

## Major UK Government Proposals on Reform of Litigation Costs and Funding

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In November 2010 the UK government issued two important consultation papers as a prelude to introducing major legislative reforms in the funding and costs of litigation. In accordance with the government's overriding policy of reducing public expenditure, it proposes to take a further major step in deconstructing legal aid. Instead, it adopts two policies. First, people are to be encouraged to resolve disputes through alternative dispute resolution mechanisms – the full details of this are not yet available. Secondly, all available means of private funding for claims within the court system are to be encouraged, ranging from legal expenses insurance (LEI) to contingency fees (known as damages-based agreements) and third party funding. The experiment with conditional fee agreements (CFAs) and associated after-the-event (ATE) insurance is to be curtailed, implementing the recommendations of Lord Justice Jackson that CFA success fees and ATE premiums are no longer to be recoverable from opponents. Many other Jackson proposals are to be implemented, notably qualified one way cost shifting (QOCS) for personal injury and various other types of claims, under which claimants would not have to pay opponents' costs unless they had appreciable assets or behaved badly in the litigation process.

The two consultations are on proposals for reform of legal aid,<sup>1</sup> and on implementation of Lord Justice Jackson's ('Jackson') recommendations.<sup>2</sup> An associated Report to the Prime Minister was published on 15 October 2010 by Lord Young of Graffham, primarily concerning reducing burdens on business of health and safety law, but containing a strong attack on a perceived 'compensation culture' and supporting the Jackson recommendations.<sup>3</sup> The government announced that it is also working on a wider reform of the legal system, which will emphasise ADR: details are to be published in 2011.

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<sup>1</sup> *Consultation paper, Proposals for Reform of Legal Aid in England and Wales*, November 2010, available at: <http://www.justice.gov.uk/consultations/legal-aid-reform-151110.htm>

<sup>2</sup> *Proposals for Reform of Civil Litigation Funding and Costs in England and Wales. Implementation of Lord Justice Jackson's Recommendations*, Ministry of Justice, Consultation Paper CP 13/10, November 2010, available at <http://www.justice.gov.uk/consultations/docs/jackson-consultation-paper.pdf>

<sup>3</sup> *Common Sense, Common Safety. A report by Lord Young of Graffham to the Prime Minister following a Whitehall-wide review of the operation of health and safety laws and the growth of the compensation culture*, (HM Government, 2010), available at [http://www.number10.gov.uk/wp-content/uploads/402906\\_CommonSense\\_acc.pdf](http://www.number10.gov.uk/wp-content/uploads/402906_CommonSense_acc.pdf). Lord Young resigned as the Prime Minister's advisor of business on 19 November 2010.

## A. Funding of Litigation

### Restricting legal aid and encouraging ADR

The Legal Aid Consultation starts from the premise that legal aid is no longer a sustainable public expenditure programme in the current economic climate,<sup>4</sup> and that deep cuts need to be made. However, the Minister of Justice's Foreword notes not just a very large shift away from public funding of litigation<sup>5</sup> towards development of various types of private funding, but also a significant shift in emphasis towards ADR:

'I believe that this has encouraged people to bring their problems before the courts too readily, even sometimes when the courts are not well placed to provide the best solutions. This has led to the availability of taxpayer funding for unnecessary litigation. There is a compelling case for going back to first principles in reforming legal aid. ...

To continue like this is unsustainable, and I want to use these lessons as an opportunity for fundamental reform of the scheme. I want to discourage people from resorting to lawyers whenever they face a problem, and instead encourage them, wherever it is sensible to do so, to consider alternative methods of dispute resolution which may be more effective and suitable. I want to reserve taxpayer funding of legal advice and representation for serious issues which have sufficient priority to justify the use of public funds, subject to people's means and the merits of the case.'

The objective is:

'These proposals complement the wider programme of reform to move towards a simpler justice system: one which is more responsive to public needs, which allows people to resolve their issues out of court without recourse to public funds, using simpler, more informal, remedies where they are appropriate, and which encourages more efficient resolution of contested cases where necessary. But these legal aid proposals are not dependent on the implementation of those wider reforms.'<sup>6</sup>

The government states that 'to help establish the right balance' it has been guided by various considerations, beginning with:

'the desire to stop the encroachment of unnecessary litigation into society by encouraging people to take greater personal responsibility for their problems, and to take advantage of alternative sources of help, advice or routes to resolution'<sup>7</sup>

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<sup>4</sup> The Ministry of Justice's target is a real reduction of 23% in its budget, worth nearly £2bn in 2012-15. Legal Aid Consultation, para 1.3.

<sup>5</sup> For many years, surveys have shown that the UK paid considerably more per capita in legal aid than any other EU state.

<sup>6</sup> Legal Aid Consultation, para 1.5.

<sup>7</sup> Legal Aid Consultation, para 2.11.

## **Legal aid reform**

Many of the proposals concern criminal and family legal aid and other issues, and are not referred to here. The detailed proposals on civil legal aid are also not summarised: they broadly concern limiting scope,<sup>8</sup> eligibility<sup>9</sup> and remuneration of lawyers.<sup>10</sup>

Legal aid is to be restricted in scope to those cases where the litigant is at risk of very serious consequences. Such restrictions are based on various factors:<sup>11</sup>

- the objective importance of the issue, taking into account the matters at stake;
- the litigant's ability to present their own case;
- the availability of alternative sources of funding; and
- the availability of other routes to resolution, and the advice and assistance available to individuals to help them achieve a resolution, including the extent to which the individual could be expected to work at resolving the issue themselves.

A significant reform is that disputes involving consumer law, breach of contract and tort claims are not considered to be of sufficient priority to justify publicly funded support.<sup>12</sup> The government notes the availability of alternative, non-court-based routes to resolution, such as the Financial Ombudsman's Service (for financial disputes) or OTELO for complaints relating to telecommunications. CFAs will also often be available for cases involving damages. Legal aid will be refused for any individual case which is suitable for an alternative source of funding, such as a CFA. This would apply to all civil cases other than family cases.<sup>13</sup>

## **Diversity of litigation funding: SLAS, TPF and contingency fees**

The government proposes to raise fees from two sources in addition to general taxation:<sup>14</sup>

- securing the interest generated by monies that solicitors hold on behalf of clients in general client accounts, and
- a Supplementary Legal Aid Scheme (SLAS) in which a percentage of funds are recouped from cases where successful claims for damages have been made and the claimant was in receipt of legal aid, and uses those funds to supplement the legal aid costs of other cases. However, the government does not indicate whether the initial funding that would be required would be from public or private sources. It does propose that the percentage collected should only come from general and not special damages.

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<sup>8</sup> Legal Aid Consultation, ch 4.

<sup>9</sup> Legal Aid Consultation, ch 5.

<sup>10</sup> Legal Aid Consultation, chs 6 and 7. All fees paid for civil work will be reduced by 10%.

<sup>11</sup> Legal Aid Consultation, paras 4.13-4.29.

<sup>12</sup> Legal Aid Consultation, paras 2.28, 4.171 and 4.243.

<sup>13</sup> Legal Aid Consultation, para 4.265.

<sup>14</sup> Legal Aid Consultation, ch 9.

In relation to civil litigation, Jackson considered that litigants should have the choice of as many funding methods as possible and the freedom to choose the one that they believe is most appropriate for their case.<sup>15</sup> That policy of diversity is pursued in the government's proposals on supporting legal expenses insurance (LEI), Third part funding (TPF) and contingency fees (DBAs):

- The government supports the recommendations of Jackson and Lord Young that before-the-event (BTE) LEI should be encouraged, especially for housing and employment cases.<sup>16</sup>
- A voluntary code has been drawn up for providers of TPF, on which consultation closes on 3 December 2010.<sup>17</sup>

### **Damages based agreements**

A damages-based agreement (DBA) is the UK statutory term for a regulated contingency fee.<sup>18</sup> These have historically been permitted in employment cases. They are similar to existing CFAs (see below) in permitting a regulated success fee, but different in that the success element is calculated by reference to the damages awarded. The government proposes to permit DBAs in general litigation.<sup>19</sup>

Jackson rejected the argument that DBAs create a greater threat of conflict of interest between lawyers and their clients than CFAs.<sup>20</sup> He recommended that DBAs

‘Under the regulations governing DBAs in the Employment Tribunal, the maximum percentage of damages that a representative may take as a fee is 35% (including VAT). In respect of CFAs, Sir Rupert proposes that in personal injury claims the maximum percentage of damages, excluding damages awarded for future care or losses, which can be payable as a success fee should be 25%. Sir Rupert says that the cap on deductions should be the same for DBAs. He recommends that no contingency fee deducted from damages under a DBA should exceed 25% of claimant's damages, excluding damages referable to future care or losses.’<sup>21</sup>

‘Sir Rupert believes that solicitors should be entitled to charge a higher percentage fee under a DBA than they otherwise would if they accept the risk of liability for their client's adverse costs in the event that the case is lost. He also believes that solicitors should be entitled to a higher percentage fee if they fund the client's disbursements. If either is funded by the client the solicitor should be entitled to a lower percentage fee. The disbursements in DBAs could include counsel's fees, or counsel could be allowed to act under a DBA and be entitled to a specified percentage of any sums recovered. If the latter is the case this must be clearly set out in the DBA itself.’<sup>22</sup>

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<sup>15</sup> Jackson Consultation, para 225.

<sup>16</sup> Jackson Consultation, para 265-267; Legal Aid Consultation, para 9.42.

<sup>17</sup> Jackson Consultation, para 270.

<sup>18</sup> 58AA of the Courts and Legal Services Act 1990, as amended by section 154 of the Coroners and Justice Act 2009.

<sup>19</sup> Jackson Consultation, para

<sup>20</sup> Jackson Consultation, para 228.

<sup>21</sup> Jackson Consultation, para 232.

<sup>22</sup> Jackson Consultation, para 233.

Costs would be recovered from the opponent on a conventional basis, as on the Ontario model. Any excess over the sum recoverable on a normal hourly rate basis would be paid by the client.<sup>23</sup>

The government does not consider that a new approach towards regulation of DBAs is necessary:

‘... in principle there would be little difference between CFAs (as reformed) and DBAs if introduced on the basis proposed by Sir Rupert. The Government is therefore not convinced that, aside from a cap on damages in personal injury cases (as with CFAs), separate detailed regulation of DBAs would be necessary and that the existing requirements in the professional rules of conduct for solicitors, for example, could be extended to cover the use of DBAs in litigation.’<sup>24</sup>

## **B. Implementing the Jackson Recommendations**

In response to serious concern amongst the judiciary that the costs of litigation in England and Wales are too high and disproportionate to sums in dispute, Lord Justice Jackson carried out a detailed and extensive review in 2009, and made 109 recommendations in his *Costs Review*.<sup>25</sup> The government proposes to implement the main points of the Jackson Review.<sup>26</sup>

### **CFAs and ATE premiums no longer recoverable**

After legal aid was largely deconstructed in the 1990s, the government privatised litigation funding with Conditional Fee Agreements (CFAs) from 1995.<sup>27</sup> Claimants’ exposure to potential liability for opponents’ costs was covered by legal expenses insurance, either pre-existing policies or a new form of after-the-event (ATE) policy. From 1999,<sup>28</sup> the government made CFA success fees and ATE premiums recoverable from losing or settling defendants. Jackson found that the CFA recoverability regime was one of the major drivers of excessive costs.<sup>29</sup> The government proposes to make CFA success fees and ATE premiums irrecoverable. Claimants would in future have to deduct such costs from their damages recovered. This has been the position in Scotland, where it has not caused difficulty.<sup>30</sup>

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<sup>23</sup> Jackson Consultation, para 234.

<sup>24</sup> Jackson Consultation, para 237.

<sup>25</sup> *Review of Civil Costs: Final Report* (2010).

<sup>26</sup> The government prefers the radical recommendations set out above, but also consults on two alternative proposals put forward by Jackson.

<sup>27</sup> Under a CFA, there is a basic fee based on work done charged at an hourly rate, and a success fee based on a percentage of the basic fee. A proportion of the basic fee, subject to court control, is recoverable from a losing opponent. There are certain regulatory requirements governing CFAs, and success fees are capped at 100% of the basic fee.

<sup>28</sup> Access to Justice Act 1999.

<sup>29</sup> *Final Report*, para 3.26.

<sup>30</sup> Lord Gill’s *Report of the Scottish Civil Courts Review* (2009), para 96.

In order to balance the diminution in value of claimants' damages that would be caused by having to pay for their lawyers' success fees and ATE premiums, Jackson proposed that general damages should rise by 10%. The government prefers to provide that the recoverable success fee element should be calculated as a sum equivalent to 10% of the general damages award in each case, rather than to introduce a general rise in general damages. That approach is intended to focus the provision on CFA cases.<sup>31</sup>

The government strongly believes that parties should attempt to reach an agreement to settle as early as possible.<sup>32</sup> Accordingly, it intends that claimants who obtain judgment that exceeds a previous settlement offer (CPR Part 36) should be rewarded by an extra 10% of damages, although the judge would be able to reduce the sum where there are good reasons to do so.<sup>33</sup> The government is considering an alternative rule: if the damages exceeded the settlement offer but not by more than 10%, the claimant would receive costs to the date of the offer but each party would meet their own costs thereafter. The rationale would be that if the offer was so close, the parties should have reached agreement.

### **Qualified one way cost shifting**

The normal rule is 'loser pays' an amount regulated by the court. In order to protect claimants against adverse costs orders in certain types of case, qualified one way cost shifting (QOCS) should apply. Under QOCS:

- Losing claimants would pay their own costs and any success fee, but only the winner's costs to the extent it was reasonable.
- Losing defendants would pay the winner's costs.

The result would be 'costs protection' for certain claimants, in a way that was standard for the many claimants who qualified for legal aid under earlier regimes.<sup>34</sup> The aim of QOCS is to reduce the financial risk for the claimant, and hence reduce the need for ATE insurance.<sup>35</sup> Calculations predict that the regime would protect the vast majority of personal injury claimants, and cost less for claimants and defendants if ATE premiums were to remain recoverable.

The 'costs protection' would apply unless the claimant acts unreasonably (for example by bringing a frivolous or fraudulent claim, or in conducting the claim unreasonably or abusively) or if the claimant is sufficiently wealthy.<sup>36</sup> In order to provide certainty to parties, the government seeks views on providing that the presumption that the claimant would not be liable to pay defendants' costs would apply unless the court orders at an early stage that the financial circumstances of the

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<sup>31</sup> Jackson Consultation, para 100.

<sup>32</sup> Jackson Consultation, para 124.

<sup>33</sup> HMCS figures suggest that 2.5% of all fast and multi track claims are decided at trial, but this figure includes a large number of undefended money claims that proceed straight to judgment without a trial. Of claims that are defended in the fast and multi track, around 25% are decided at trial, but the percentage varies between different types of claim. Jackson Consultation, para 115.

<sup>34</sup> Jackson Consultation, para 131.

<sup>35</sup> Jackson Consultation, paras 85 and 132.

<sup>36</sup> Jackson Consultation, para 136.

parties are such that the claimant should be liable for all or a fixed amount of defendants' costs if the claim fails.<sup>37</sup>

The principal type of case that would be protected would be all personal injury claims (including clinical negligence) so as to preserve claimants' damages being reduced by success fees and ATE premiums.<sup>38</sup> A background point noted by Jackson was that almost all personal injury claimants who bring individual claims have suffered injury and their cases have some merit. (Note that he did consider the position in collective claims.) Jackson also suggested that protection could apply in other types of cases: judicial review claims; defamation claims; housing disrepair claims; actions against the police; and professional negligence claims.<sup>39</sup> He considered that socio-political considerations justify the encouragement of such claims, in which there is often an imbalance of power and means between the parties that he considered should be made more balanced. Many such cases are not funded on a CFA basis. In some cases, there are other controls on the claims that are brought, such as the necessity for the court's scrutiny of merits and approval in judicial review of government action.<sup>40</sup> The government proposes that a defendant of modest means faced with a wealthy claimant could apply at the beginning of a case for the cap on the claimant's costs recovery to be lifted altogether or increased.<sup>41</sup> There is also a suggestion from the environmental sector that an unsuccessful claimant should not be ordered to pay the costs of any other party save where the claimant has acted unreasonably in bringing or conducting the proceedings.<sup>42</sup>

The government has concerns about extending QOCS to (i) cases funded on a traditional hourly rates basis and (ii) to judicial review claims. If QOCS were to be introduced for these claims, the Government considers that it should apply only to individual claimants who should be liable to pay some costs (up to an appropriate limit) – which limit may vary depending on the type of case.<sup>43</sup>

QOCS would apply to individual only and not commercial organisations.<sup>44</sup> It is unclear whether it would apply to civil society bodies like consumer associations: the government notes that some NGOs have substantial assets and should not be afforded costs protection. The consultation does state that organisations would instead be able to apply, as now, for Protective Costs Orders,<sup>45</sup> but it seeks views on whether QOCS should apply to non-commercial organisations bringing claims in the public interest.<sup>46</sup>

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<sup>37</sup> Jackson Consultation, para 143.

<sup>38</sup> Jackson Consultation, para 153.

<sup>39</sup> Jackson Consultation, para 154.

<sup>40</sup> Immigration and asylum cases constitute by far the largest area of judicial claims. Over 90% of contested judicial review claims are not granted permission to proceed: National Audit Office Report HC 124 Session 2008-9. Figures provided by the UK Border Agency indicate that in around 50% of the 2,133 immigration and asylum claims in 2009 where permission was refused on the papers, the court found that the claim was 'abusive' or 'devoid of merit' and/or ordered that a renewed oral application for permission need not be a barrier to removal. Jackson Consultation, para 160.

<sup>41</sup> Jackson Consultation, para 164.

<sup>42</sup> Jackson Consultation, para 165.

<sup>43</sup> Jackson Consultation, para 169.

<sup>44</sup> Jackson Consultation, para 152.

<sup>45</sup> Jackson Consultation, para 165.

<sup>46</sup> Jackson Consultation, para 167.

Claimants would be able to take out ATE insurance if they chose and could afford it. Their lawyers would be permitted to fund disbursements in return for an increased success fee, subject to a 25% of damages cap in personal injury cases.

Trade unions and consumer associations are able to recover costs from opponents on a notionally self-insured basis: this would no longer be permitted.<sup>47</sup>

### **New test of proportionality of costs**

The government accepts Jackson's recommendation that a new test should be introduced that costs should be proportionate to the amount in dispute, which should dominate over the tests of either reasonableness or necessity. He proposed a definition of proportionality as:<sup>48</sup>

*Costs are proportionate if, and only if, the costs incurred bear a reasonable relationship to:*

- *the sums at issue in the proceedings;*
- *the value of any non-monetary relief in issue in the proceedings;*
- *the complexity of the litigation;*
- *any additional work generated by the conduct of the paying party; and*
- *any wider factors involved in the proceedings, such as reputation or public importance.*

The government notes that concerns have been raised that the definition of proportionality as suggested by Jackson may generate satellite litigation because of uncertainty as to when costs would be judged to be disproportionate. To avoid this difficulty, it might be helpful to emphasise in the Costs Practice Direction that the test is intended to be used in the small number of cases where costs assessed as reasonable are nevertheless disproportionate. The Costs Practice Direction might also set out examples of cases where it would generally be inappropriate for the paying party to seek to challenge costs assessed as reasonable on the basis of the proportionality principle.<sup>49</sup>

### **Other issues**

There are various other matters included in the Consultation. The most notable is that fixed recoverable costs should be introduced into certain categories of fast track claims linked to the stage at which the claim is resolved. This was initially proposed by Lord Woolf in 1995, has been strongly recommended by Lord Young of Graffham's Report, *Common Sense, Common Safety* in 2010, and would copy the position in Germany (although no official documents note that). The government aims to introduce a new regime for low value personal injury claims in road traffic cases by April 2012.

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<sup>47</sup> Jackson Consultation, para 94.

<sup>48</sup> Final Report page 38, para 5.15

<sup>49</sup> Jackson Consultation, para 219.



A working party is also considering making damages predictable. A pilot scheme will be developed by June 2011. The government does not consider that it is necessary to abolish the indemnity principle, which prevents a party recovering more by way of costs from an opponent than it is obliged to pay its own lawyers.<sup>50</sup> Consideration is being given to improving fact-finding in clinical negligence cases.

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<sup>50</sup> Jackson Consultation, para 276.