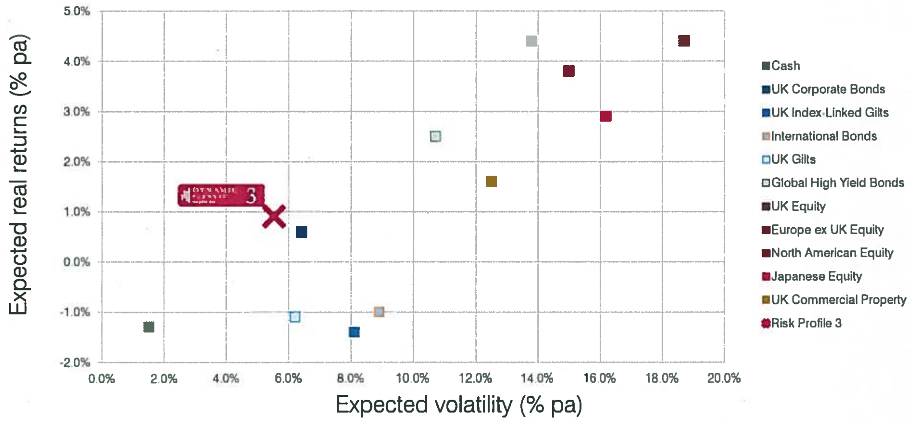
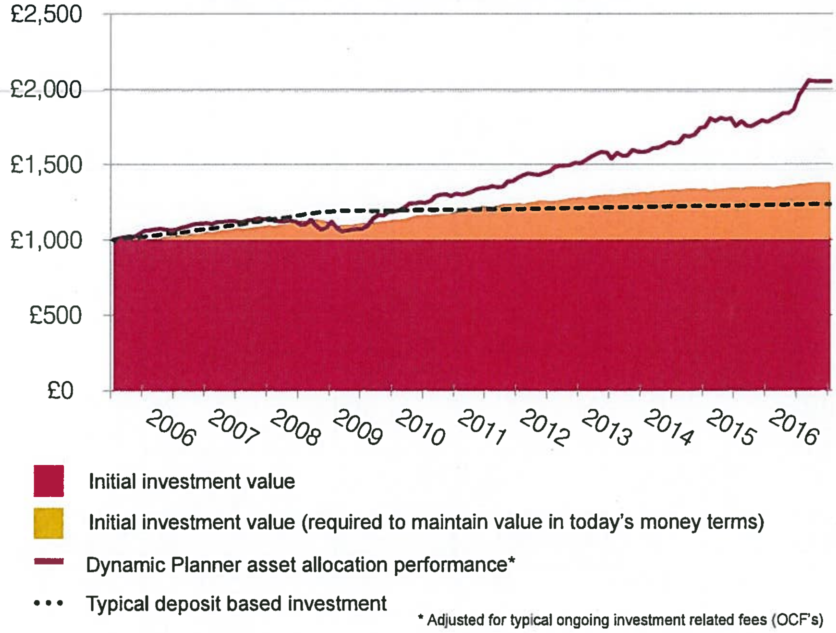
Asset Classes - Quarterly Changes in Expected Returns



Expectations of Asset Classes Used in Dynamic Planner Risk Profile 3



Performance of Dynamic Planner Asset Allocation 3 Since Launch - for £1000 Investment



* Adjusted for typical ongoing investment related fees (OCF's)

Important Information:
All asset allocations, assumptions, forecasts and past performance is calculated based on data live in Dynamic Planner as at the calendar quarter end date.

Dynamic Planner Quarterly Asset Allocation Factsheet Q4 2016
Risk Profile 4 - Lowest Medium Risk

Expected return **1.9%** pa (Inflation adjusted)

Expected volatility **7.4%** pa

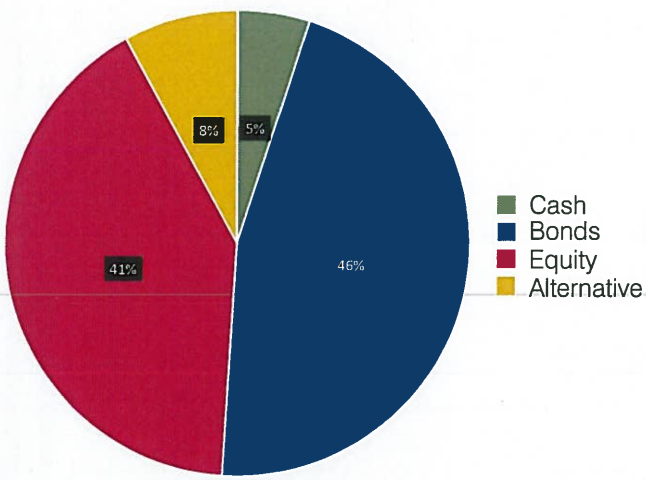
Profile Description: An investor who is a Risk Profile 4 would probably be concerned about the possibility of losing money on their investments, but may also want to achieve higher returns than are offered by bank accounts and low-risk investments. As a result, these investors are willing to accept only small losses by investing in some medium-risk assets such as property and possibly some shares, in order to achieve a higher return.

Market Round Up - Q4 2016

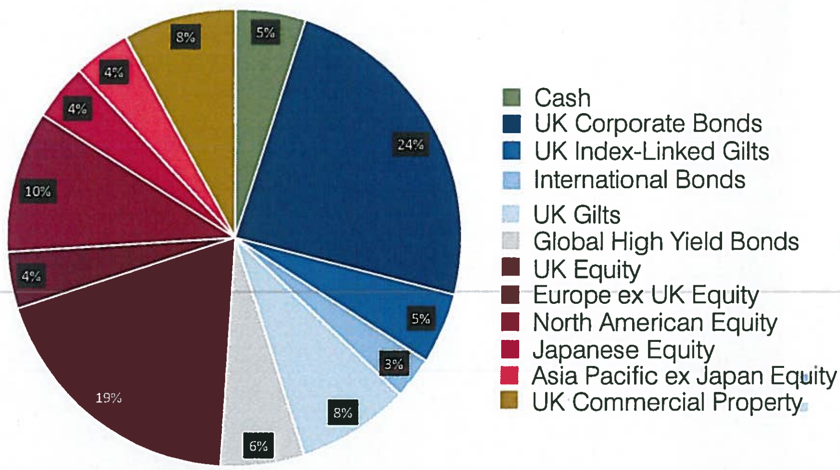
- Bonds - Political uncertainty in the US and Europe, the prospect of expansionary government spending plus another 0.25% rise in US interest rates all contributed to a broad sell-off for Government and (to a lesser extent) investment grade corporate bonds. However, High Yield Global Bonds made headway over the period, spurred by the search for yield and hopes of strengthening corporate balance sheets.
- Equities - Global markets, in general, enjoyed a strong quarter with the key theme being a rotation from defensive towards cyclical growth sectors of the market, referred to as the "reflation trade". Despite the political volatility, expectations for the global economy grew more optimistic, mainly in response to the election promises of Mr Trump. In the Eurozone, the extension of the ECB's quantitative easing programme provided continuing support, whilst UK equities also made progress, particularly financials (beneficiaries of steepening bond yields) and resources stocks. Japanese equities benefited from the further weakness of the yen. In contrast, emerging markets weakened due to continuing US dollar strength and worries over the potential direction of US trade and foreign policy.
- Alternatives - Commodities performed well given the release of more supportive Chinese economic data and stronger oil prices after OPEC agreed to production cuts. UK commercial property showed a continued recovery in confidence from its post-Brexit woes.

Risk Profile 4: Asset Allocation Breakdown

Broad Asset Classes



Sub Asset Classes



Realised Cumulative Performance (Inflation Adjusted) to 31st December 2016

	1 Year	3 Year	5 Year	Since Inception (June 2005)
Annualised Return	14.4%	7.7%	7.6%	3.7%
Annualised Return (Nominal)	17.3%	9.6%	9.9%	6.7%
Annualised Volatility	5.8%	6.1%	5.9%	7.3%
Maximum Drawdown *[Period]*	*2.0% [Oct 16 - Nov 16]*	*5.6% [Mar 15 - Sep 15]*	*5.6% [Mar 15 - Sep 15]*	*27.8% [May 07 - Feb 09]*
Beta	0.6	0.5	0.5	0.5

For more information get in touch: 0333 6000 500 sales@dynamicplanner.com www.dynamicplanner.com

Key Terms

Expected Real Return:

The portfolio's inflation adjusted expected return is based on the current asset allocation and the expected gross returns per asset class.

Expected Volatility:

The portfolio's potential inflation adjusted volatility based on the current asset allocation and the risk and correlation per asset class. This is known as ex-ante volatility.

Realised Volatility:

The dispersion of the portfolio's experienced inflation adjusted returns as measured by standard deviation. This is known as ex-post volatility.

Maximum Drawdown:

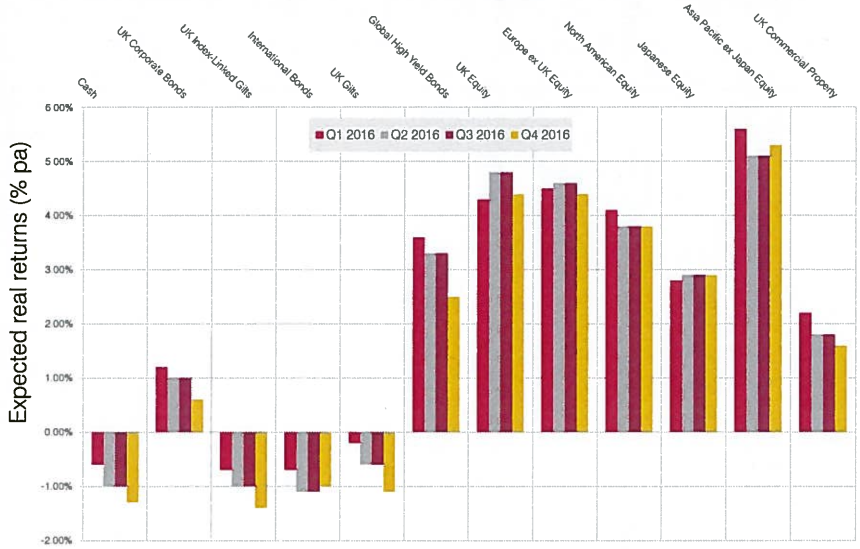
The largest continuous decline in the value of a portfolio for the given period.

Beta:

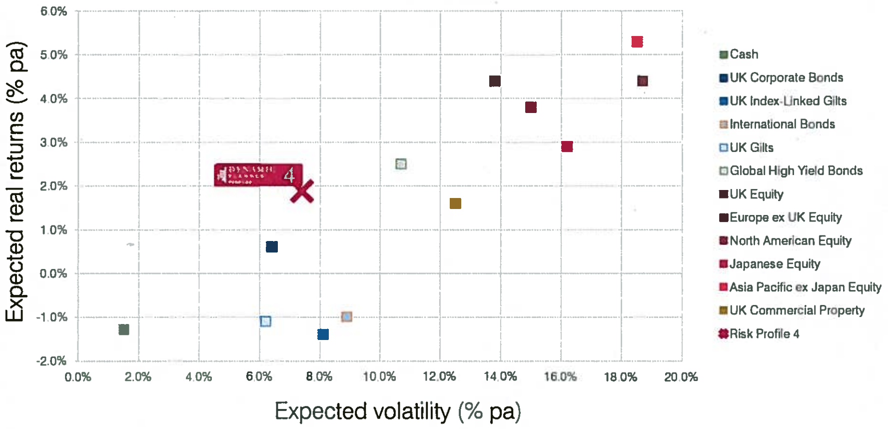
A relative measure of portfolio 'risk' that compares the realised volatility of the portfolio to a common UK equity index.

DYNAMIC PLANNER®

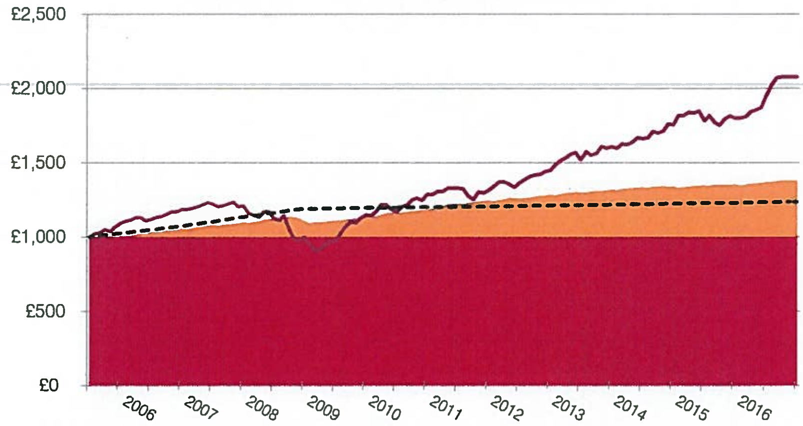
Asset Classes - Quarterly Changes in Expected Returns



Expectations of Asset Classes Used in Dynamic Planner Risk Profile 4



Performance of Dynamic Planner Asset Allocation 4 Since Launch - for £1000 Investment



- Initial investment value
- Initial investment value (required to maintain value in today's money terms)
- Dynamic Planner asset allocation performance*
- Typical deposit based investment

* Adjusted for typical ongoing investment related fees (OCF's)

Important Information:
All asset allocations, assumptions, forecasts and past performance is calculated based on data live in Dynamic Planner as at the calendar quarter end date.

Dynamic Planner Quarterly Asset Allocation Factsheet Q4 2016
Risk Profile 5 - Low Medium Risk

Expected return **2.9%** pa (Inflation adjusted)

Expected volatility **9.6%** pa

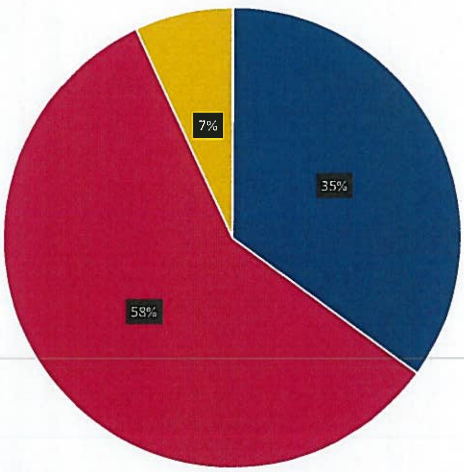
Profile Description: An investor who is a Risk Profile 5 is prepared to accept small losses, particularly in the short term, to gain higher returns than simply investing in low-risk investments. An appropriate investment portfolio would consist of a balanced mix of lower and medium-risk investments such as bonds and property as well as some higher-risk investments such as equities.

Market Round Up - Q4 2016

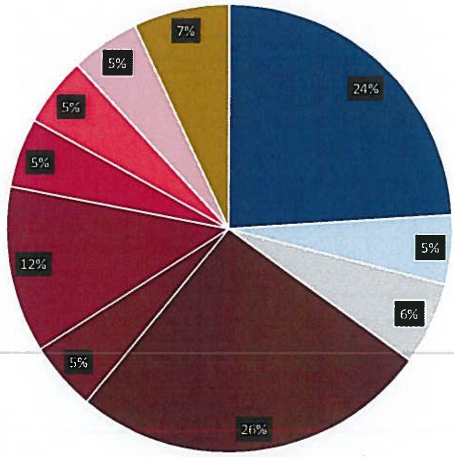
- Bonds - Political uncertainty in the US and Europe, the prospect of expansionary government spending plus another 0.25% rise in US interest rates all contributed to a broad sell-off for Government and (to a lesser extent) investment grade corporate bonds. However, High Yield Global Bonds made headway over the period, spurred by the search for yield and hopes of strengthening corporate balance sheets.
- Equities - Global markets, in general, enjoyed a strong quarter with the key theme being a rotation from defensive towards cyclical growth sectors of the market, referred to as the "reflation trade". Despite the political volatility, expectations for the global economy grew more optimistic, mainly in response to the election promises of Mr Trump. In the Eurozone, the extension of the ECB's quantitative easing programme provided continuing support, whilst UK equities also made progress, particularly financials (beneficiaries of steepening bond yields) and resources stocks. Japanese equities benefited from the further weakness of the yen. In contrast, emerging markets weakened due to continuing US dollar strength and worries over the potential direction of US trade and foreign policy.
- Alternatives - Commodities performed well given the release of more supportive Chinese economic data and stronger oil prices after OPEC agreed to production cuts. UK commercial property showed a continued recovery in confidence from its post-Brexit woes.

Risk Profile 5: Asset Allocation Breakdown

Broad Asset Classes



Sub Asset Classes



Realised Cumulative Performance (Inflation Adjusted) to 31st December 2016

	1 Year	3 Year	5 Year	Since Inception (June 2005)
Annualised Return	16.9%	7.8%	8.1%	4.4%
Annualised Return (Nominal)	19.8%	9.7%	10.5%	7.5%
Annualised Volatility	6.6%	7.1%	7.1%	9.3%
Maximum Drawdown *[Period]*	*2.1% [Oct 16 - Nov 16]*	*7.8% [May 15 - Sep 15]*	*7.8% [May 15 - Sep 15]*	*30.4% [Oct 07 - Feb 09]*
Beta	0.8	0.6	0.6	0.7

For more information get in touch: 0333 6000 500 sales@dynamicplanner.com www.dynamicplanner.com

Key Terms

Expected Real Return:

The portfolio's inflation adjusted expected return is based on the current asset allocation and the expected gross returns per asset class.

Expected Volatility:

The portfolio's potential inflation adjusted volatility based on the current asset allocation and the risk and correlation per asset class. This is known as ex-ante volatility.

Realised Volatility:

The dispersion of the portfolio's experienced inflation adjusted returns as measured by standard deviation. This is known as ex-post volatility.

Maximum Drawdown:

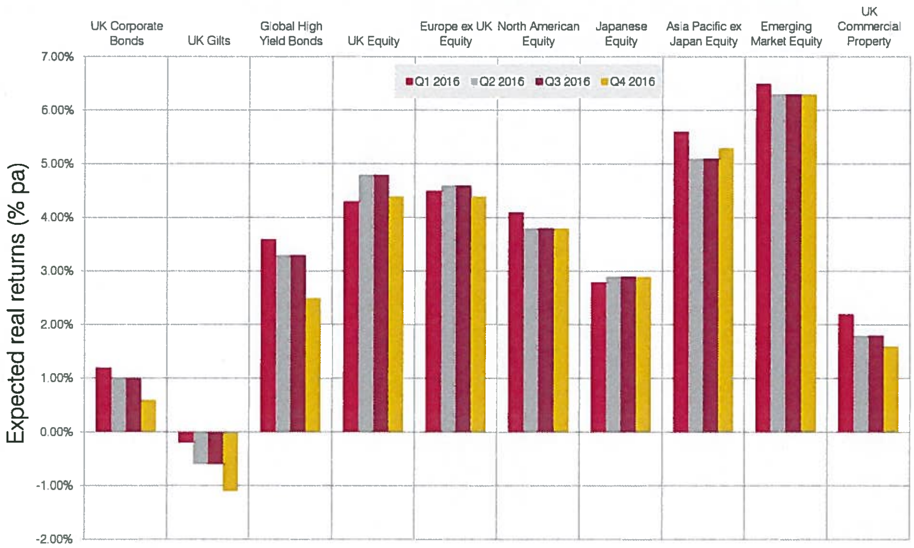
The largest continuous decline in the value of a portfolio for the given period.

Beta:

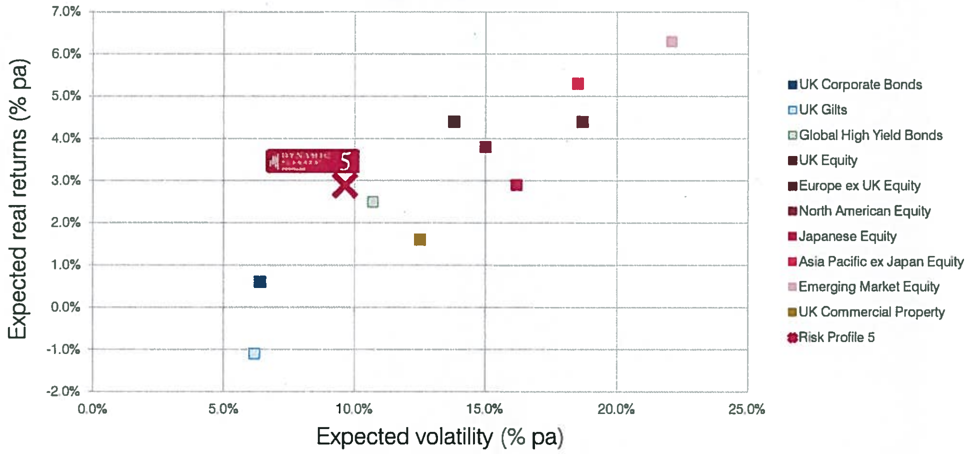
A relative measure of portfolio 'risk' that compares the realised volatility of the portfolio to a common UK equity index.

DYNAMIC PLANNER®

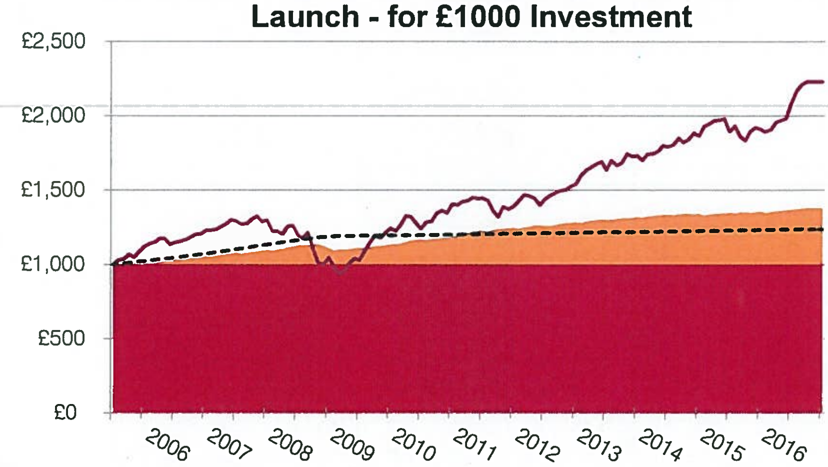
Asset Classes - Quarterly Changes in Expected Returns



Expectations of Asset Classes Used in Dynamic Planner Risk Profile 5



Performance of Dynamic Planner Asset Allocation 5 Since Launch - for £1000 Investment



Initial investment value

Initial investment value (required to maintain value in today's money terms)

Dynamic Planner asset allocation performance*

Typical deposit based investment

* Adjusted for typical ongoing investment related fees (OCF's)

Important Information:
All asset allocations, assumptions, forecasts and past performance is calculated based on data live in Dynamic Planner as at the calendar quarter end date.

Dynamic Planner Quarterly Asset Allocation Factsheet Q4 2016

Risk Profile 6 - High Medium Risk

Expected return
3.6%
pa
(Inflation adjusted)

Expected volatility
11.6%
pa

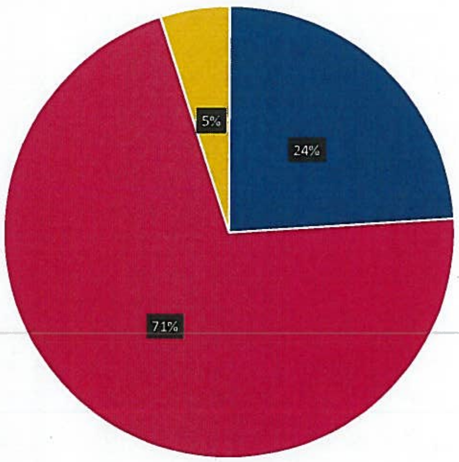
Profile Description: An investor who is a Risk Profile 6 is prepared to accept some losses, particularly in the short term, to achieve higher returns than by simply investing in low-risk investments. An investment portfolio within this profile would consist mainly of higher-risk investments such as shares with some lower and medium-risk investments.

Market Round Up - Q4 2016

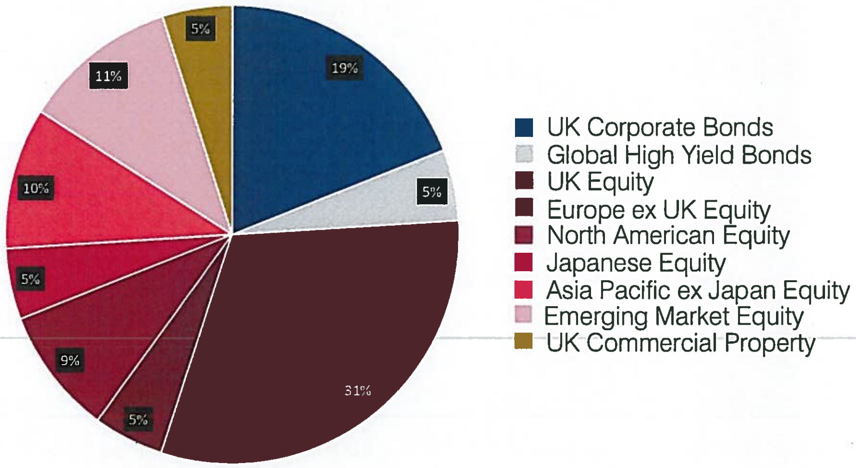
- Bonds - Political uncertainty in the US and Europe, the prospect of expansionary government spending plus another 0.25% rise in US interest rates all contributed to a broad sell-off for Government and (to a lesser extent) investment grade corporate bonds. However, High Yield Global Bonds made headway over the period, spurred by the search for yield and hopes of strengthening corporate balance sheets.
- Equities - Global markets, in general, enjoyed a strong quarter with the key theme being a rotation from defensive towards cyclical growth sectors of the market, referred to as the "reflation trade". Despite the political volatility, expectations for the global economy grew more optimistic, mainly in response to the election promises of Mr Trump. In the Eurozone, the extension of the ECB's quantitative easing programme provided continuing support, whilst UK equities also made progress, particularly financials (beneficiaries of steepening bond yields) and resources stocks. Japanese equities benefited from the further weakness of the yen. In contrast, emerging markets weakened due to continuing US dollar strength and worries over the potential direction of US trade and foreign policy.
- Alternatives - Commodities performed well given the release of more supportive Chinese economic data and stronger oil prices after OPEC agreed to production cuts. UK commercial property showed a continued recovery in confidence from its post-Brexit woes.

Risk Profile 6: Asset Allocation Breakdown

Broad Asset Classes



Sub Asset Classes



Realised Cumulative Performance (Inflation Adjusted) to 31st December 2016

	1 Year	3 Year	5 Year	Since Inception (June 2005)
Annualised Return	19.4%	7.8%	8.6%	4.8%
Annualised Return (Nominal)	22.4%	9.8%	11.0%	7.9%
Annualised Volatility	8.2%	8.4%	8.4%	11.1%
Maximum Drawdown *[Period]*	*2.6% [Oct 16 - Nov 16]*	*10.1% [Apr 15 - Sep 15]*	*10.1% [Apr 15 - Sep 15]*	*34.5% [Oct 07 - Feb 09]*
Beta	1.0	0.7	0.7	0.8

For more information get in touch: 0333 6000 500 sales@dynamicplanner.com www.dynamicplanner.com

IMPORTANT INFORMATION: PAST PERFORMANCE IS NOT A GUIDE TO FUTURE PERFORMANCE. THE VALUE OF INVESTMENTS, AND THE INCOME FROM THEM CAN FALL AS WELL AS RISE.

Key Terms

Expected Real Return:

The portfolio's inflation adjusted expected return is based on the current asset allocation and the expected gross returns per asset class.

Expected Volatility:

The portfolio's potential inflation adjusted volatility based on the current asset allocation and the risk and correlation per asset class. This is known as ex-ante volatility.

Realised Volatility:

The dispersion of the portfolio's experienced inflation adjusted returns as measured by standard deviation. This is known as ex-post volatility.

Maximum Drawdown:

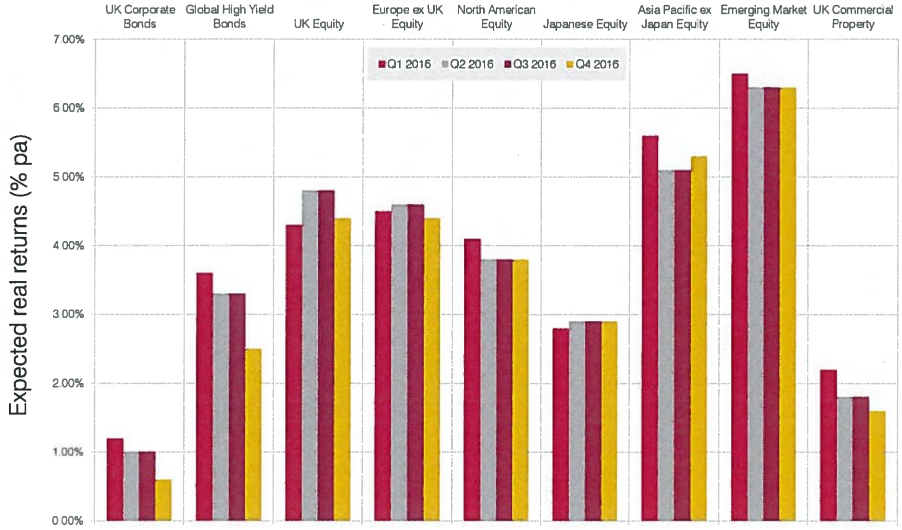
The largest continuous decline in the value of a portfolio for the given period.

Beta:

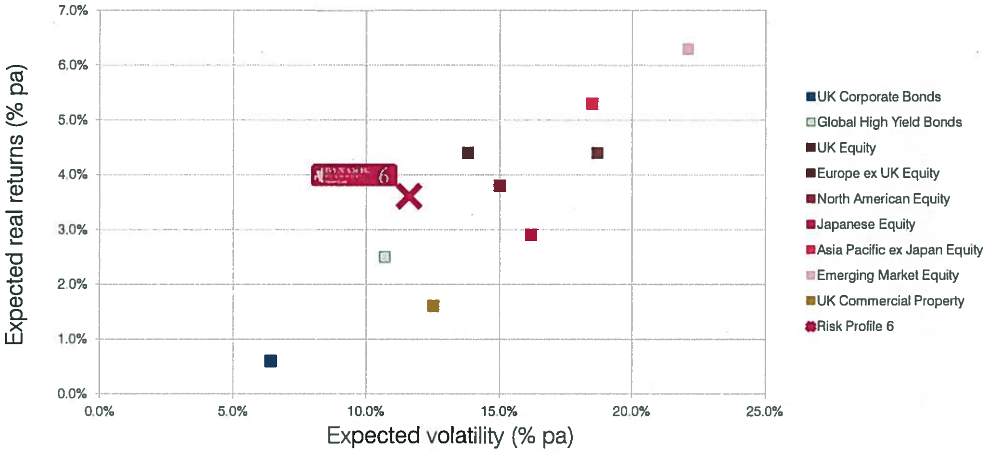
A relative measure of portfolio 'risk' that compares the realised volatility of the portfolio to a common UK equity index.

DYNAMIC PLANNER®

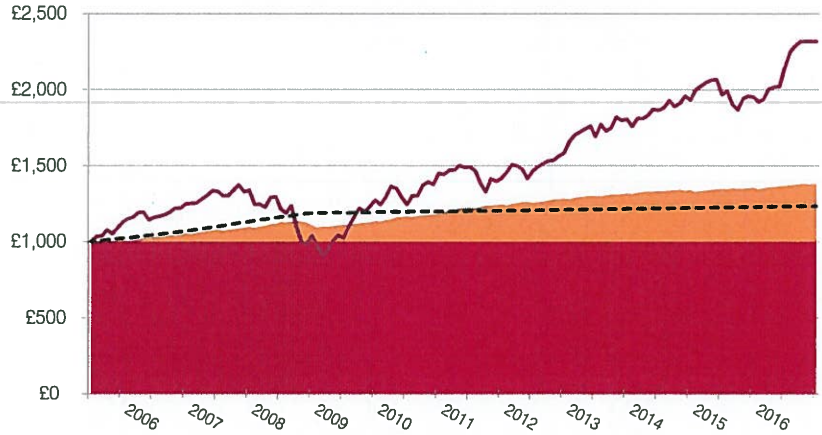
Asset Classes - Quarterly Changes in Expected Returns



Expectations of Asset Classes Used in Dynamic Planner Risk Profile 6



Performance of Dynamic Planner Asset Allocation 6 Since Launch - for £1000 Investment



Initial investment value

Initial investment value (required to maintain value in today's money terms)

Dynamic Planner asset allocation performance*

Typical deposit based investment

* Adjusted for typical ongoing investment related fees (OCF's)

Important Information:
All asset allocations, assumptions, forecasts and past performance is calculated based on data live in Dynamic Planner as at the calendar quarter end date.

Appendix 3

ASHE 6115 & RPI Research in relation to Percentage Increases

Year	ASHE 6115										RPI (Sept - Sept [1987 = 100])
	10%	20%	25%	30%	40%	60%	70%	75%	80%	90%	
1999	£3.60	£3.90	£4.07	£4.25	£4.67	£5.40	£5.94	£6.23	£6.58	£7.65	166.2
1999/2000	2.78%	3.33%	3.19%	3.53%	3.64%	1.85%	2.36%	3.05%	3.34%	2.61%	3.31%
2000	£3.70	£4.03	£4.20	£4.40	£4.84	£5.50	£6.08	£6.42	£6.80	£7.85	171.7
2000/01	5.68%	6.70%	7.62%	7.27%	6.40%	5.45%	4.93%	4.21%	3.97%	4.33%	1.69%
2001	£3.91	£4.30	£4.52	£4.72	£5.15	£5.80	£6.38	£6.69	£7.07	£8.19	174.6
2001/02	8.70%	6.98%	6.64%	6.57%	5.44%	7.76%	7.99%	8.22%	8.20%	6.84%	1.72%
2002	£4.25	£4.60	£4.82	£5.03	£5.43	£6.25	£6.89	£7.24	£7.65	£8.75	177.6
2002/03	5.88%	8.70%	8.71%	9.34%	7.92%	8.64%	8.13%	8.01%	8.10%	8.91%	2.76%
2003	£4.50	£5.00	£5.24	£5.50	£5.86	£6.79	£7.45	£7.82	£8.27	£9.53	182.5
2003/04	7.78%	7.40%	6.49%	4.91%	4.44%	4.71%	3.09%	3.45%	3.99%	4.62%	3.07%
2004	£4.85	£5.37	£5.58	£5.77	£6.12	£7.11	£7.68	£8.09	£8.60	£9.97	188.1
2004/05	5.15%	4.10%	4.30%	5.20%	5.23%	4.50%	4.56%	4.70%	4.19%	3.31%	2.66%
2005	£5.10	£5.59	£5.82	£6.07	£6.44	£7.43	£8.03	£8.47	£8.96	£10.30	193.1
2005/06	5.29%	4.47%	3.95%	2.80%	3.26%	3.63%	3.74%	2.83%	3.24%	3.59%	3.63%
2006	£5.37	£5.84	£6.05	£6.24	£6.65	£7.70	£8.33	£8.71	£9.25	£10.67	200.1
2006/07	5.40%	5.31%	5.12%	4.97%	5.41%	5.45%	5.64%	5.74%	5.84%	6.65%	3.95%
2007	£5.66	£6.15	£6.36	£6.55	£7.01	£8.12	£8.80	£9.21	£9.79	£11.38	208
2007/08	3.36%	2.44%	2.04%	2.29%	2.71%	2.59%	3.64%	3.80%	3.27%	2.64%	5.00%
2008	£5.85	£6.30	£6.49	£6.70	£7.20	£8.33	£9.12	£9.56	£10.11	£11.68	218.4
2008/09	2.56%	2.70%	2.93%	2.99%	3.06%	2.16%	2.30%	2.72%	2.47%	3.60%	-1.42%
2009	£6.00	£6.47	£6.68	£6.90	£7.42	£8.51	£9.33	£9.82	£10.36	£12.10	215.3
2009/10	1.00%	1.24%	1.80%	2.03%	1.08%	2.23%	1.29%	0.92%	0.77%	0.50%	4.64%
2010	£6.06	£6.55	£6.80	£7.04	£7.50	£8.70	£9.45	£9.91	£10.44	£12.16	225.3
2010/11	-0.17%	-1.68%	-2.21%	-2.41%	-2.93%	-2.87%	-2.96%	-2.42%	-2.11%	-1.97%	5.59%
* 2011	£6.05	£6.44	£6.65	£6.87	£7.28	£8.45	£9.17	£9.67	£10.22	£11.92	237.9
2011/12	2.64%	2.02%	2.26%	1.89%	2.20%	0.71%	0.44%	0.21%	0.29%	0.42%	2.65%
2012	£6.21	£6.57	£6.80	£7.00	£7.44	£8.51	£9.21	£9.69	£10.25	£11.97	244.2
2012/13	1.45%	0.61%	0.00%	0.00%	-0.54%	-0.12%	0.11%	0.41%	0.39%	0.42%	3.15%
2013	£6.30	£6.61	£6.80	£7.00	£7.40	£8.50	£9.22	£9.73	£10.29	£12.02	251.9
2013/14	1.75%	1.97%	2.06%	1.71%	1.76%	0.59%	0.11%	-0.10%	-0.78%	-0.58%	2.26%
2014	£6.41	£6.74	£6.94	£7.12	£7.53	£8.55	£9.23	£9.72	£10.21	£11.95	257.6
2014/15	3.59%	3.56%	2.45%	2.53%	2.52%	2.11%	2.28%	1.65%	1.67%	2.18%	0.78%
2015	£6.64	£6.98	£7.11	£7.30	£7.72	£8.73	£9.44	£9.88	£10.38	£12.21	259.6
2015/16	8.43%	5.44%	5.49%	5.48%	4.66%	3.32%	3.50%	3.24%	3.66%	2.78%	2.04%
** 2016 First Release	£7.20	£7.36	£7.50	£7.70	£8.08	£9.02	£9.77	£10.20	£10.76	£12.55	264.9

A Response to the Discount Rate Consultation

PREPARED FOR

The Association of Personal Injury Lawyers (APIL)

PREPARED BY

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EXPERT WITNESS

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CONTENTS

APPENDIX

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EXPERT WITNESS

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SECTION 1 - INTRODUCTION

1. I have been instructed by the Association of Personal Injury Lawyers (APIL) to review the current position with regards to the calculation of the Discount Rate used to quantify personal injury and clinical negligence settlements.

2. Frenkel Topping Expert Witness are a part of Frenkel Topping Limited who are wholly owned by Frenkel Topping Group PLC.

3. Frenkel Topping Limited are a specialist independent financial adviser (IFA) firm who were established in 1989 and provide both pre and post settlement advice to clients in receipt of a personal injury or clinical negligence award.

4. Frenkel Topping Limited introduced the concept of Structured Settlements to the UK and advised on the first settlement to include a structure which was completed in 1989.

5. In addition to this Frenkel Topping Limited pioneered the use of personal injury trust to protect vulnerable individuals entitlement to means tested benefits,

6. A Frenkel Topping Amendment was included in section 142 of the Finance Act 1995 which added a provision to the Income and Other Taxes Act 1988 which ensured that annuity payments and subsequently periodical payments made to recipients of personal injury or clinical negligence settlements would not be classed as income for the purposes of income tax and would accordingly be paid without deduction of tax.

7. In addition to the above Frenkel Topping Limited were the first IFA to be appointed by the Court of Protection to provide investment advice to protected parties.

8. I am the Commercial Director of Frenkel Topping Limited and also a Director or Frenkel Topping Group.

9. I have over 20 years' experience providing financial advice to retail, personal injury, clinical negligence and corporate clients.

10. I pioneered the current method of assessing the suitability of periodical payments used by Frenkel Topping when providing advice to the Court on this matter and have been instrumental in the design and implementation of Frenkel Topping training seminars to Counsel and Solicitors including “Complex Claims and Periodical Payments 2016” and “The Implications of the Discount Rate 2017”.

11. To date I have prepared in excess of 400 Expert Witness Reports and Joint Statements for the Court on the use of Periodical Payments in the structure of an award and also the value of the loss of retirement benefits within personal injury and clinical negligence claims.

12. I have been assisted in the preparation of this report by members of my firms staff although the opinions expressed in this report are my own.

13. A copy of my Curriculum Vitae is provided in Appendix A to this Report.

SECTION 2 - BACKGROUND

14. The Damages Act 1996 gave the Lord Chancellor general power to set a discount rate. Originally multipliers gave credit for a discount rate of 4% to 5% but this made no provision for the effects of inflation.

15. In the case of Wells V Wells heard by the House of Lords in May 1998 no order had been made under section 1 (1) of the damages act in respect of an appropriate discount rate. The rate applied, derived by Lord Diplock, was referred to as being set based on "interest rates to times of stable currency".

16. Following the decision in Wells V Wells the discount rate was set at the then current net rate of return from Index Linked Gilt Securities (ILGS) which was 3%, this was amended by Lord Irvine in 2001 to the 2.5% which was applied until 20th March 2017 when the rate was amended to -0.75%.

17. The use of ILGS is based on the fact that investors of personal injury or clinical negligence settlements are unlikely or should not be exposed to the same levels of investment risk as ordinary investors given the fact that they cannot return to Court for additional funds should a poor investment decision be made and the impact that a poor decision may have on the claimants standard of living.

18. The returns available from ILGS have altered significantly since the decision was taken to base the discount rate on investments solely into this type of asset yet until the announcement in February 2017 there had been no change to this rate, in my opinion this will have resulted in the under settlement of claims for a significant number of claimants over the last few years.

19. There are a number of arguments in respect of the suitability of linking the discount rate to ILGS and I have covered these in more detail in a section 3 of this report, however to summarise the arguments are:

- No one has ever invested solely in ILGS

- It is highly unlikely that ILGS can be purchased on the 'Primary Market'
- ILGS purchased on the 'Secondary Market' will be subject to price fluctuations and may not be fair/good value for money
- Timeframe of holding assets to redemption is unlikely to fit with a client's need for income or capital to meet their needs

20. If linking the discount rate to an investment in ILGS then what would be the correct approach and what would be the potential implications for settlement of each of these.

21. Alternative methods addressed in more detail in section 7 of this report could be;

    - Assumed investment into cash based deposits only
    - Investment into a basket of assets more akin to the investment decisions claimants are faced with in the real world, covered in section 4 of this report
    - Nil discount rate for shorter term losses with longer term losses being paid via a periodical payment or with risk built into solely longer term losses

22. Regardless of the correct approach decided upon there are also a number of 'knock on effects' which will impact on the claimants financial position as a result of the decisions made:

    - Table 27 – based on the current -0.75% 'discount rate' table 27 actually now enhances rather than discounts the value of the loss to the client
    - Roberts v Johnstone Calculations

23. Since the announcement in February 2017 regarding the change of discount rate my experience of the approach of Defendants in settling claims has changed significantly. Whereas Defendants were, in the main, resistant to the inclusion of Periodical Payments (PPO) in settlements this has changed and more Defendants have been making offers utilising PPO's to provide for longer term losses. This statement does not include cases litigated against NHSLA as they have always been aware and mindful of the importance of PPO's to claimants.

24. The above statement is confirmed by the GIRO Working Party paper which illustrates the propensity of insurers to include PPO's in large loss settlements. The 'Paper' also demonstrates the 'Real Discount Rate' that Insurance companies have applied to their reserves to cover the costs of future PPO's. It is unsurprising that most Insurance companies have over recent years applied a 0% equivalent rate for their own reserves.

25. The move for defendant insurers to resist the inclusion of PPO's in settlements has come directly from their own actuaries, believing that a larger payment for a 'once and for all settlement' on a lump sum basis only was a better proposition for their respective cash flows and balance sheets.

26. I have covered the impact of including PPO's in a claimant's settlement in more detail in section 5 of this report.

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SECTION 3 - INDEX LINKED GILTS (ILGS)

27. What is an Index Linked Gilt

The premise of a Gilt investment is where an investor 'loans' an amount of money to the Government on the agreement that at the end of a specified term they will receive back the amount of the 'loan' plus a specified rate of interest, known as the coupon rate.

28. An index linked gilt (ILGS) is where the amount of the loan is linked to inflation via the retail price index and the coupon rate is paid on the new loan value which has been adjusted for inflation, eg;

	Conventional Gilt	ILGS
Initial Investment / Loan Amount	£100	£100
Coupon Rate	1%	1%
Increase in RPI/Inflation	3%	3%
New Investment / Loan Amount adjusted for Inflation	N/a	£103
Value of Investment at end of Year 1 (including Coupon)	£101	£104.03

29. ILGS are issued by the Debt Management Office on a quarterly basis and investors make a bid to purchase these on the 'primary market'. The price paid for an ILGS will depend on market forces or the demand for new issues across all types of investor.

30. Upon the issue of new ILGS there are 16 banks who act as what are referred to as market makers for the gilt market. These banks will bid for the gilts in order to try and purchase them at a competitive rate. Whoever puts in the most competitive bid will secure the ILGS.

31. At present there is a high demand for Gilts and ILGS which has inflated the purchase price and led to negative returns.

30. The reason for additional demand is the Government's policy of Quantitive Easing, which is aimed to stimulate the economy. When the Debt Management Office issue Gilts these are being purchased by the Bank of England which is exhausting the supply on the primary market.

31. Other Banks and Institutional Investors such as Pension Funds use gilts to hedge their liabilities and as a result of the shortage on the primary market they are being forced to either purchase gilts on the secondary market at a price which is currently inflated and make alternative investments into Corporate Bonds which is providing funding for businesses and therefore helping to stimulate the economy.

32. This cycle means that it is virtually impossible for a retail investor to purchase an ILGS on the primary market which they could then hold to redemption and receive a positive return.

33. A retail investor is entitled to put in a non-competitive bid to the Debt Management Office up to a maximum of £0.5million on first issue of a gilt. In light of the demand for Gilts with Institutional Investors and Banks it would not be possible for a retail investor to secure a gilt on the primary market and even if they did the price that they would need to pay would lead to a negative return on the gilt investment.

34. Each ILGS will have what is known as a 'break-even point', this is the rate that inflation would need to be for the ILGS not to provide a negative return or in other words lose money. If an investor is paying over 'par' (face value) for an investment, this will have an even bigger impact on the overall return/loss.

35. Based on current markets the average break-even point would be 3.14%. What this means is that the rate of increase in the Retail Prices Index would need to be 3.14% in order for an investor to get their money back on a gilt.

36. Average RPI over the last 10 years has been 2.75%, based on information provided by the Office for National Statistics. This means that in the current financial market gilts do not represent good value.

37. Alternative Methods of Holding ILGS

As detailed in the previous section it would not be possible, in the current financial climate for a retail investor to purchase ILGS on the primary market on issue and hold them until their redemption date as is assumed in the current methodology behind the setting of the discount rate.

32. As a result a retail investor would have to purchase either an ILGS fund or portfolio on the secondary market. Both of these alternative options would result in the investor having to pay an initial charge to purchase the investment and an ongoing annual management charge for the fund or portfolio provider to manage the investments on an ongoing basis.

33. An ILGS fund or portfolio buys and sells gilts on the secondary market in order to try and achieve a positive return, it would be unlikely for any gilt held within an ILGS fund or portfolio to be held to redemption.

34. Many large investment providers will have an ILGS fund within their fund range, the retail investor would have to decide which of the funds available on the market would be the most suitable and how much money should be invested.

35. Alternatively they could instruct a stockbroker to provide them with a portfolio of ILGS which have been purchased on the secondary market and decide whether or not the gilts held within the portfolio should be held to redemption or sold before they reach their redemption date.

36. Few investors would have the financial investment knowledge to manage this themselves and would therefore need to instruct an expert to provide them with advice and manage the

additional costs associated with investment through the secondary markets such as dealing, transactional and management fees.

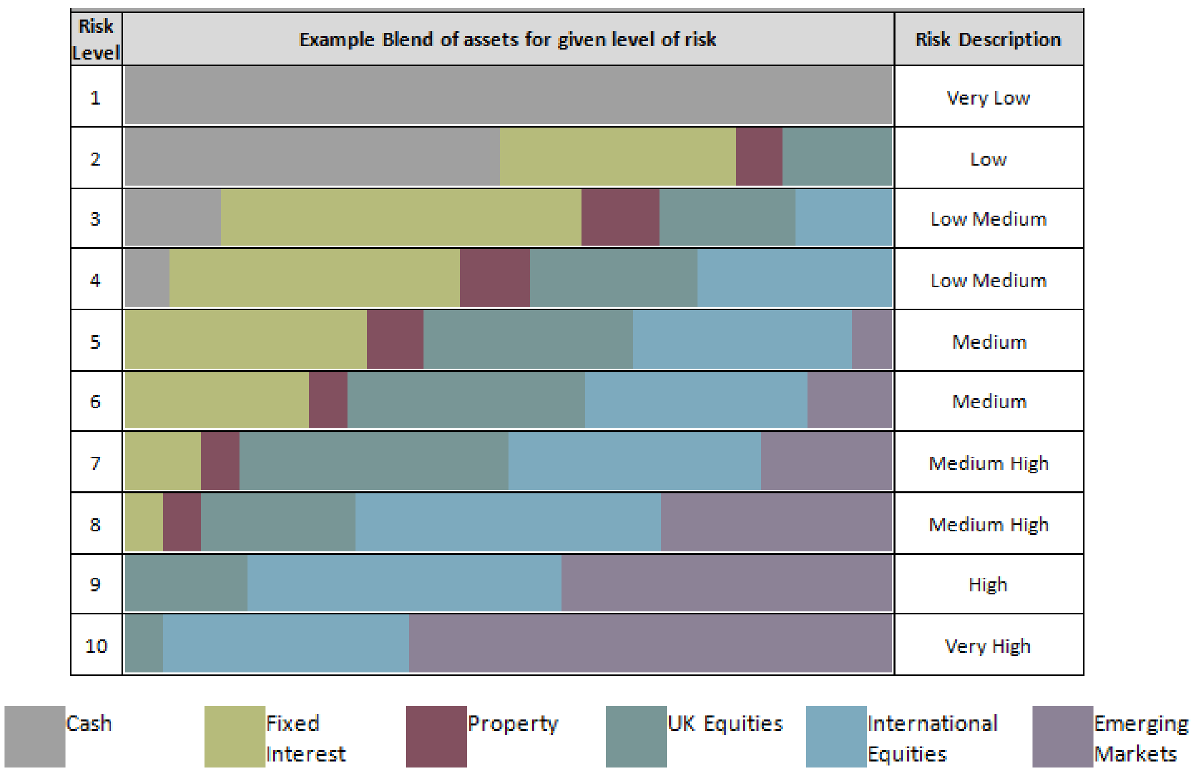
37. The investor would have to seek advice from a specialist in Index Linked Gilts, who may not have experience in dealing with financial settlements received through the Court. It would be unlikely that a Whole of Market Independent Financial Adviser would provide advice to a retail investor solely in relation to ILGS, as they are required by the Financial Conduct Authority to provide holistic financial advice on all products and services available in the current market place. Furthermore it is incumbent on them to provide advice on the most suitable solution for the clients ongoing financial needs, objectives, attitude to risk and capacity for loss which may not be investment in ILGS.

SECTION 4 – HOW DO CLAIMANTS CURRENTLY INVEST

38. When a claim has settled it is essential for the claimant and their representatives to receive independent financial advice, this is to ensure that the settlement received can be invested appropriately to meet their ongoing needs and objectives.

39. As previously explained, a retail investor would not be able to invest directly via the primary market in index linked gilts, advice must be provided that fits with a claimants attitude to investment risk, needs and objectives. The investment returns received from claimant portfolios will vary depending on when the funds are invested, when a claimant needs access to them and attitude to investment risk.

40. Different advisers assess risk using different scales, Frenkel Topping assess risk on a scale of 1-10, these risk parameters are broken down into the following risk profiles:



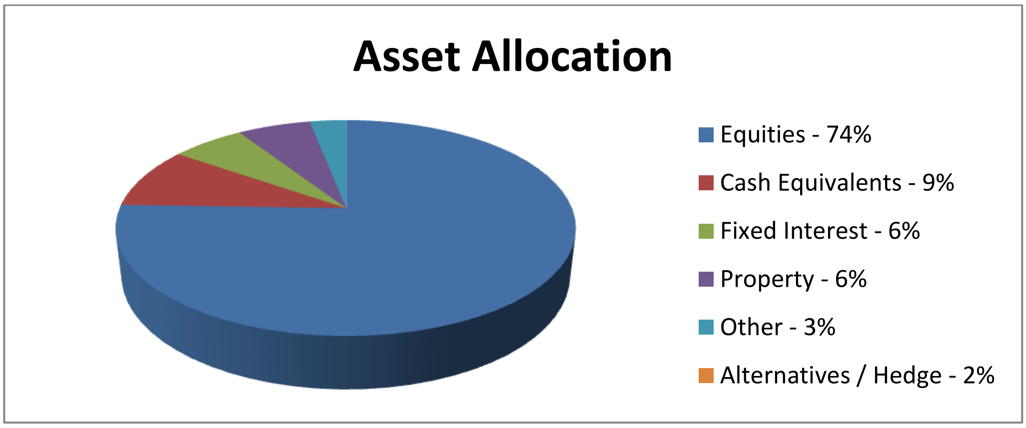
41. I have taken a sample of our existing client's investment portfolios to show the variation of returns between different risk profiles and asset allocation, the table below shows the returns received by real clients:

Table1

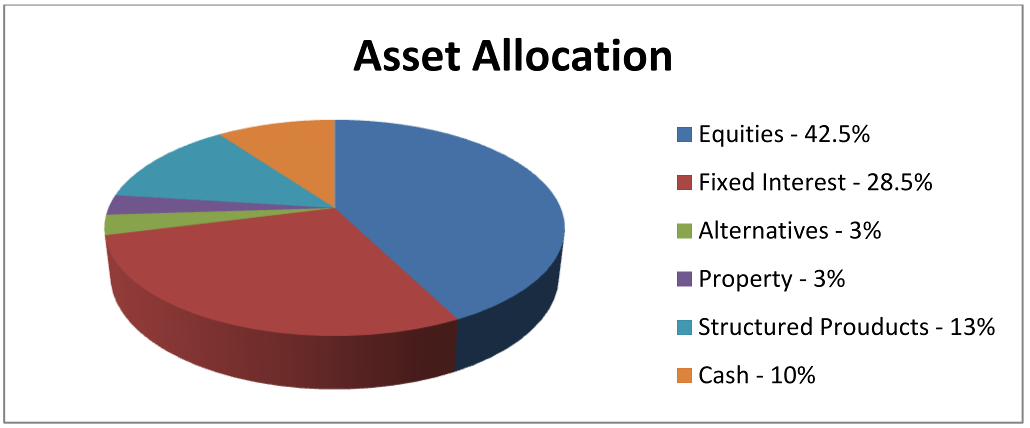
Client Name	Risk Profile	Start Date	Since Inception	Annualised Return	Best performing Period
Client A	6 - Medium	March 2005	71.77%	5.98%	13.71%
Client B	5 – Medium	October 2003	38.24%	2.83%	15.50%
Client C – portfolio 1	4 – low medium	June 2011	27.35%	5.47%	4.69%
Client C – portfolio 2	4 – low medium	June 2011	23.33%	4.66%	5.41%
Client D	3 – low medium	December 2009	17.19%	2.45%	3.61%

42. I have detailed below the asset allocation for each client in the best performing period of investment returns:

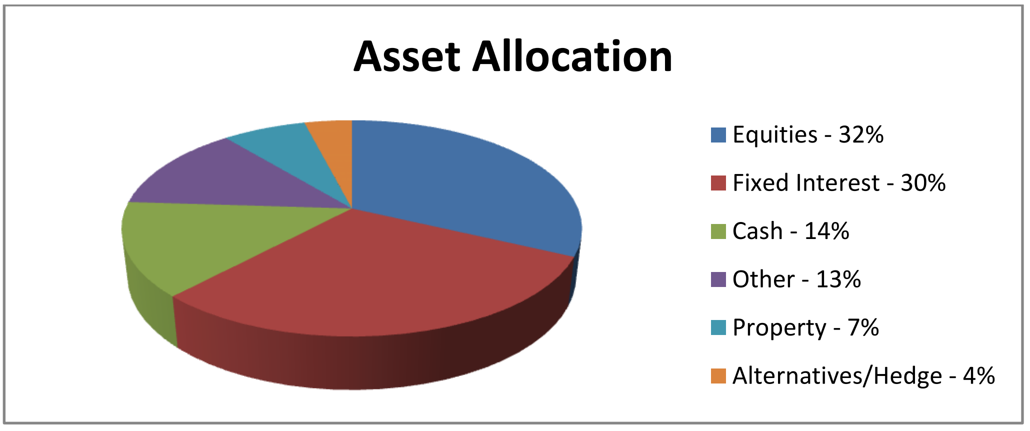
Client A – Best performing period, 6 months to August 2016



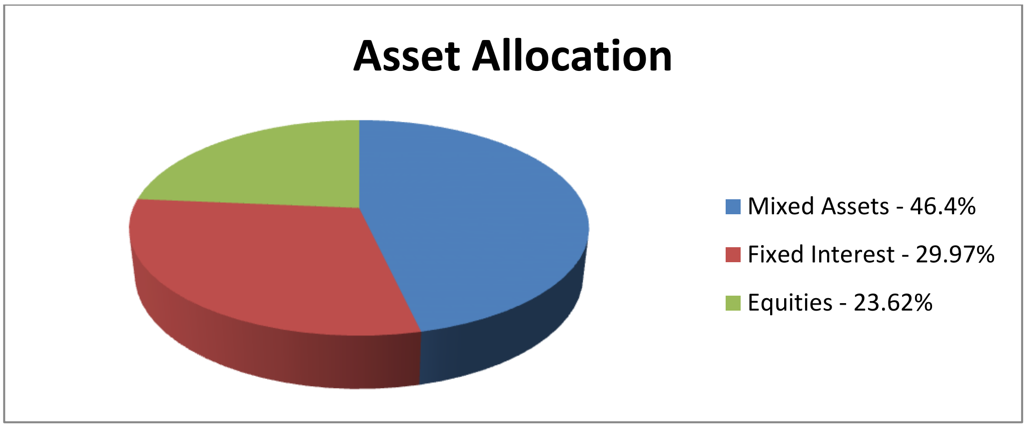
Client B – Best performing period, 6 months to August 2009



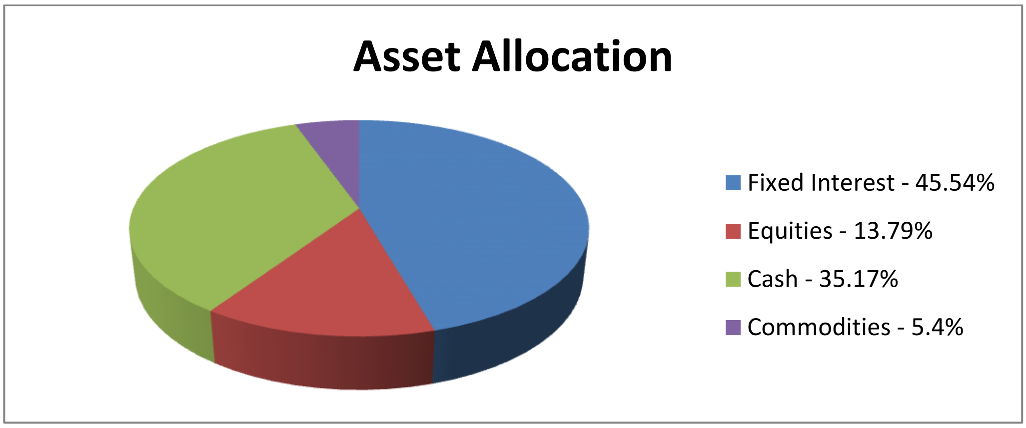
Client C (portfolio 1) – Best performing period, 6 months to December 2012



Client C (portfolio 2) – Best performing period, 6 months to December 2013



Client D – Best performing period, 6 months to December 2016



43. The table and charts above show just how different a claimant's investment portfolio can look based on the timing of the investments, global market conditions at the time and level of risk the best suits their needs and objectives.

44. When making investment decisions claimants and their representatives, alongside their investment advisers may need to think about how much risk is needed to meet what they need from the funds. This could result in a need to take more risk than a claimant would be ordinarily comfortable with to meet their needs or a claimant having to make adjustments to their daily living or care package that could impact on their wellbeing.

45. Robust investment decisions are essential to the longevity of the personal injury or clinical negligence settlement and it is essential that these decisions are regularly reviewed and monitored by the claimant's investment adviser to ensure that they continue to meet the client needs and that returns are maximised with the utilisation of the different tax wrappers available to ensure that the level of risk needed to meet a claimant's needs is minimised.

46. It is vitally important to note however the correlation between the returns of the aforementioned portfolio's and their corresponding asset allocations. For example client A has annualised return of 5.98% but has an exposure to equities of 74%. This is not an asset allocation we would expect to see or recommend for a client with a nil/low risk appetite.

47. In addition to the above it is also noteworthy that the above figures (table 1) reflect a 'Gross' return on investment and take no account of inflation and a claimants individual tax position. It is not quite so simple to make assumptions on the implications of tax as this is heavily dependent on an individual's tax position and their marginal rate of taxation. However, the court in 'Wells v Wells' adopted an arbitrary 15% rate so I have applied the same to these returns.

48. Consumer prices in the United Kingdom rose by 2.3 percent in the year to March 2017, the same pace as in February and in line with market expectations. The inflation rate remained at its highest level since September 2013, mainly boosted by rising cost of food, alcohol and tobacco, clothing and footwear, and miscellaneous goods and services. The annual core inflation rate, which excludes prices of energy, food, alcohol and tobacco, fell to 1.8 percent in March from 2 percent in February and below market consensus of 1.9 percent. Inflation Rate in the United Kingdom averaged 2.58 percent from 1989 until 2017, reaching an all-time high of 8.50 percent in April of 1991 and a record low of -0.10 percent in April of 2015.

49. **Table 2**

Client Name	Risk Profile	Start Date	Annualised Return (Net of 15% Tax)	Average Inflation since 1989	Equivalent Discount Rate
Client A	6 - Medium	March 2005	5.08%	2.58%	2.5%
Client B	5 – Medium	October 2003	2.41%	2.58%	-0.17%
Client C – portfolio 1	4 – low medium	June 2011	4.65%	2.58%	2.07%
Client C – portfolio 2	4 – low medium	June 2011	3.96%	2.58%	1.38%
Client D	3 – low medium	December 2009	2.08%	2.58%	-0.50%

50. Given the information contained in the above table it is clearly evident that if an individual is prepared to accept an elevated level of risk, has a much higher equity content and times the investment market particularly well, that a positive return can be achieved.

51. Equally important to note though is that the polar opposite is also true. Therefore if you don’t have a greater capacity for loss/appetite for risk and investment market timings don’t play to your advantage, then you could be looking at negative returns, even with a balanced portfolio of assets.

SECTION 5 – THE ADVANTAGES AND DISADVANTAGES OF PERIODICAL PAYMENTS

52. Since the introduction of the revised discount rate, -0.75%, there has been an increase in the number of defendants wishing to include periodical payments in the structure of a settlement, this is a significant shift from a defendant's approach under the 2.5% discount rate regime when defendants preferred settling claims on a lump sum basis as this allowed them to value the claim and discharge it from their accounts in the year of settlement.

53. Inclusion of Periodical Payments in a settlement does reduce a claimants need to take investment risk with a portfolio however they are generally only considered to be an appropriate financially viable option for settlements in excess of £500,000 as a minimum.

54. Whilst PPO's are inherently investment risk free there are a number of advantages and disadvantages that should be considered when thinking about whether they are appropriate to provide a claimant with a fair and adequate settlement. I have detailed below the advantages and disadvantages associated with PPO's.

Advantages	**Disadvantages**
Guaranteed Payments All payments would be guaranteed throughout the Claimant's lifetime, which is a major advantage. Payments made by way of Periodical Payments ensure that the Claimant is neither under or over-compensated.	**Inflexibility** A Periodical Payment Order is required to specify at the outset the amount and frequency of payments, which cannot later be varied. Thus, should the Claimant's needs alter in the future, the Periodical Payments would be fixed, which may lead to a shortfall in the provision of care.

Investment Risk Any investment risk which would apply to a lump sum is removed by the use of Periodical Payments. There is no investment risk, and the Claimant can be secure in the knowledge that the payments will continue for the rest of their lifetime.	**Investment Opportunities** Payment by way of a lump sum would allow Claimants access to investment opportunities which would not be available should the award be made by way of Periodical Payments. This would also assist with the issue of flexibility, in that Claimants could choose to "cut their suit according to their cloth" as their care needs ebb and flow throughout their lifetime
Security The Court will only award periodical Payments where the Defendant is considered to be "reasonably secure". Most Police Authorities and authorised insurers will fall into this category.	**Security** The Court will only award periodical Payments where the Defendant is considered to be "reasonably secure". Most Police Authorities and authorised insurers will fall into this category.
Tax-Free Income Payments under Periodical Payment Orders are free of tax, whilst although the damages award itself is tax-free, any income derived from the investment of the award would be subject to Income Tax at both basic and higher rates, if applicable.	

Index-Linking Payments under a PPO are likely to be increased in line with an earnings based index, e.g. ASHE 6115, if they are intended to be made for future care or other relevant indices. This should ensure that the payments will provide a sustainable care regime for the remainder of the Claimants' life, irrespective of prevailing economic conditions at the time.	

55. You will see in the table above that I have included the Security of the Defendant in both sections. Whilst the Court will only award a PPO where the Defendant is deemed to be 'Secure' to ensure continuity of payments to the Claimant throughout their lifetime, what if the Defendant is not considered to be financially secure.

56. Some Claimants will be automatically excluded from having a settlement which is structured to include PPO's as the Defendant or Defendant Insurer they are making the claim against are not deemed to be secure to provide income for their lifetime. This puts them at a major disadvantage where there may be large future losses.

57. Whilst including PPO's more frequently in settlements would remove some of the issues associated with setting an appropriate discount rate a solution would need to be considered to allow all Claimants access to PPO's regardless of the security of the Defendant.

58. There are a number of options that could be considered to remove the security issue, the Government could provide an underwritten guarantee for non-secure Defendants, depending on the assessed risk of providing the PPO for the Claimant's lifetime or further work could be undertaken in the Insurance Industry to provide a PPO Annuity, similar to the old style Structured Settlement Annuities which would be purchased by the Defendant from a 'Secure' Insurer who would guarantee the income for the Claimant's lifetime.

SECTION 6 – MULTIPLIERS

59. The introduction of a negative discount rate also hasn't negated the necessity for the Claimant to take some Investment Risk when settlement is made by way of a lump sum.

60. Taking an example of a Claimant Male who is aged 24 at date of trial and has a normal Life expectation to age 89, he has care costs which equate to £35,000 per annum.

61. Based on this example the difference in Multiplier would be significant if we look at the comparison between the 2.5% and -0.75% discount rates:

Discount Rate	**Multiplier**	**Capitalised Lump Sum**
2.5%	31.17	£1,090,950
-0.75%	81.75	£2,861,250
Difference		**£1,770,300**

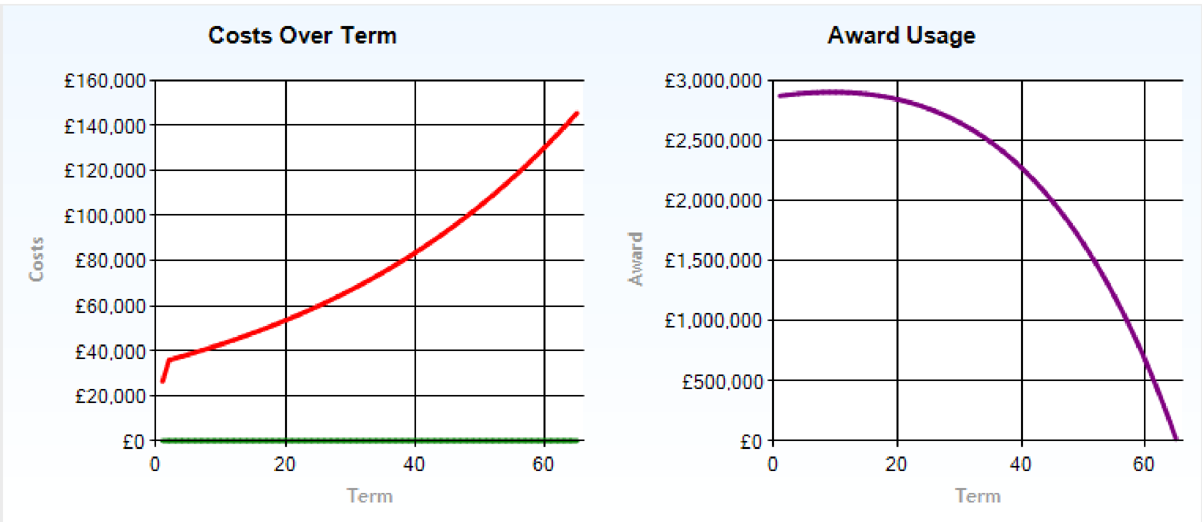
62. If the Claimant does nothing with the money (tax neutral) and spends £35,000.00 per annum which is indexed at the average increase rate for the ASHE 80th Percentile, 2.25%, then the funds are exhausted after 47 years i.e. 18 years early, therefore investment returns are still required and risk necessary to replicate the PPO offering.

63. I have prepared some cash flow modelling to show the returns that would be needed based on an investment of £2,861,250, the capitalised value of care in line with the -0.75% discount rate, and the risk that would be required in order for the funds to last for the remainder of the Claimants lifetime.

64. **Cash Flow Model Example - Inputs**

Client's Current Age	24	Personal Allowance	11,500.00
Expectancy	89		
Lump Sum (leave blank for auto-calc)	2861250		
Target Lump Sum	0	Higher Rate Tax Band	45,000.01
Start Date	26/04/201	Additional Rate Tax Band	150,000.01
Lump Split (Income, Capital) %	40.00	Tax On Basic Rate %	20.0
	60.00	Tax On Higher Rate %	40.0
Growth Rates (Income, Capital) %	2.6	Tax On Additional Rate %	45.00
	2.6	CGT Basic Rate %	18.00
Investment Charges (Income, Capital) %	0.75	CGT Standard Rate %	28.00
	0.75	CGT Exemption	11300

65. **Cash Flow Model Example - Results**



The required term is 65 years. The proposed award will run for a term of 65 years
At the end of the projected term, the remaining balance is: £14,572.14

66. Even with a negative discount rate the Claimant would still need to invest their award and receive an annual return of 2.6% per annum gross of investment charges (1.85% net of investment charges) to meet the cost of his care.

67. The existence of contributory negligence in a case is made more complicated now as the PPO may well prove to be the better option for more future losses than just care and case management. This will mean that there is less available by way of a residual lump sum to meet the shortfall in Care, Case Management and other significant future losses.

SECTION 7 – AN ALTERNATIVE APPROACH

68. **Cash Account Investments**

Cash account deposits do not hold the investment risks associated with a basket of assets which could contain equities or other investments classed as being 'riskier'. However it is currently virtually impossible to obtain and inflation proof return from a cash account.

Current deposit cash interest rate continue to be at an all-time low at circa 1%, Inflation as measured by CPI (Consumer Price Index), soon to be replaced by CPIH, is 1.8% for the 12 months from 1st February 2016 to 1st February 2017.

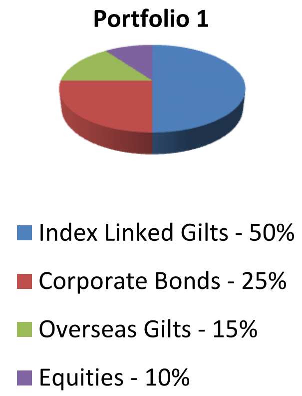
Therefore the risk free rate if the claimant left their award in cash would be -0.8% not factoring income tax into the equation. This is not dissimilar to the current discount rate of -0.75% and would mean that Claimant were receiving a real terms negative return on their investments.

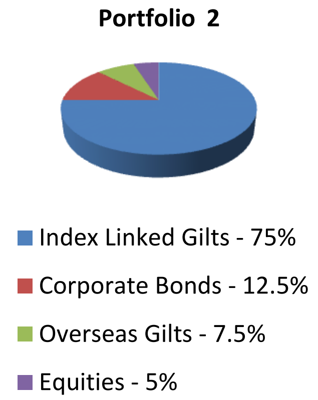
In addition to this, other than National Savings and Investment Accounts, bank accounts are only protected by the Financial Services Compensation Scheme up to a maximum of £75,000 per banking institution this could leave a Claimant who receives a lump sum of £2,000,000 having to search for 27 bank accounts to hold their settlement. It is unlikely that the Claimant would be able to source sufficient interest paying accounts to meet their needs, if the funds are held within a Trust then this would be even more difficult.

69. **Investment in a Low Risk Mixed Basket of Assets**

In previous consultations a discount rate based on alternative investment solutions consisting of different asset classes to be held alongside index linked gilts has been considered.

Choosing the correct mix of assets is difficult but we have based out assessments on the following possible asset mix.





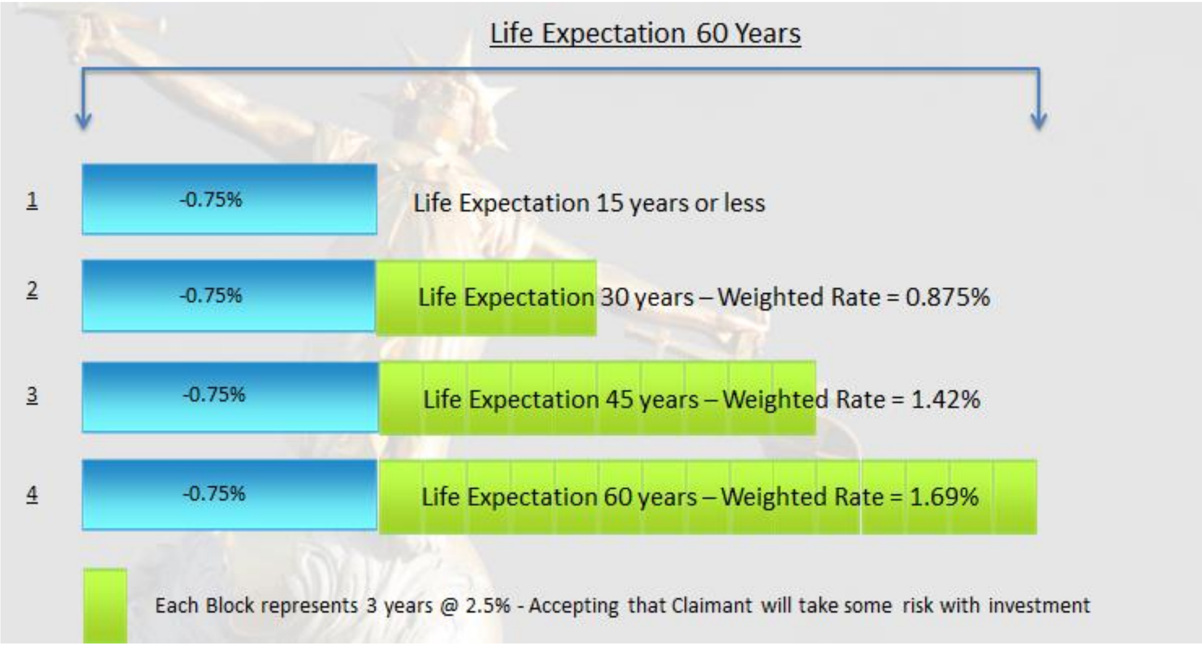
We built a portfolio of assets based on this asset breakdown and back tested them for volatility, the ups and downs of the returns, and performance.

I have looked at the best and worst performing periods for each portfolio over the last 5 years, this demonstrates that investing in a basket of assets I would not be a smooth ride for Claimants and they would have to accept some investment risk.

	Max Gain		Max Loss		Difference	
	Portfolio 01	Portfolio 02	Portfolio 01	Portfolio 02	Portfolio 1	Portfolio 2
April 12-13	4.88	6.31	-1.64	-2.23	6.52	8.54
April 13-14	3.98	2.93	-5.85	-5.89	9.83	8.82
April 14-15	6.29	8.09	-4.2	-5.38	10.49	13.47
April 15-16	3.25	3.89	-2.36	-2.49	5.61	6.38
April 16-17	11.88	13.31	-3.85	-4.71	15.73	18.02

If setting a discount rate based on an alternative basket of assets is deemed to be the preferred method of calculation then this leaves open the question of whether a variable discount rate should be set dependent on a claimant's life expectation. For example a 70 year old claimant with a 15 year life expectancy would not have the capacity to take the same level of risk as a 25 year old claimant with a 65 year life expectancy.

The chart below provides an example of how this may impact on the discount rate for claimants of varying ages with different life expectations:



In real terms this would mean that a claimant with 15 years of less with care costs of £35,000 per annum would have this capitalised accounting for a -0.75% discount rate, yet a claimant with 60 years to live would have the same annual cost of care capitalised accounting for a 1.69% discount rate.

There are some issues with setting the rate on this basis which will need to be agreed upon, namely:

- Whose Life Expectation evidence to apply
- Accepted that risk is now required and therefore there it is essential for claimants to receive professional investment advice this will result in the need to allow a claim for Investment Management Charges within the schedule
  - For example; £1.0m managed for 24 year old until life expectation at age 89, drawn down at a rate of £16k per annum until £0.00 balance would absorb approximately £456,182.00 in investment management fee's.
- 'Eagles v Chambers' simply can't be applicable

- Assessment of the appropriate discount rate on a case by case basis will be complicated and is likely to be subject to challenge in many cases.

70. **Nil discount rate for shorter term losses with longer term losses being paid via a periodical payments or with risk built into solely longer term losses**

Another alternative is to consider payment of short term losses with a nil discount rate and pay all longer term losses either by way of PPO or with some built in assessment of risk to meet longer term needs.

As mentioned earlier in this report PPO's have historically only been considered appropriate in larger value cases, minimum of £500,000 quantum, where there are large ongoing future losses.

I have covered the advantages and disadvantages of PPOs in section 5 of this report and they should be considered when assessing whether a PPO would be appropriate for future losses.

There will be issues where a claimant has accommodation needs as where longer term losses are met by a PPO there will not be sufficient residual lump sums available to meet these needs.

The solution may well lie in the Jurisprudence of 'George v Pinnock'

- In GEORGE v. PINNOCK, Orr LJ held that there was no difference between the loss of income on capital tied up in the property and the "annual mortgage interest which would have been payable if capital to buy the bungalow had not been available".
- In ROBERTS v. JOHNSTONE, the Court of Appeal's task was to determine the appropriate rate for a GEORGE v. PINNOCK calculation.

A mortgage on the required property could be a solution however it would be virtually impossible for a Claimant to secure a mortgage on a 'Interest Only' basis, particularly where you have protected parties and they have their property and affairs managed by a Trust Corporation?

Could a solution be that the Defendants purchase the property for the benefit of the claimant and have a Discretionary Will Trust drafted to return the asset to them on the death of the individual? This would clearly be unfeasible for a number of reasons for both Claimants and Defendants.

SECTION 8 – SUMMARY AND CONCLUSION

71. It is difficult to assess, under the current financial and economic climate the best long term solution to value damages in the most fair and adequate way. It would seem that the alternatives will require some further research and quantification and it is likely that an expert witness will need to be appointed to provide advice and guidance as to the correct assumptions and calculations required to provide the appropriate method of quantifying a claim.

72. In my opinion it is difficult to advise as to the correct solution as many have previously attempted and ultimately failed to find a suitable alternative. This has been well documented by the MoJ through their consultations conducted in 2012 and 2013.

73. Clearly the Lord Chancellor created a wave of uncertainty as no-one was expecting the discount rate to be cut to the now -0.75% position that is now in situ.

74. I have seen many articles and advisor's comments about whether the Lord Chancellor went too far in reducing the rate to a negative position but we must be mindful of the current law. The Lord Chancellor effectively had her hands tied as the method for calculating the discount rate has not changed since Lord Irving adjusted it to 2.5% in 2001. Based on current methodology, the rate should be lower than the -0.75% currently set if the yield on all index linked gilts had been used in the calculation.

75. The major problem in my opinion is that the methodology that is assumed to provide a risk-free environment for the claimant to invest their damages is predicated on an investment solution that simply cannot be enacted once settlement is reached.

76. On the current methodology, the rate of 2.5% has clearly been too high for a long period of time, particularly given that when the first announcement to review the discount rate by Tsol in 2010 the equivalent discount rate, based on ILGS was already as low as 0.75%.

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77. I have demonstrated above that even in larger loss cases where Periodical Payments might be more prevalent, the Claimant, if choosing to take the capitalised lump sum , must take an investment risk to replicate the income that would be received from the PPO over their given lifetime.

78. The most appropriate question might be “Is there such a thing in today’s market as a risk-free investment” with the only answer to that question simply being “no”.

79. An investment purely into cash carries with it several risks, the most dramatic being “systemic risk” i.e. what would the individual do if the institution holding those funds failed and only £75,000 of that pot was protected?

80. The implication of introducing alternative methods of evaluating an appropriate discount rate, including the possibility of a blend of investment products/basket of products presents its own unique set of additional questions and problems discussed above.

………………………………….

Mark Holt MLIBF DipFA
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Appendix A

CURRICULUM VITAE

MARK S. HOLT

Education

1987 – 1992	Standish Community High School
1992 – 1994	Winstanley College of Technology
1994 – 1996	University of Central Lancashire

Grades and Qualifications

4 A-Levels (Including Maths, Further Maths & Economics)

Financial Planning Certificate FPC Paper 1

Certificate for Financial Advisors CeFA papers 2 & 3

CeMAP Fully Qualified

Investment Advice Certificate Papers 1 & 2

Diploma for Financial Advisors (QCA Level 4)

'Statement of Professional Standing' issued by (London Institute of Banking & Finance) LIBF

Employment Details

2016 – Date	Frenkel Topping Group Plc	Commercial Director
2016 – Date	Frenkel Topping ltd	Commercial Director
2013 – 2015	Frenkel Topping ltd	Senior Consultant/Head of Litigation Support
2011 – 2013	Frenkel Topping ltd	Senior Consultant
2008 – 2011	Sterling Holt Limited	Managing Director

2004 – 2008	Avertis Risk Solutions	Business Consultant
2002 – 2004	Newleaf Limited	Director of Financial Services
2000 – 2002	JGFS	Financial Advisor
1998 – 2000	Barclays Life Assurance	Financial Advisor
1996 – 1998	Nelson Money Managers	Financial Support

Relevant Experience

- 20 Years qualified experience providing Financial Advice to retail, personal injury, clinical negligence and corporate clients.
- I have prepared in excess of 450 Claimant Reports and Joint Statements for the Court, on the value of the loss of retirement benefits within personal injury and clinical negligence claims.
- Highly experienced in evaluating the suitability of the use of Periodical Payments in the structuring of awards.
- Regularly provide training to Barristers and Solicitors alike on the methodology and merits of Periodical Payment Orders.
- Personally involved in advising claimants at settlement in numerous cases, well in excess of £550m total quantum.
- Instrumental in the design and implementation of Frenkel Topping training seminars to Counsel & Solicitors including “Complex Claims and Periodical Payments” 2016, The Implications of the Discount Rate 2017.
- Regular guest lecturer to AvMa, APIL, MASS, NABIF and SIA.