DEPARTMENT FOR WORK AND PENSIONS

REVIEW OF EMPLOYERS' LIABILITY COMPULSORY INSURANCE

A RESPONSE BY THE ASSOCIATION OF PERSONAL INJURY LAWYERS

FEBRUARY 2003

The Association of Personal Injury Lawyers (APIL) was formed in 1990 by claimant lawyers with a view to representing the interests of personal injury victims. APIL currently has over 5300 members in the UK and abroad. Membership comprises solicitors, barristers, legal executives and academics whose interest in personal injury work is predominantly on behalf of injured claimants. APIL does not generate business on behalf of its members.

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EXECUTIVE SUMMARY

Employers' liability compulsory insurance has clearly been a huge issue in the last year and has been discussed widely by insurers, brokers, employers and both claimant and defendant lawyers.

Injured workers, or those suffering from ill health, must not suffer as a result of this review. They have a right, at common law, to be fully compensated where their employers have acted negligently or in breach of statutory duty and this right must not be removed or limited.

Independent analysis of the personal injury claims market has revealed that the number of claims is unlikely to increase, as suggested by the insurance industry. No win-no fee agreements have not led to an explosion of personal injury claims. Nor is compensation spiralling out of control. Compensation awards are actually lower than the Law Commission believes they should be.

In this paper, APIL states that the system of employers' liability insurance is sustainable if:

- Insurers react to personal injury claims promptly and thoroughly and comply with the mechanisms in place, such as the pre-action protocol, to reduce legal costs;
- Injured workers receive timely and appropriate rehabilitation;
- Insurers change their approach to the sale of employers' liability insurance;
- Insurers link employers' liability premiums to the health and safety performance of employers by referring to a list of relevant considerations.

To reform the system of employers' liability insurance before seeking to tackle problems relating to:

- insurers' claims management;
- low rates of rehabilitation;
- insurers' approach to the sale of employers' liability insurance;
- the poor health and safety performance of employers;

would be both inequitable and unpopular. In the interests of injured workers, all those with an interest in this issue must work together to make the current system work. A complete overhaul of the system would be an unnecessary and short-sighted attempt to deal with the symptoms rather than the causes of the current problems.

REVIEW OF EMPLOYERS' LIABILITY COMPULSORY INSURANCE

Introduction

Many are concerned that there are underlying and long-term difficulties with the way in which the system of compulsory insurance for employers' liability (ELCI) operates in the UK. Whilst APIL believes that some change is necessary, it does not believe that either the system of employers liability, or the system of compulsory insurance that supports it, is in need of radical reform. Subject to some adjustments, the system of ELCI is sustainable both in the short and the long term. A complete overhaul of the system would be an unnecessary and short-sighted attempt to deal with the symptoms rather than the causes of the current problems.

The Importance of the Employers Liability System

The current fault-based system of employers' liability and the common law entitlement to full compensation must be retained. Both play an important role in our society. The fault based system satisfies society's justifiable expectations that careless employers will be held accountable for their actions. It also seeks to deter negligent or unlawful behaviour – if employers are not held responsible for their actions, no incentive exists to ensure that they seek to protect the health and safety of their workforce. In addition, at common law, injured workers are entitled to full compensation to put them in the position they would have been in had the negligence or breach of statutory duty not occurred. Compensation is not, therefore, awarded as a bonus but is awarded to ensure that the injured person does not have to incur losses or expenses due to his employer's careless behaviour.

Insurance is, of course, necessary to support the system of employers' liability. It ensures that compensation can be paid where claims are successfully pursued. For this reason, any potential problems with the system must be taken seriously and addressed.

Unfortunately, it is extremely difficult to gauge the extent of any problems being experienced in relation to ELCI. It seems that not even the insurance industry can agree internally on this and APIL will be extremely interested to see the results of the OFT's review of this matter. On 6th February, APIL posted a notice on its website inviting APIL members to notify the association of claims where the potentially responsible employer was uninsured. The website receives approximately 500 hits a week but only one member has responded, stating that he was aware of three such cases. In summary, we do not believe that there are sufficient problems with ELCI to lead to:

- A restriction in the circumstances in which injured employees can recover compensation; or

- A restriction in the amount of compensation employees can recover where they can establish negligence or a breach of statutory duty.

The Alleged Problems With ELCI

The sustainability of ELCI will depend on a number of factors, including the number of employers liability claims pursued, the amount of compensation paid in each claim, the administration or legal costs involved in delivering that compensation and the extent to which the insurance industry can meet those costs. Many reasons are being advanced for the reputed unsustainability of ELCI, as follows:

- The development of a 'compensation culture';
- Increasing legal costs;
- Increasing levels of compensation;
- Difficulties relating to disease claims;
- The insurers' approach to the ELCI market.

The Alleged Development of a Compensation Culture

The sustainability of ELCI will, in part, depend on the number of employers' liability claims being pursued and in considering this, the insurance industry often refers to the crippling effect of the 'compensation culture'. APIL submits that there is little evidence of a 'compensation culture' and does not believe that the number of claims likely to be pursued in the future would make the system unsustainable. Datamonitor, an independent market analyst, recently considered the extent to which a 'compensation culture' existed in the UK. Its report entitled "UK Personal Injury Litigation 2002 – The Compensation Culture Myth Exploded", published in 2002, is attached for further information at annex A. After a thorough analysis of this issue, Datamonitor concluded that "the much-feared compensation culture will not really develop much further".

Between April 2001 and March 2002, 688,691 claims were made to insurers, 24.8 per cent of which were employers' liability claims. This represented a decrease of 7.4 per cent on the 743,593 claims registered the previous year. Datamonitor found that this decrease was largely due to a steep decline in disease claims, dropping from 123,814 in 2000-2001 to 74,408 claims in 2001-2002 – a fall of 39.9 per cent. In looking at the number of potential employers liability claims, Datamonitor predicted that 67.2 per cent of potential workplace injury claims are not being pursued. This picture certainly does not seem to accord with consistent claims of a 'compensation culture'. It does, however, reflect poorly on the extent to which employers are complying with health and safety legislation and this is addressed in more detail below.

In predicting what would happen in the future, Datamonitor concluded that "[t]he UK is unlikely to reach the same levels of compensation numbers and awards as the US." This, it explained, was due to the following factors:

- The UK does not have a similar provision of lawyers or culture of legal representation;
- There is no need to pay for healthcare since the NHS is a free service, meaning that claimants are not worried about funding their return to health;

- The prospect of multi-million pound damages are some way off in the UK, with many awards being capped and average payouts being substantially less than those in the US.

It estimated that claims numbers would grow by an annual average of just 0.4 per cent to reach a total of 627,081 claims in 2007 (excluding disease claims). This would represent a total increase of only 2.1 per cent between 2001 and 2007. Datamonitor concluded that the "compensation culture has reached its peak and thus there is not much left to be squeezed out of the market." As far as APIL is aware, Datamonitor is the only independent analyst to have considered the future of the personal injury market and we submit that its conclusions on the issue of 'compensation culture' are extremely persuasive.

It is also alleged that the introduction of conditional fee agreements, outlined in more detail below, has made it easier for injured people to claim compensation. APIL disputes this. Conditional fee agreements require solicitors to take the financial risk of losing cases and must, therefore, be careful about the cases they take on a conditional fee basis. In short, under the conditional fee system, lawyers are unable to support weak personal injury claims.

The Alleged Increase in Legal Costs

According to the ABI, legal fees account for 40 per cent of the costs of claims. APIL cannot verify this figure, which seems to have been extracted from insurance sources informally. Independent analysis of legal costs in employers liability claims since recent funding and procedural reforms is now beginning to emerge. **Professor Paul Fenn of the University of Nottingham has recently looked into this issue on behalf of the Civil Justice Council, although his research has not yet been published. It is also believed that the Lord Chancellor's Department has recently commissioned research into legal costs and so this research is still in its early stages.**

It is true, however, that legal costs to be paid by insurers in their lost cases have increased in recent years. This is not due, however, to 'greedy' lawyers or a 'compensation culture' but to the Government's introduction of new funding arrangements in 1999. Before 1999, most personal injury cases were funded by legal aid. In 1999, the Government removed legal aid for personal injury cases and introduced conditional fee agreements as the alternative funding mechanism. These are often referred to as 'no win-no fee' agreements.

Under a conditional fee agreement, if an injured victim loses his case, he does not have to pay his own lawyers for the work they have done. The victim does, however, become liable for the costs of the winning defendant. To protect himself against such an adverse costs order, the victim takes out an after-the-event insurance policy. If the victim wins his case, he can recover his lawyer's costs from the losing defendant or, rather, the defendant's insurers. This will include not only the lawyer's actual costs, but also what is known as a "success fee". Conditional fee agreements require solicitors to take on the financial risks of losing cases, as they do not recover any costs at all in cases they lose. Losing a case can be extremely expensive for even the largest of lawyers' firms and to reflect this, lawyers are entitled to recover a success fee in winning cases. Recovering success fees in the winning cases allow lawyers to absorb the costs of losing cases.

The new system means that, in the losing cases, insurance companies have to pay not only the actual legal costs, but also the claimant lawyer's success fee and the premium for the after the event insurance policy. Success fees and ATE premiums are recoverable because the Government decided that a claimant, injured through no fault of his own, should not have to bear the costs associated with the new funding system. The Government introduced conditional fee agreements to increase access to justice for a greater proportion of the population. It would be extremely regrettable if this policy led, in the long term, to a restriction in the ability of injured victims to achieve access to justice by restricting either the circumstances in which an injured victim would be able to recover compensation or the amount of compensation he could recover.

Costs are, however, an inevitable part of any system of compensation. In the 1990s, Lord Woolf reviewed, amongst other things, the procedures for pursuing personal injury claims. He found that the civil justice system was cumbersome, complex and expensive and new civil procedure rules were introduced as a result in April 1999. The new rules introduced the principle of proportionality. This means that the costs incurred in any one case should be proportionate to its complexity and overall value. This principle is enforced by the courts through judicial case management. Lord Woolf also introduced pre-action protocols, which seek to reduce costs by encouraging early settlement of cases, thereby reducing the number of costly trials. The Lord Chancellor's Department conducts a continuing evaluation of the new civil procedure rules and published its last evaluation in August 2002. It concluded that whilst the civil procedure rules were generally working well, it was too early to make a definitive assessment on the issue of legal costs, stating that "the picture is still relatively unclear with statistics difficult to obtain and conflicting anecdotal evidence".

It is unfair for the insurance industry to question the existence and operation of ELCI on the basis of legal costs, when anecdotal evidence suggests that they routinely fail to comply with the mechanisms in place, such as the pre-action protocol, to reduce legal costs. In seeking to maintain the sustainability of ELCI, all stakeholders, including the insurance industry, must approach claims efficiently, cost effectively and fairly. This must start with compliance with the pre-action protocol for personal injury cases, which is likely to lead to an overall reduction in costs.

Extra legal costs are also incurred because the legal system generally requires an injured worker to be compensated in a lump sum. This means that lawyers and the courts must consider an injured worker's life expectancy. The Government is currently in the process of introducing 'periodical payments' which will remove this argument and is likely, therefore, to lead to cost savings for the insurance industry in this respect. In the debate on the sustainability of ELCI, insurers have asserted that the introduction of periodical payments will make employer's liability claims even more expensive. This is not

reflected, however, in the Government's regulatory impact assessment of the matter. The Lord Chancellor's Department has stated:

> "General insurers would achieve savings of around 4% by purchasing annuities compared to paying a lump sum, subject to changes in annuity rates. "Taking our mid range estimates of the total annual value of lump sum awards likely to convert to periodical payments, this suggests an overall annual reduction in the liabilities of insurers in the order of £17 million, of which £14 million relates to claims against motor policies and £3 million to claims against liability policies. These figures need to be viewed against the estimated £10 billion paid in liability insurance premiums in 2000. However, given the uncertainties involved in this calculation the safest conclusion to draw may be that these proposals will not materially increase the value of claims against liability insurers."

The Alleged Increase in Damages

The sustainability of the system does depend, in part, on the amount of compensation awarded in any one case. Compensation is not awarded as a bonus but is meticulously calculated to reflect the actual losses, expenses, pain and suffering incurred by the injured worker. The principle behind compensation is that, so far as possible, the injured worker should be put into the position they would have been in had the negligence or breach of statutory duty not occurred. Compensation comprises three elements:

- Damages for past financial losses and expenses;
- Damages for future financial losses and expenses;
- Damages for pain, suffering and loss of amenity.

In assessing the claimant's losses and expenses, lawyers, with the assistance of expert witnesses, must carefully compare the financial position the claimant would have in before the negligent conduct, with his position after its occurrence. Damages for pain,

suffering and loss of amenity are awarded in accordance with the Judicial Studies Board guidelines.

Insurers are claiming that damages have increased in recent years and that this is having an impact on the sustainability of ELCI. While APIL agrees that damages have increased marginally, it must be recognised that recent increases in damages for pain, suffering and loss of amenity represent only a small proportion of the increases recommended by the Law Commission. The Law Commission's recommendations, which were issued in 1999, are attached for further information at annex B.

The Law Commission's recommendations were considered by the Court of Appeal in Heil v Rankin (2000). A transcript of the judgment is attached at annex C. In 1999, the Law Commission reported that damages for pain, suffering and loss of amenity should be increased. For injuries where the current award for non-pecuniary loss would be over £3,000, the recommendation was for an increase by a factor of at least 1.5 (i.e. 50 per cent) but by not more than a factor of 2 (i.e. 100 per cent). The Law Commission based its recommendations on the views of consultees responding to its consultation paper, and particularly, the results of empirical research to ascertain the views of people generally, conducted for the Law Commission by the Office for National Statistics. The Law Commission recommended that the proposed increases would be best achieved by the higher courts exercising their powers to issue guidelines in a case or series of cases. If the courts did not increase the awards in accordance with the Law Commission's recommendations within a reasonable period, it further recommended that legislation should be enacted to achieve this. The Court of Appeal did not follow the Law Commission's recommendations and only applied limited increases to damages for pain suffering and loss of amenity. Nor does it appear that the Government intends to legislate in accordance with the Law Commission's recommendation. Whilst damages have increased, therefore, they have not increased as much as recommended by the Law Commission or in accordance with public opinion. As a result many negligently injured people still do not receive the level of compensation needed to return them to the position they were in before being injured.

In addition, insurers often refer to the impact of the discount rate on damages. The discount rate is a deduction made from the compensation awarded for future financial losses and expenses on the basis that the successful claimant will invest their damages award and increase the value of the original sum. On 27 June 2001, the Lord Chancellor exercised his power under section 1 of the Damages Act 1996 to prescribe the discount rate. He set the rate at 2.5 per cent. Previously the rate generally used by the courts was 3 per cent.

The Potential Impact of Rehabilitation

APIL supports rehabilitation, which seeks to restore an injured person to as productive and as independent lifestyle as possible through the use of medical, functional and vocational interventions. APIL was involved in drafting the Code of Best Practice on Rehabilitation for personal injury claims which seeks to encourage claimant and defendant lawyers to liaise with each other to secure rehabilitation for injured claimants. A copy of the code is attached at annex D. Rehabilitation is, however, not only an advantage for claimants. If a claimant is successfully rehabilitated, he is likely to be able to live more independently and have an increased chance of securing employment. This would mean that the defendant, or rather his insurer, would have to pay less in compensation. The increased use of rehabilitation in the context of personal injury claims would, therefore, have a positive impact on the sustainability of ELCI.

Rehabilitation, however, should not only be considered within the context of litigation. APIL believes that employers should be under a legal duty to consider the use of rehabilitation. In short, rehabilitation should be an integral part of an employer's health and safety strategy and, more specifically, it should be mandatory for employers to have a rehabilitation policy. In addition, rehabilitation services within the NHS appear to be available, organized and financed on an ad hoc basis. APIL calls for rehabilitation to become the priority it should be within the healthcare and social support system.

Alleged Difficulties Relating to Disease Claims

Insurers often point to the difficulties they experience in relation to disease claims, noting that long latency periods make diseases a difficult risk to insure. The latest HSE estimates reveal that mesothelioma deaths are expected to peak in 2011 at 1,700 deaths per year and insurers undoubtedly need to prepare themselves. Insurers are not expected, however, to pay compensation for diseases which may not even be known about when the insurance is taken out. In law, a disease claim will only succeed where it can be shown that, at the time harm was caused, the employer knew, or ought to have known, that harm was, in fact, likely. The law does not expect an employer, or an insurer, to gaze into a crystal ball. The fact is, that the two types of disease claim which have had the greatest impact on ELCI in recent years are asbestos-related disease and noise-induced deafness and the dangers of both have been well-known for decades. As long ago as the 1950s, it was established that there was an obligation on employers to keep themselves abreast of health and safety developments. They should know, for example, that HM Factory Inspectorate (as was) reported the dangers of asbestos as long ago as the 1930s, and in 1963 it explained the dangers of exposing workers to loud noise. If employers had responded positively to these warnings, they would have dramatically reduced future claims. For example, a recent court case highlighted the risk of dermatitis to workers who wear latex gloves. Any responsible employer who wishes to avoid illnesses in the workforce and compensation claims for dermatitis linked to latex gloves simply has to remove the latex gloves. The logic is simple.

The Insurers' Approach to the ELCI market

It is now widely acknowledged that ELCI has been mismanaged by the insurance industry for years, since it was sold as a loss leader when it first became compulsory in the 1970s. Any shortfall was offset by the then-buoyant stock market. That market has now hardened and many insurers are being forced to inflate premiums to cover losses. In looking at the sale of ELCI, Datamonitor found:

"It has traditionally been more difficult to push through rate rises in the commercial sector, since each individual account is worth so much to an insurer. A key factor that affects the performance of the general liability market is that most underwriters do not sell liability as a stand-alone product – rather it is offered as part of a package alongside property and motor cover. Insurers have been wary of pushing up employers' liability premiums to a sufficiently profitable degree in case it results in loss of the account altogether. Furthermore, competition to retain market share in the commercial motor and property markets has led to the neglect of employers' liability and a continued softening of rates."

It concluded:

"The declining size of the total general liability market in terms of premium income continued in 2000, dropping 4.8% to a value of £2.5 billion. Following an improvement in the underwriting result in 1999, general liability began to worsen once again. If insurers could steel themselves and gently push through liability rate rises, they might be able to achieve what the motor insurance industry itself has done. By acting as a unit, insurers could jointly force the market upwards, thus improving their underwriting position further."

APIL believes that the insurance industry should at least try to rectify their approach to the sale of ELCI. It would be totally inequitable, and unpopular with the public, if the circumstances in which compensation can be recovered and/or the amount of compensation that can be recovered were limited because of the insurance industry's

historical approach to the ELCI market. Means of improving the ELCI system by tailoring premiums to health and safety performance are outlined below.

Alternatives to a fault-based system

We have already explained the importance of having a fault based system of employers liability. Some, however, argue for the introduction of a no-fault compensation scheme for either all occupational health claims or for disease claims only. We admit that initially such a scheme looks very attractive. It would appear to allow for compensation to be paid to an increased number of injured workers. Further analysis of such a scheme, however, highlights its deficiencies in practice and demonstrates that the term "no-fault compensation" is misleading. Such a scheme would not truly operate on the basis of "no fault" as does our social security system, as causation would still have to be established. Nor would the monetary awards through such a scheme be compensatory in the sense of being restitutionary as under the common law.

Whilst the administrative costs per claim could probably be reduced through a no-fault scheme, more people would qualify for compensation and so it would become more expensive. The prohibitive costs of a no-fault scheme were discovered in New Zealand where the scheme was made affordable by firstly, restricting access to the scheme and secondly, reducing the amount of compensation available to those claimants who were able to access the scheme. Neither of these moves would be popular with the public.

Ensuring the Sustainability of ELCI

In considering the sustainability of the employers' liability system, and ELCI which supports it, we have noted that:

- the number of claims is unlikely to increase significantly in recent years as suggested by the insurance industry;
- thorough, prompt and appropriate claims management as envisaged in the civil procedure rules can lead to reduced legal costs;
- the increased provision of rehabilitation could lead to a reduction in the amount of compensation paid in each case.

The most important factor in considering the sustainability of the current system is the 'risk' insured. Poor health and safety performance leads to an increased number of injuries, which can, in turn, lead to an increased number of claims and so on. Minimising the risks of injury, ill health or fatality to the workforce must be the key to the sustainability of ELCI and the employer's liability system. Responsibility for the enforcement of health and safety legislation falls to the Health and Safety Executive.

APIL calls for ELCI premiums to reflect the health and safety performance of the insured more closely. This would require the ELCI market to operate similarly to the motor insurance market. Good health and safety performance should attract lower premiums. This would satisfy employers who are currently concerned that their ELCI premiums are extremely high, despite a good health and safety record. It would also, however, act as an economic incentive for employers to comply with health and safety legislation. If this legislation is complied with, fewer accidents will occur and fewer claims will be made. Insurers often suggest that it would be too difficult to tailor the level of ELCI premiums to an employer's health and safety performance. As the Department for Work and Pensions is aware, however, the Health and Safety Executive is looking into the development of a list of considerations for insurers when setting the premium. A central register with information on any and all enforcement action taken by the HSE would also help insurers to assess the correct level of premium.

Conclusion

In conclusion, APIL submits that the ELCI system will be sustainable if:

- Insurers improve their approach to claims management;
- The provision of rehabilitation is increased;
- Insurers take a different approach to the sale of ELCI;
- Employers' health and safety performance improves;
- ELCI premiums are linked to an employers' health and safety performance.

It would be unfair to limit the compensation of injured workers because of a hardening of the market and the insurers' approach to date. A complete overhaul of the system is unnecessary and would be a short-sighted attempt to deal with the symptoms rather than the causes of current problems.