Case No: B3/2000/0540

Neutral Citation Number: [2001] EWCA Civ 1246
IN THE SUPREME COURT OF JUDICATURE
COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM CHESTER COUNTY COURT
His Honour Judge Edwards
District Judge Wallace

Royal Courts of Justice
Strand, London, WC2A 2LL

Tuesday 31st July 2001

B e f o r e :

LORD PHILLIPS M.R.
and
LORD JUSTICE BROOKE

Stephen Callery — **Claimant/Respondent**

- and -

Charles Gray — **Defendant/Appellant**

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(Transcript of the Handed Down Judgment of
Smith Bernal Reporting Limited, 190 Fleet Street
London EC4A 2AG
Tel No: 020 7421 4040, Fax No: 020 7831 8838
Official Shorthand Writers to the Court)

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Peter Birts, QC and David Holland (instructed by **Beachcroft Wansbroughs** for the Appellant)
Geoffrey Nice, QC and Nicholas Bacon (instructed by **Amelans** for the Respondent)

Representations by Other Interested Parties:
Allan Gore (instructed by **Pattinson & Brewer** for the Association of Personal Injury Lawyers)
John Leighton Williams QC (instructed by **Barlow Lyde & Gilbert** for the Association of British Insurers)
Timothy Dutton QC (instructed by **Rowe Cohen** on behalf of the After Event Insurers' Group Forum)
William Norris QC (instructed by **Colman Coyle** on behalf of Claims Direct Ltd)
Cyrus Katrak (instructed by **Andrew Gardner Partnership** on behalf of Motor Accident Solicitors Society)
Carine Patry (instructed by **Anthony Brooks** of The Law Society)

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Judgment As Approved by the Court

Summary

(This summary does not form part of the judgment)

In its first judgment on this appeal the Court of Appeal (Lord Woolf CJ, Lord Phillips MR and Brooke LJ) explained why they were not then able to deal with one issue in the appeal. This related to the reasonableness of the "after the event" insurance premium of £350.

The court had invited Master O'Hare, a costs judge, to inquire into the make up of premiums of this kind. His inquiry revealed that there were disputes between the various parties about the recoverability of certain elements of such premiums. For convenience, his report has been annexed to this judgment, subject to a warning as to its status (see para 4). In Lord Woolf's absence on official business the court reconstituted itself as a two-judge court to determine these disputes before the end of the current legal term.

In this judgment the court has held that the words "insurance against the risk of incurring a costs liability" in section 29 of the Access to Justice Act 1999 mean "insurance against the risk of incurring a costs liability that cannot be passed on to the opposing party" (see para 59). The court is satisfied that this interpretation accords with Parliament's legislative intention and with the overall scheme for the funding of legal costs (see para 60). In Mr Callery's case the whole of the cover, including the small element of cover for "own costs insurance" could be regarded as falling within the description of insurance against the risk of liability within section 29 (see para 61) and the premium of £350 was reasonable (see paras 70 and 73).

In relation to other policies the circumstances in which and the terms on which "own costs" cover will be reasonable, so that the whole premium can be recovered as costs, will have to be determined by the courts when dealing with individual cases, assisted, if appropriate, by the Rules Committee (para 61). Other issues mentioned in Master O'Hare's report will fall to be judicially determined as and when they arise in individual cases. The Court of Appeal is anxious that issues of general importance shall be brought before it for authoritative determination as quickly as possible and will give expedition to cases that raise such issues (para 4).

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LORD PHILLIPS M.R.

This is the judgment of the Court.

Introduction.

1. On 17 July this Court, presided over by the Lord Chief Justice, gave judgment in this Action and in *Russell v. Pal PaK Corrugated Ltd.* Each was an appeal against an order for costs made in costs-only proceedings pursuant to CPR 44.12A. The two appeals were heard together as they raised common issues. Those issues arose out of challenges made by the defendant in each action to the recovery of uplift under a conditional fee arrangement (CFA) and, in this Action, to the recovery by way of costs of the premium for an after the event (ATE) insurance policy.

2. In that judgment the Court ruled that there was jurisdiction, under section 29 of the Access to Justice Act 1999, to include in an award of costs made under CPR 44.12A an insurance premium paid in respect of contemplated proceedings notwithstanding that the claim was subsequently settled before those proceedings were initiated. The Court also ruled that, in principle, in a case such as this it is reasonable for a claimant to take out ATE cover at an early stage of the proceedings and before it is known whether the defendant is contesting the claim.

3. In issue in this appeal was whether the amount of the ATE premium, that is to say £350, was reasonable. The Court did not consider that it had sufficient information about ATE insurance to rule on that issue. Accordingly it directed that Master O'Hare should, after considering submissions and evidence submitted on behalf of the parties and others with an interest in the issues raised, submit a report to the Court. Master O'Hare has now submitted that report, dated 23 July 2OO1. That report raises issues of general importance in relation to ATE insurance which need to be determined as quickly as possible. For that reason this Court has reconstituted, in the absence of the Lord Chief Justice on official duties, in order to give judgment before the end of term.

The status of Master O'Hare's report.

4. Master O'Hare's report has been provided to the parties and is thus in the public domain. We have decided to annexe it to this judgment but must emphasise that, by doing so, we do not confer upon it a status which it does not, in law, enjoy. In the course of his report Master O'Hare has identified a number of issues of principle. He has expressed a provisional view in relation to the answer to some of those issues. His views may prove of assistance to those faced with the task of

ruling on the recoverability of ATE premiums, but they cannot be treated as definitive. The issues will fall to be judicially determined as and when they arise in individual cases. This Court is anxious that issues of general importance should be brought before it for authoritative determination as quickly as possible and will give expedition to cases that raise such issues. The hearing of this appeal exemplifies that policy.

5. In the present appeal we propose to address only those issues identified by Master O'Hare which arise on the facts of this case. It would not accord with the interests of justice to express views on other issues without hearing detailed argument on behalf of those directly affected by them in the context of the facts that raise those issues. We shall, in the course of our judgment, identify some of the issues which are not raised by the facts of this case and which remain to be resolved. The principal issue raised by this appeal is whether the cost of insuring against failure to recover ones own costs can be recovered under section 29 of the Access to Justice Act 1999.

The statutory framework

6. The jurisdiction to include in an award of costs an ATE insurance premium is conferred by section 29 of the Access to Justice Act 1999, which provides:

> "**Recovery of insurance premiums by way of costs**
>
> Where in any proceedings a costs order is made in favour of any party who has taken out an insurance policy against the risk of incurring a liability in those proceedings, the costs payable to him may, subject in the case of court proceedings to rules of court, include costs in respect of the premium of the policy."

7. The phrase 'a liability in those proceedings' is imprecise. It does not define the nature of the liability. That the liability is restricted to liability in respect of legal costs is not, however, in issue or in doubt. That restriction can be clearly identified from Parliamentary material admissible under the principle in *Pepper v Hart* [1993] AC 593. It is also apparent from the rules of Court, subject to which section 29 expressly takes effect.

8. CPR 43.2, which sets out definitions, provides:

> "(k) 'funding arrangement' means an arrangement where a person has -

(ii) taken out an insurance policy to which section 29 of the Access to Justice Act 1999 (recovery of insurance premiums by way of costs) applies;

(m) 'insurance premium' means a sum of money paid or payable for insurance against the risk of incurring a costs liability in the proceedings, taken out after the event that is the subject matter of the claim;"

It is thus necessary, when considering whether, or to what extent, a premium is recoverable by way of costs to ask the question whether it is consideration paid or payable for insurance against the risk of incurring a costs liability in the proceedings.

9. The following rule is also relevant to the issues arising on this appeal:

"**44.5 Factors to be taken into account in deciding the amount of costs**

(1) The court is to have regard to all the circumstances in deciding whether costs were-

(a) if it is assessing costs on the standard basis-

(i) proportionately and reasonably incurred; or

(ii) were proportionate and reasonable in amount,"

10. The following provisions of the Costs Practice Direction are also of relevance:

"**Section 11 Factors to be taken into account in deciding the amount of costs: rule 44.5**

11.7 Subject to paragraph 17.8(2), when the court is considering the factors to be taken into account in assessing an additional liability, it will have regard to the facts and circumstances as they reasonably appeared to the solicitor or counsel when the funding arrangement was entered into and at the time of any variation of the arrangement.

> 11.10 In deciding whether the costs of insurance cover is reasonable, relevant factors to be taken into account include:
>
> > (1) where the insurance cover is not purchased in support of a conditional fee agreement with a success fee, how its cost compares with the likely cost of funding the case with a conditional fee agreement with a success fee and supporting insurance cover;
> >
> > (2) the level and extent of the cover provided;
> >
> > (3) the availability of any pre-existing insurance cover;
> >
> > (4) whether any part of the premium would be rebated in the event of early settlement;
> >
> > (5) the amount of commission payable to the receiving party or his legal representatives or other agents."

The test of what is reasonable

11. It was common ground, and rightly so, that the Court, when considering whether to award an insurance premium by way of costs, has to consider whether the premium is reasonable. It was also common ground that, insofar as the Court finds that the premium is not reasonable, it can and should reduce it. There was debate as to the appropriate approach to the application of the test of what is reasonable.

12. It is important in this context to draw a distinction between two separate matters. The first is the nature of the benefits to which the litigant is contractually entitled in exchange for the payment of the premium. This falls to be determined from the terms of the contract under which the premium is paid. Section 29 permits the recovery of a premium where this is payment for insurance against the risk of liability for costs. If payment of a so-called premium buys a contractual entitlement to other benefits it is, to say the least, arguable that the premium cannot, to that extent, be recovered under section 29. Thus the Court has to consider the terms of the contract under which the premium is paid to see whether it is simply a contract of insurance against liability for costs or whether it is something other than, or additional to, that.

13. The contractual benefits purchased by the premium must be distinguished from the use made by the insurer of the premium. An insurer will necessarily look to premium income to meet the costs of the business. The primary costs are likely to be those of meeting claims, but the costs will also include matters such as commissions, advertising and, indeed, refurbishing the insurer's premises. The Court will not be directly concerned with how, or on what, the insurer spends the premium income. The Court will, however, be concerned with the question of whether the premium is a reasonable price to pay for the benefits that it purchases. Ultimately, this should be a question to be considered having regard to experience, or evidence, of the market. If an insurer is conducting his business in a manner which incurs extravagant, extraneous or otherwise unnecessary expenditure, which has to be covered by the premiums, those premiums are likely to be uncompetitive. To pay such a premium where other more reasonable premiums are available may disentitle the litigant from making a full recovery of the costs of the premium.

14. Unfortunately Master O'Hare concluded that the market in ATE insurance was not yet sufficiently developed to enable him to identify standard or average rates of premium for different categories of ATE insurance. He expressed doubt as to whether market forces were yet sufficiently compelling. He received a considerable body of evidence of the costs of individual insurers, proffered in confidence, in an endeavour to form a view of the level of premium that was reasonably needed to cover costs. We shall revert to his conclusions in due course. At this point we will confine ourselves to some general observations.

15. It is highly desirable in the interests of justice that an effective and transparent market should develop in ATE insurance. If the litigant is not at risk as to the premium, which is a matter that we shall consider in due course, it is less easy for a competitive market to develop. Nonetheless, we consider that the solicitor advising the client should be in a position to assist him in selecting ATE insurance cover that caters for his needs on reasonable terms. Master O'Hare informed us that there are at present two sources of information as to availability of ATE cover: the magazine "Litigation Funding", published by the Law Society and the web site www.thejudge.co.uk. We would encourage solicitors to take advantage of such sources of information and hope that before long the exercise of choice will result in competition for ATE business which establishes transparent market rates.

16. In the meantime, where an insurance premium is challenged it must be open to the insurer, whose position is akin to a subrogated underwriter, to place evidence before the Court in an attempt to demonstrate that the premium is reasonable having regard to the costs that have to be covered. Satellite litigation involving such an exercise is, however, unsatisfactory. The Judge can only be expected to

give broad consideration to such evidence, for it is not part of the function of a judge assessing costs to carry out an audit of an insurer's business.

17. Master O'Hare remarked in his report that he expected that fairly quickly courts conducting detailed costs assessments would be able to develop benchmark figures. The sooner that market rates for ATE insurance become recognised the better.

The terms of the ATE cover

18. In order to identify the issues of principle which arise in this case it is necessary to identify the material terms of the policy of insurance to which the disputed premium relates.

19. The policy is issued on behalf of Lloyd's underwriters on whose behalf this business is managed by Temple Legal Protection Limited. The cover was issued, under the authority of the underwriters, by Legal Protect Assurance Services Ltd, as Coverholder. The terms of the cover were set out in a Certificate of Insurance. This provided by a schedule that the cover was in relation to a personal injury action against Charles Gray, that the period of insurance was from 04/05/00 to the conclusion of the legal action and that the limit of indemnity was £100,000. The Certificate went on to provide as follows:

> "**THE RISKS THAT YOU ARE INSURED AGAINST**
>
> Insurers agree to indemnify the Insured up to the Limit of Indemnity;
>
> for Opponent's Costs in the event that the Insured becomes liable to pay such costs whether by order of the Court or because the Legal Action has been withdrawn or discontinued or settled with the prior approval of the Insurers, and,
>
> for the Insured's Disbursements in the event that
>
> (a) the Insured become liable to pay Opponent's Costs whether by order of the Court or because the Legal Action has, with the prior approval of Insurers been withdrawn or discontinued or,

(b) following commencement of proceedings and with the prior approval of the Insurers, the Legal Action is settled without the Insured's Disbursements being payable by the Opponent."

"**THE MEANING OF WORDS USED IN THIS INSURANCE**

….

Disbursements

Fees and expenses including the premium and mediators fees, which are not the subject of any contingent or conditional fee agreement, paid by the Appointed Legal Representative on behalf of the Insured to any third party, other than to counsel, in connection with the Legal Action but not including (1) any VAT to the extent that the Insured can recover such VAT from H.M. Customs and Excise and (2) any Disbursements which the Court orders the Opponent to pay to the Insured.

….

Opponent's Costs

All costs, expenses and disbursements ordered by the Court to be paid by the Insured to the Opponent in the Legal Action during the Period of Insurance. Where in the Legal Action orders are made both that costs be paid by the Insured to the Opponent and that costs be paid by the Opponent to the Insured, Opponent's Costs shall then be limited to the net sum (if any) payable by the Insured to the Opponent after all costs payable by the Opponent to the Insured have been set off.

….

EXCLUSIONS

Insurers shall not be liable under this Certificate in respect of:

6. any Disbursements where an order is made by the Court for the Disbursements to be paid by the Opponent, irrespective of whether or not payment is actually made. If the Insured recovers any monies

> from the Opponent in the Legal Action, whether described as damages, costs or howsoever described and whether recovered by judgment or settlement, such recovery shall be deemed to include a recovery of Disbursements insofar as the monies payable by the Opponent (whether or not actually paid) are sufficient to do so.
>
> ….
>
> **6. Assessment of the Premium**
>
> If, in any process of assessment, the Opponent is successful in any challenge to the cost of the premium then it is agreed that the premium which was payable at the conclusion of the Legal Action shall be reduced to the amount which was approved or allowed on assessment. It is agreed by the Insured that the Insurer shall have the right to make any representation to the Court or the Opponent as may be necessary in this matter. Any such challenge must be immediately notified by the Insured to the Insurer."

Issues identified by Master O'Hare

20. Master O'Hare considered the elements that are responsible for the size of the insurance premium, distinguishing between (i) costs and expenses of the insurer funded by the premium and (ii) benefits covered by the premium. He considered whether, and to what extent, a premium covered by section 29 should reflect each of these. We shall do likewise.

Costs and expenses

21. Master O'Hare identified four elements of these: the burning cost, the risk/profit cost, administrative costs and distribution commission.

The burning cost

22. This term describes the cost of meeting claims made under policies issued. Overall premium income must suffice to cover claims made, or the insurer's business will not be viable. Master O'Hare learned that, in respect of claims for personal injury, ATE insurers set out to cover this cost on two different bases:

i) An individual premium is assessed for each risk, or each category of risk ('individual assessment').

ii) A uniform premium is charged in respect of any claim which carries a prospect of success of more than 50% ('block rating').

23. Master O'Hare set out in his report the information supplied by Temple as to the basis upon which the premiums for their policies are determined. Temple has two insurance schemes, one under which a premium is quoted having regard to the facts of the particular case and one under which authority to issue cover is delegated. Under the latter a solicitor is authorised to issue certificates in respect of any case undertaken, rating the case and applying the appropriate premium according to a premium table supplied by Temple. It was on this basis, as we understand it, that Mr Callery's premium was fixed at £350 plus £7.50 insurance premium tax ('IPT'). Thus on this appeal we are concerned with a premium fixed on an individual assessment basis. Master O'Hare was informed by Accident Group Limited, which claims to be the market leader in issuing insurance cover in conjunction with CFA's, that, on a block rating basis, Mr Callery would have been charged £997.50 including IPT. The issue of whether it would have been reasonable for Mr Callery to take out insurance for his claim at a much higher premium than £350, costed on a block rating basis, does not arise for determination on this appeal. On the face of it, adoption of such an option would seem hard to justify.

Risk/Profit cost

24. This item will include the cost of laying off risk by way of reinsurance, where this course is adopted. Master O'Hare received widely differing submissions as to the proportion of the premium which should reflect this item. In the longer term market forces ought to constrain it to reasonable proportions. Plainly no objection can be taken to a premium reflecting a reasonable risk/profit cost.

Administrative costs

25. These must cover items such as personnel, premises, policy issue and processing and claims administration. No objection could be taken to a premium reflecting costs such as these.

Distribution commission

26. Before Master O'Hare objection was taken in principle in some submissions to premiums being increased to cover advertising and other marketing and commissions. We are not aware of the extent to which these are relevant factors in the case of Temple, but we agree with Master O'Hare that no objection can be taken to these in principle. As he has pointed out, PD 11.10 provides that 'the amount of commission payable' is one of the factors that should be taken into account when deciding whether the cost of insurance cover is reasonable. In the longer term, market forces should prevent premiums being unreasonably inflated to reflect extravagant commission payments.

Benefits

27. We now turn to consider the different types of benefit that Master O'Hare identified may be provided in exchange for the 'premium' paid.

Costs awarded by the Court to the opposing party

28. The primary liability covered by Mr Callery's policy was that for opponent's costs as a result of order of the Court or withdrawal, discontinuance or settlement of the Action with the prior approval of the insurers. Such liability can arise in a number of circumstances, which include:

i) An order of the Court to pay the defendant's costs as a result of judgment on liability being given in favour of the defendant, on the normal principle that costs follow the event.

ii) An order of the Court to pay the defendant's costs as a consequence of a failure to beat a Part 36 offer.

iii) An order of the Court to pay the defendant's costs as a result of losing an issue, whether at an interim hearing or at the final hearing.

iv) Any other costs order in favour of the defendant made in the exercise of discretion.

29. All parties were agreed that it is legitimate for ATE insurance to provide cover that falls within the first category set out above. They were right to do so. Such

insurance falls fairly and squarely within the meaning of insurance against the risk of incurring a costs liability in the proceedings - see paragraph 8 above.

30. For the defendant, Mr Peter Birts, QC, objected to the defendant being held liable for that part of the premium which reflects the risk of being ordered to pay costs falling within the second category set out above, and we believe that his argument would naturally extend to the third and fourth categories. In essence this argument was simply that it was unfair to defendants that claimants should be able to pass on to them liability for insuring against costs liabilities of such a type in that those liabilities are likely to have been incurred as a result of failure on the part of claimants to conduct the litigation in a reasonable manner.

31. It seems to us that such an argument would frequently be open in relation to costs which follow the event after a claim fails. All four categories of risk aptly fall within the words 'risk of incurring a costs liability in the proceedings'. In our judgment insurance against such risks falls within the ambit of section 29.

Collateral benefits

32. The benefits purchased by Mr Callery for his £350 premium were restricted to insurance against the risk of paying legal costs of one kind or another. The contract did not entitle him to any collateral benefits. This position contrasts with that of a litigant who engages the services of an organisation such as Claims Direct. Master O'Hare received evidence of:

> "work done handling and negotiating the claim (whether or not it duplicates what the solicitors may do) and work done to comfort and reassure the insured and/or his family, e.g: practical help in the home, counselling, helping in the arrangement of business matters and accompanying the insured on hospital appointments and other appointments."

33. If a payment described as a 'premium' entitles the insured to benefits such as these it is, as we have already observed, at least arguable that - to that extent - the 'premium' does not fall within the ambit of section 29. Mr Norris, QC, who appeared with our permission to protect the interests of Claims Direct, was concerned that we might, in this judgment, purport to determine this issue. We do not do so, but express the hope that it will rapidly be brought before this Court in a case where it is raised on the facts.

Own costs cover

34. The insurance granted by Temple to Mr Callery entitled him to an indemnity in respect of his own disbursements, as defined in the cover note, in the event of the contingencies identified in the cover note. Those contingencies amounted, in effect, to the failure of Mr Callery's claim.

35. Mr Birts contended that an insurance premium that purchases a benefit of this nature does not fall within the scope of section 29. Section 29 insures against 'the risk of incurring a liability'. The cover provided in relation to Mr Callery's disbursements was not against the *risk of incurring* those liabilities. It was against the risk of being unable to recover an indemnity in respect of them consequent upon the failure of the claim. The liabilities themselves *were incurred* voluntarily, not in consequence of a fortuity such as an order of the Court.

36. Mr Nice, QC, on behalf of Mr Callery, and those who support his case, argued that it was necessary to bring own costs insurance within the ambit of section 29 if effect was to be given to the scheme of the legislation, which was to enable litigants to bring meritorious claims without incurring any significant risk as to either their own or their opponents' legal costs. They did not, however, attempt to explain the precise route of statutory interpretation which would enable own costs insurance to fall within the definition of 'insurance against the risk of incurring a liability'.

37. The issue is not one of great significance in the context of this appeal. Insurance in respect of certain of his own costs constituted a relatively minor element of Mr Callery's cover, for most of his own costs were covered by his CFA. But the issue is one of general importance. Some types of legal costs insurance, including that offered by Claims Direct, are not designed to be used in conjunction with a CFA, but provide the litigant with insurance against the risk of having to pay both sides' costs if the claim fails. This is sometimes referred to as BSI (both sides insurance), as opposed to CFI (conditional fee insurance). Does the part of a BSI premium that reflects the risk that the insured will be left to bear his own costs falls within the ambit of section 29? The answer to this question turns on the answer to the issue that arises in respect of Mr Callery's disbursements.

38. Insurance is the purchase of an indemnity against the risk of loss caused by a fortuity. A contract that provides for the payment of a sum of money upon the occurrence of a fortuitous event will not be insurance unless the sum in question is intended to indemnify against a consequence of that event. When considering the nature of 'own costs insurance', it is necessary to identify the fortuity that

triggers liability and to consider the extent to which this fortuity exposes the insured to the loss against which cover is provided.

39. A litigant may be left to bear his own costs in a number of different circumstances. The costs incurred may be excessive or otherwise unreasonable, so that they will in no circumstances be recoverable from the litigant's opponent. Reasonable costs will be recoverable only under a settlement agreement or an order of the Court. A litigant may fail to obtain a Court order for payment of costs for a number of reasons. His claim may fail, so that costs are ordered against him, rather than in his favour. He may fail on a particular issue at an interlocutory stage or at the final hearing and, in consequence, fail to obtain a costs order in relation to that issue. If he is successful the costs order made in his favour will not necessarily cover his solicitor and client costs.

40. If section 29 is to be interpreted so as to cover insurance against the risk of the litigant being left to bear his own costs, it is necessary to identify the scope of the cover that is permissible. At the end of the day an interpretation must be given to section 29 that can be applied in practice to different varieties of cover. There are a number of possibilities.

41. Cover may provide a litigant with an indemnity against his own costs in the event that the claim fails. In such a situation the fortuity of the claim failing is likely, in large measure, to be the reason why the insured fails to obtain an order that his opponent indemnify him in respect of his costs. This will, however, only be true to the extent that he would have obtained an order for those costs had the claim succeeded. To what extent can one say, even speaking broadly, that he has 'incurred a liability' for his costs as a result of the failure of his claim? Mr Callery's cover does not make it a condition of the recoverability of his disbursements in the event of the failure of his claim that these would have been recoverable had his claim succeeded. In the case of BSI this question is likely to be much more significant.

42. Even where a litigant's claim succeeds he may not obtain an order requiring the unsuccessful defendant to pay all his costs. Under CPR 44.3 there are many circumstances which may lead a Court to exercise its discretion not to award a successful claimant all his costs. We are not aware of the extent to which insurance cover can be obtained which protects a litigant from the risk of failing to obtain an order for the recovery of all his costs when his claim succeeds. It appears, however, that such cover does exist.

43. Master O'Hare refers in his report to a practice of granting a benefit which consists of 'ring-fencing' the damages; that is providing that unrecovered costs will not reduce the amount of damages below a specified minimum figure. More

specifically, some policies provide an indemnity against failing to recover, in whole or in part, the premium paid for the insurance itself. Such an indemnity will apply to the extent that recovery of premium is disallowed because it is excessive, or outside the ambit of section 29.

44. Mr O'Hare was informed that, when Claims Direct decided to 'ring fence' the first £1,000 of damages recoverable, they added £200 to the premium to cover the cost of assuming this risk. Can the cost of insuring against the risk of having costs disallowed when the claim succeeds be brought within the ambit of 'insurance against the risk of incurring a costs liability' in section 29?

45. There is a small element of such cover in the policy issued on behalf of Temple to Mr Callery. Condition 6 provides for a reduction of the premium to the extent that this is disallowed on assessment of costs. This is, on analysis, protection against the failure to recover an element of own legal costs, notwithstanding the success of the claim. On the facts of the present case the extent to which this feature is reflected in the amount of premium must be minimal or non-existent.

46. The considerations set out above have to be borne in mind when considering what appeared at one time to be the simple submission that the proportion of the premium paid for 'own costs insurance' is recoverable under section 29.

47. In support of this submission Mr Nice and his supporters made the following points: (1) It was Parliament's intention that the cost of own costs insurance should be recoverable. (2) The overall scheme for funding litigation requires that the cost of own costs insurance should be recoverable. (3) The Civil Procedure Rules and Practice Directions envisage that the cost of own costs insurance will be recoverable.

Parliamentary material

48. The provisions of the Access to Justice Act 1999 that deal with the funding of litigation were preceded and followed by a lengthy and thorough consultation exercise. Counsel referred us to a passage from the Lord Chancellor's Department's explanation of policy published in February 2000, following consultation. It sets out the matters that the court might wish to consider before awarding an insurance premium by way of costs:

> "where the insurance cover is purchased in support of a conditional fee agreement with a success fee, the percentage of the premium compared to the level of cover;

> where the insurance cover is not purchased in support of a conditional fee agreement with a success fee how its cost compares with the likely costs of a similar case running under a success fee and supporting insurance cover;
>
> the level of cover provided;
>
> the extent of the cover provided, for example against the other side's costs or both sides' costs;
>
> the availability and accessibility of alternative products to the one chosen;"

This indicates that it was the Government's intention that it would be possible to recover the cost of own costs insurance.

49. In June 2000 the Government published a consultation paper on collective conditional fees. This included the following statement:

> "**Section 29** of the Act allows the court to include in any costs order, any premium paid for an insurance policy against the risk of incurring a liability in those proceedings. The recovery of the insurance premium is not limited to policies backing conditional fee agreements, but covers all after the event policies. The way in which recovery operates is subject to rule of court."

This indicates that the Government believed that it had achieved the intention set out in the previous paragraph.

50. Counsel have not been able to refer us to any authority which supports the use of materials such as those referred to in the previous two paragraphs as an aid to statutory interpretation and we do not consider that they are admissible for this purpose.

51. Of more significance are explanatory notes to the Access to Justice Bill that were provided when this was brought from the House of Lords to the House of Commons on 17 March 1999. The notes explain that they were 'prepared by the Lord Chancellor's Department in order to assist the reader of the Bill and to help inform debate on it. They do not form part of the Bill and have not been endorsed by Parliament'. The notes included the following passage:

> "There are also available insurance policies which can be taken out when someone is contemplating litigation to cover the costs of the other party and the client's own costs (including, if not a conditional fee case, the client's solicitor's fees) if the case is lost. Some of them were developed to support the use of conditional fee agreements but others are used to meet lawyers' fees charged in the more traditional way. For the same reason that the success fee under a conditional fee is being made recoverable, it is also proposed to make any premium paid for protective insurance recoverable too."

52. Counsel were no more successful in referring us to authority on the use of material such as this as an aid to statutory interpretation. They were agreed, however, that it followed logically from *Pepper v Hart* [1993] AC 593 that this material was admissible as an aid to interpretation where the wording of a statute was ambiguous. We were referred to the following passage of the speech of Lord Bingham of Cornhill in *R v Environment Secretary, ex p. Spath Holme Ltd* [2001] 2 WLR 15 at p.31:

> "In *Pepper v Hart* the House (Lord Mackay of Clashfern LC dissenting) relaxed the general rule which had been understood to preclude reference in the courts of this country to statements made in Parliament for the purpose of construing a statutory provision. In his leading speech, with which all in the majority concurred, Lord Browne-Wilkinson made plain that such reference was permissible only where (a) legislation was ambiguous or obscure, or led to an absurdity; (b) the material relied on consisted of one or more statements by a minister or other promoter of the Bill together, if necessary, with such other parliamentary material as might be necessary to understand such statements and their effect; and (c) the effect of such statements was clear (see pp 640B, 631D, 634D). In my opinion, each of these conditions is critical to the majority decision."

53. Mr Birts accepted that explanatory notes provided by the sponsoring Department constituted 'parliamentary material' to which reference could be made, although he questioned how much, if any, weight could be attached to it. It seems to us that this concession follows logically from the principle in *Pepper v. Hart.* We have commented on the enigmatic nature of section 29. In interpreting the section we have derived considerable assistance from this Parliamentary material.

54. The passage in the explanatory notes suggests that it was the intention of the Lord Chancellor that own costs insurance should be available as an alternative to a CFA as a method of protecting the litigant against the risk, consequent upon the failure of a claim, of having to bear his own legal costs. We have seen nothing to suggest that it was the intention that claimants should be entitled to pass on to defendants the cost of insuring against failure to be awarded costs on the ground that the costs had been unreasonably incurred or were otherwise objectionable.

The overall scheme

55. Those interests supporting Mr Callery argue that the overall scheme of funding litigation under CFAs and ATE insurance is designed to make it possible for a solicitor to provide the client with a package that will remove any risk as to costs, whether his own or his opponents. This, they argue, cannot be achieved unless the litigant is able to insure against the risk of having to pay his own disbursements. Furthermore, so it is argued, the availability of BSI will increase flexibility and enable the litigant to select the most advantageous means of covering his liability to pay costs.

56. Mr Birts contended that it is not part of the legislative scheme that litigants should be provided with the opportunity to litigate free of all cost risk. He drew attention to the fact that the consultation paper issued by the Lord Chancellor's Department in September 1999, which sought views on the detailed implementation of the Access to Justice Act 1999 provisions for funding litigation, was entitled *Conditional Fees: Sharing the Risks of Litigation.* He pointed out that under the previous legal aid regime a litigant in receipt of legal aid was not shielded from all liability as to costs. There was no warrant for seeking to provide such protection under the new regime. The Court should proceed with caution in order to avoid unjustifiable increases in legal costs.

57. There is some force in Mr Birts' submissions. We observe that the combination of the CFA and the ATE cover available to Mr Callery does not afford him complete protection against the risk of liability to pay costs. At the same time we are in no doubt that it is a primary objective of the present scheme that a litigant with an apparently meritorious claim should not be precluded from advancing it by the obligation to pay costs, or the risk of having to do so. If a litigant is precluded from insuring against having to meet his own disbursements, there will be occasions when the cost of these will discourage or preclude him from bringing his claim. Furthermore, it does seem clear that it has always been the intention of the Lord Chancellor, as promoter of the legislation, that own cost insurance should be available as an alternative to the CFA.

The Civil Procedure Rules and the Practice Direction

58. As we pointed out at the outset, the provisions of section 29 are imprecise. The September 1999 consultation paper stated:

> "…the Act only provides the legislative framework. The detail of the changes to conditional fees will be provided through secondary legislation, while the operation of the recoverability of the success fee and insurance premium will be informed by Rule of Court and Practice Directions."

The provisions of the Rules and Practice Directions are of particular importance in clarifying and delimiting the circumstances in which an insurance premium can be claimed under section 29.

59. The provisions of Practice Direction 11.10 clearly anticipates that insurance cover that falls within the ambit of section 29 may provide alternative protection to that provided by a CFA coupled with insurance. Such cover will necessarily include own cost insurance. The Practice Direction cannot, of course, confer on the court a jurisdiction that falls outside that conferred by section 29. The question is whether section 29 can and should be interpreted so as to treat the words 'insurance against the risk of incurring a costs liability' as meaning 'insurance against the risk of incurring a costs liability that cannot be passed on to the opposing party'.

60. We have concluded that section 29 can and should be interpreted in this way. We believe that such an interpretation will do no more than give the words the meaning that would be attributed to them by the reasonable litigant. It will also give the words a meaning that accords with the legislative intention and with the overall scheme for the funding of legal costs.

61. The circumstances in which and the terms on which own costs insurance will be reasonable, so that the whole premium can be recovered as costs, will have to be determined by the courts, when dealing with individual cases, assisted, if appropriate, by the Rules Committee.

62. In the case of Mr Callery's policy, the right to recover the costs of disbursements is tied to the situations where the protection afforded by the CFA would come into play. It is arguable that the disbursements that are covered are disbursements of a kind that would be recoverable as costs. We cannot see that there is any objection in principle to this cover forming part of that afforded to Mr Callery by his legal costs insurance and consider that the whole of the cover can be

considered as falling within the description 'insurance against the risk of liability' within section 29. In this context our only reservation arises in relation to the premium rebate provision in condition 6. As we have indicated, however, this is of no practical significance in the present case and we consider that it is better that the issue of whether the cost of such cover is recoverable under section 29 should be dealt with in a case where this matters.

The cost of the premium

63. The cover provided by the Temple policy, as is usual, includes cover against the risk of being unable to recover the premium as a consequence of losing the action. This item of own cost cover received special consideration by Master O'Hare. We can see no reason, in principle, why this should not form part of the cover provided under insurance that falls within section 29, provided always that any part of the premium attributable to it is reasonable in amount.

Deferred payment of the premium

64. No challenge to the amount of the premium was made by Mr Birts on the ground that it must include an element to reflect delay in paying it. Indeed, it is not clear to us from the documents precisely what was agreed as to the payment of Mr Callary's premium. Condition 6 of the cover note suggests that the premium was 'payable at the conclusion of the legal action'. If so, this would be typical of ATE insurance and necessarily so if litigants are not going to be discouraged by the obligation of making a substantial payment 'up front'.

65. CPR 44.3B(1) precludes a solicitor from recovering any proportion of uplift that relates to deferred receipt of fees and expenses. Amelans had added 20% to their uplift to reflect delayed payment and, rightly, did not seek to recover this in these proceedings. Solicitors have always had to wait for payment of legal aid work to a greater or lesser degree, and their fee structure has, no doubt, reflected this. We understand that, in most cases, solicitors do not make any specific addition to uplift to compensate for deferred payment. Nor, so far as we are aware, do they do so in the case of ATE insurance premiums. If and when objection is taken to an insurance premium on the ground that it has been increased to compensate for deferred payment, this issue will have to be addressed. It does not arise in the present case.

The effect of BTE insurance

66. In the case of *Sarwar v Alam* a claimant passenger took out ATE insurance but was subsequently found to be covered by a policy of BTE insurance that the defendant driver had taken out. In these circumstances His Honour Judge Halbert disallowed the cost of the ATE premium. Permission to appeal against his decision has been given, and the Court will expedite the hearing so that the issue can be determined before the end of the vacation. It is not an issue which arises in the present case.

Is £350 too much?

67. We have concluded that there is no reason of principle for refusing to award under section 29 any part of the premium payable for Mr Callery's ATE insurance cover. We have, however, to deal with a challenge made by Mr Birts to the amount of £350 on the ground that it was excessive in the case of a simple passenger claim. His submission was that the maximum premium that would have been reasonable would have been in the region of £160. In support of this figure, he placed before the court a sheet of calculations. Some of the data upon which these were based was not before this Court at the substantive hearing of the appeal. None of it had been placed before the Judge below. The respondent had been given no advance notice of these calculations. Critically, the calculations depended upon an assumed loss rate of 2.1%, which was not supported by any evidence placed before us. In the circumstances, we did not find it possible to base any conclusions on these calculations.

68. Master O'Hare did his best to investigate premium rates in the market. He found that it was not possible to state standard or average premiums for different classes of business. He also found that results over several years had been uniformly poor, leading to several major increases in premium rates over those years. This led him to conclude that it was reasonable to presume as a starting point that a premium was reasonable unless the contrary was shown.

69. We do not consider it correct to start with Master O'Hare's presumption. When considering whether a premium is reasonable, the Court must have regard to such evidence as there is, or knowledge that experience has provided, of the relationship between the premium and the risk and also of the cost of alternative cover available. As time progresses this task should become easier. In the present case it is not easy as both data and experience are sparse. When considering CFA uplift, we proceeded on the basis that the success rate of claims was at least 90%. Claims that do not succeed will not inevitably be pursued to judgment. Sometimes they will be withdrawn in circumstances that do not involve any liability for defendant's costs. As against this, Mr Callery's cover

extended to adverse costs orders after a Part 36 offer, or an interlocutory defeat. The amount insured was £100,000, but this, of course, was the limit of underwriters' liability and no guide to the much smaller indemnity that is likely to be involved when such a claim fails.

70. In the circumstances, the amount of the premium does not strike us as manifestly disproportionate to the risk. We do not find it possible to be more precise than this. So far as alternatives are concerned, Mr Callery was able to choose, with the assistance of his solicitors, cover at a premium near the bottom of the range of what was available. The premium was one tailored to the risk and the cover was suitable for Mr Callery's needs. The policy terms also had the attractive feature that they gave his solicitors control over the conduct of the proceedings on his behalf, without any involvement by a claims manager until a settlement offer was made. We have concluded that the Court below was right to find that the premium was reasonable.

71. Just as in the case of our decision on the CFA uplift, we should emphasise that this judgment should not be treated as determining once and for all that a premium of £350 is reasonable in a case such as this. As further information and experience about the market becomes available it will be possible to found conclusions as to whether premiums are reasonable on a sounder basis.

72. We see no reason in principle why the £7.50 IPT should not also be recoverable, and none was suggested.

73. For these reasons the appeal against the inclusion of the whole of Mr Callery's insurance premium as an item of his costs will be dismissed.

COURT OF APPEAL Case No. 2001/0540/33

MC002977
ON APPEAL FROM THE CHESTER COUNTY COURT

B E T W E E N

STEPHEN CALLERY

Claimant

- and -

CHARLES GRAY

Defendant

REPORT OF MASTER O'HARE

DATED 23 JULY 2001

BACKGROUND

1. In this case, the Court of Appeal has referred to me eleven questions relating to after-the-event, (ATE) insurance in connection with claims for damages for personal injury in respect of road traffic accidents (RTA). The purpose of the inquiry and report is to enable the Court of Appeal to give guidance in its judgment as to the practice to be adopted in future when taking out such insurance.

2. In preparing this report, I have received written submissions from twenty parties and interested parties: their names are set out in Annex 1 to this report. In many of the submissions there is a request for confidentiality as to the whole or part of the submission. Written submissions received on or before 29 June 2001 raised in my mind a series of supplementary questions which I communicated to the parties and interested parties on Tuesday, 3rd July 2001. The Court of Appeal order setting up my inquiry and report had specified Friday, 6th July as a day upon which I would seek clarification of the written submissions received. At that hearing representations were made by or on behalf of parties and interested parties whose names are set out in Annex 2 to this report. An account of the 6 July hearing and certain related matters is set out in paragraphs 3 to 8 below. My report on the submissions on all of the questions, original and supplementary are set out in paragraphs 9 to 77 below. Some conclusions are set out in paras 78 and 79.

HEARING ON 6 JULY 2001

3. I began the hearing by making the following preliminary points:

(a) I was keen to include in my final report guidance on reasonable ATE premiums in pounds and pence for all classes and categories of insurance in personal injury claims if I could. However, I doubted whether it would be practicable to do so and, in any event, I was aware of the limited nature of my Inquiry, which concerns RTA claims.

(b) The guidance I would give would be as to historic cases only, ie, policies taken out before a certain date. I was provisionally of the view that, for the future, further guidance could be published by the Senior Costs Judge. It might be appropriate to publish such guidance, after consultation, every six months unless and until such guidance became unnecessary. The guidance would be guidance to judges. The guidance would not fetter the discretion of such judges and, although given after consultation with interested parties, would not be intended to regulate interested parties.

(c) I did not consider it part of my jurisdiction to decide the so called question of prematurity, ie, is it unreasonable for an intending claimant to take out insurance before seeking an indication from the defendant as to whether the claim is to be contested. I would try to give figures for polices taken out at the outset and also policies taken out after the intended defendant had indicated his position.

(d) I expressed my provisional view that I did not think it part of my jurisdiction to decide whether Section 29 of the Access to Justice 1999 covers the cost of insurance cover not only in respect of the "other side's costs" but also in respect of "both sides' costs". As with the prematurity issue, I would try to produce figures covering all possibilities.

4. Questions were then raised about my jurisdiction to ask supplementary questions, the extremely limited time allowed to answer them and the fears which some of those supplementary questions had raised that I had made preliminary decisions rejecting arguments made in answer made to the original questions. I was addressed on these points particularly by Mr Birts QC (for the Appellants), Mr Norris QC (for Claims Direct) and Mr Langford (Group Chairman of the Accident Group Ltd). As a result of those submissions I made the following decisions:

(a) By Tuesday 10 July 2001 I would deliver my draft report (mainly concerning the original questions) to all parties and interested parties named in Annex 1 and 2 of this Report.

(b) I would take into account for my final report all written submissions received from parties and interested parties on or before Friday 20 July 2001.

(c) There would be no further oral hearings in this Inquiry.

5. The hearing lasted just over 3 hours. I will deal with the many submissions made when I deal with the answers to the Inquiry questions below. The last persons to make submissions were Mr Norris QC and Mr Birts QC. As the hearing developed I had noted down particular questions I would like them or their clients to deal with. Both wanted to give their replies by way of written submissions. Mr Birts QC also asked me to order the mutual disclosure of all written submissions to the original questions and to the follow-up questions edited as parties wished to remove confidential information. I had no hesitation in refusing that application. It seems to me that this Inquiry is only a quasi-judicial Inquiry made by a person independent of any interest group who will hear anything which any interest group wishes to say. The importance of confidentiality was referred to in the directions setting up this Inquiry.

6. On Tuesday 9 July 2001 I circulated copies of my draft Report to all the parties and interested parties who had contacted me in this matter by that date. The draft Report set out the further questions I wished to ask of Claims Direct and of the Appellants. Both have supplied answers. For convenience the further questions are set out in Annex 3 to this Report together with the supplementary questions which I had circulated on 2 July 2001.

7. On 17 July 2001 the Court of Appeal handed down its judgment in Callery v Gray. I must here draw attention to two paragraphs of that judgment, paragraphs 15 and 65 which are as follows:

"15. The introduction of CFAs in 1995 still left a litigant at risk of having to pay the other side's costs. The Law Society therefore developed the ATE policy, with the help of insurance brokers, as a new form of insurance cover. Since about that time there have also been forms of ATE insurance which provide cover

against other risks, but we are not concerned with such cover, whatever form it takes, in this judgment .

...

65. We have already observed (see para 15 above) that ATE insurance can take a number of quite distinct forms. The major distinction is between the ATE insurers who provide litigation costs insurance cover for personal injury related claims directly through solicitors or through claims management companies and those who insure non-personal injury or commercial claims. There is also a distinction between ATE cover that is provided only in respect of the "other side's costs" and that provided "for both sides' costs". ATE cover can also be provided for an individual claimant or in standard form by solicitors under delegated authority. As we stated in paragraph 15, the only form of ATE insurance to which this judgment relates is insurance providing cover against the other side's costs. We do not deal with the question whether ATE cover against other risks falls within section 29." (See also, para 78 of the judgment.)

8. Having regard those paragraphs and to the submissions which have been made to me upon my jurisdiction to decide the question set out in para 3(d) above, I am now of the view that I should not report any conclusions I have reached on ATE insurance covering "both sides' costs". I understand that there is to be a hearing tomorrow, 24 July 2001, on the question whether the own costs element in a policy supporting a CFA is recoverable under Section 29 of the Access to Justice Act 1999. Accordingly my conclusions seek to identify as a separate item the reasonable costs incurred in respect of the own costs element. This item may then be stripped out if appropriate.

QUESTION 1

Which firms, organisations and insurers are currently offering ATE insurance and

(a) Are they all members of the ATE group?
(b) If not, are they members of any other group or independent?

9. The ATE group gave me a list of 27 companies and firms currently offering ATE insurance. About twenty of them are members of the ATE group. The list comprises pure risk carriers, brokers and some claims management companies. The ATE group believe that there are at least another thirty claims management companies and/or referral agencies which also have an involvement in offering various types of ATE insurance. DAS have supplied me with a list of over 60 names of insurers, claims management companies and similar bodies all dealing in ATE insurance.

10. Some members of the ATE group are also members of other groups. For example, DAS is also a member of the Association of British Insurers (ABI), The Motor

Uninsured Loss Recovery Association (MULRA), the International Association of Legal Expenses Insurance (RIAD), the British Insurance Law Association (BILA) and the ABI Legal Expenses Forum.

11. There are two sources of information for the intending litigant or his solicitor when looking for the most suitable policy: the magazine "Litigation Funding" published by the Law Society regularly includes charts which compare the various ATE products available. To obtain what may often be the most up-to-date information, it is possible to visit the commonly used web-site www.thejudge.co.uk. It must be said that both of these sources of information are directed towards professionals rather than litigants. Both require the payment of annual subscriptions.

QUESTION 2

What are the different categories or classes of ATE insurance which they are offering?

12. I shall use the term category to refer to the types of risks covered and the term class to refer to the type of cases covered. There are two main categories of insurance: Conditional Fee Insurance, (CFI) and Both Sides' Costs Insurance (BSC). Each category is capable of almost infinite variation. CFI will invariably provide cover for the opponent's costs and the insured's solicitors' disbursements other than counsel's fees. That said, such policies may or may not cover own counsel's fees and adverse orders for costs made at interim hearings. The conditional fee agreements which the CFI supports may or may not require the insured to pay a success fee to his solicitor and/or counsel. BSC provides cover for adverse orders for costs and also for the insured's solicitors' costs and disbursements (with or without counsel's fees). It is also possible to obtain a hybrid category, ie, a policy which covers adverse orders for costs and also a proportion of the insured solicitors' costs. In theory these categories could equally apply to insurance taken out by defendants. In practice, most insurance is taken out only by claimants, and therefore, the rest of this report will be confined to insurance taken out by claimants.

13. As to classes of insurance, some of the claims management companies supply the same policies for all personal injury claims which have a prospect of success which exceeds 50% and in which there is a prospect of recovering damages exceeding £1,500. The Accident Group Limited which states that it is the market leader, issues CFI policies under which the current premium is £997.50 (including Insurance Premium Tax, IPT). Another major claims management company, Claims Direct, issues BSC policies in which the current premium is £1,569 (including IPT). In their written submissions on the original questions both of these ATE providers vigorously defended the appropriateness of block rating personal injury claims and state that they in fact sell the majority of ATE policies sold in this country.

14. Most other ATE providers classify personal injury claims in at least two ways: different premiums are quoted for fast-track cases, and for multi-track cases; each of those classes is further sub-divided into different types of personal injury claim. For

example, under the Law Society approved Accident Line Protect Scheme (sold by Abbey Legal Protection Limited) the current premiums (including IPT) for different classes of CFI are as follows: road accident claims, (RTA), £315 fast track and £693 multi track; occupational disease £892.50 fast track and £3,045 multi track; other claims £682.50, fast track and £2520 multi track. All of the policies mentioned above, ie, Accident group, Claims Direct and Accident Line Protect, are issued prior to communicating to the proposed defendant or his insurer. All of these policies are issued at these premiums for all litigants whose cases are accepted; no distinction is made between litigants who have borderline cases or litigants who have very strong cases.

15. In order to investigate the issue of policies which block rate all personal injury claims I raised some supplementary questions about them. None of the answers I received suggested that such policies were inherently wrong. It is true that some of the major players (eg Abbey) do differentiate between types of claim and it may be that, in time, all ATE providers will have better claims statistics which will compel them all to differentiate. However, I am persuaded that that time has not arrived yet.

16. Policies which do not differentiate between cases which are strong and cases which are borderline are characteristic of those insurers who give delegated authority to solicitors admitted to their panel (see further, below, QUESTION 10). It is often a requirement of such policies that they are issued before sending a letter before claim to the intended defendant. By these means the ATE provider seeks to obtain a wide basket of cases. Including many good risk cases will lower the number of claims later made. An all-in approach also reduces the administrative cost of risk assessment. There is also the point that risk assessment at the outset of proceedings may well be imprecise or unreliable.

17. As well as noting the different categories and classes of insurance it is necessary to observe also that there are two different schemes; standard off the peg policies issued to all cases within the same class (see for example Abbey and The Accident Group); and one-off insurance policies (eg policies issued by more specialist ATE providers such as Saturn). Premiums are lower in standard policies than they are in one off policies. This is because the most difficult cases and therefore the higher risk cases are likely to gravitate towards one off insurance policies (although, it is not proven before me to what extent this is true of RTA cases). The most difficult cases are also the ones in which the solicitor will be reasonably entitled to a higher than average success fee.

18. I asked a series of supplementary questions and further questions about different types of policy in an attempt to identify what if any extra cost is involved in issuing policies which cover all classes of personal injury claim. For example, what percentage of the cases insured by an ATE provider such as The Accident Group are RTA cases or other cases and, with each class, how are they subdivided between fast track cases and multi track cases. I had hoped that the answers to these questions would give me some insight into how much extra it is reasonable to charge for an all risks policy. In fact the information produced (for which I am most grateful) does not enable me to do that.

QUESTION 3

What is the standard or average premium for the different classes or categories of insurance?

> ***(a) If the insurance is taken out prior to communicating to the proposed defendant or his insurer?***
> ***(b) After the proposed Defendant or his insurer has indicated whether the claim is to be contested?***
> ***(c) After the conclusion of the protocol period?***

19. For several reasons it is not possible to state standard or average premiums for different classes or categories of ATE insurance. The industry is still immature and its results over several years have been uniformly poor. Premiums have undergone several major increases over those years. The range of projects offered by the industry and the details of the profit costs and disbursements they cover are both extremely varied.

20. In FOIL's submission the wide range or premiums on offer is evidence that there is no true market for ATE insurance. If there were, the market pressure would ensure that the premiums on offer were broadly in line with other products that offer the same model of insurance cover. FOIL argues that the published prices of ATE insurance's products show that this does not occur. On the contrary, it argues that the absence of alignment of similar products arises from the fact that there is no pressure whatsoever on the ATE providers to be competitive on price with their rivals. Without this pressure, the premiums publicly quoted are, it submits, a flawed basis from which to judge the reasonableness of the range. APIL challenges FOIL's argument. In their submission wide ranges of premiums feature in other (established) areas of insurance, for example motor insurance. On balance I accept what FOIL says on this. There may well be strong competition between underwriters to supply compulsory insurance schemes and between different other ATE providers selling standard insurance schemes or one off policies to different solicitors or solicitor groups. However, I am not convinced these market forces impinge upon the premium levied to the ultimate consumer and claimed by him from his unsuccessful opponent.

21. A large majority of ATE insurers and also the Appellants (in their oral submissions) urged me not to contemplate favouring or imposing a range of standard premiums. The ATE providers fear that, however carefully expressed to indicate judicial discretion, any such guidance will be applied inflexibly and will effectively cap the premiums charged. If that cap does not reflect the commercial realities of the ATE market place the market will disappear. That said, some ATE providers gave guarded support to some actual figures which I suggested in my draft report.

22. The opposition to guidelines expressed by the Appellants derives from their grave disquiet as to the course of this Inquiry (their position changed on seeing the judgment in Callery v Gray). Giving guidelines would amount to conducting hypothetical detailed assessment without hearing real arguments or evidence as to the policies being assessed. In written submissions made by Temple (via counsel for the Respondents) it is argued that a regime of standard premiums would inevitably lead defendants to challenge any premium said to fall outside the appropriate standard premium parameters. This, it argues, would inevitably deter insurers like Temple from even contemplating insurance for non-standard risks. It states that the ATE market is sufficiently competitive and difficult that insurers are unlikely to insure a risk where there is a high probability of the premium being disputed (a dispute that is itself costly and almost certainly unrewarded). Elsewhere in its submissions Temple states that the court should not arrogate to itself the functions of a financial regulator of the insurance industry.

23. I accept that now is not the time to publish guideline figures for ATE premiums but I expect that, fairly quickly, courts conducting detailed assessments will develop individual benchmark figures for major providers such as The Accident Group and Abbey.

If taken out prior to communicating with the proposed defendant or his insurer

24. A search of www.thejudge.co.uk conducted by APIL shows the range of RTACFI to be £210 to £1,050 for the fast track and £210 to £1,837 for the multi track. These figures which are inclusive of IPT are for policies which have differing limits of indemnity. The £210 premiums are for AMICUS policies which have a limit of indemnity of £100,000. The £1,050 premium is for a Wren policy and the £1,837 is for a Temple policy (which is described further in para 65, below) both of these policies have a limit of indemnity of £50,000.

25. An ATE provider who requests anonymity describes a fair premium rate for RTA personal injury claims as 6% to 12% (including IPT) based on the level of insurance cover required. In most cases the minimum rate would apply subject to a minimum amount of premium. The 6% rate would produce a premium of £945 (including IPT) for cover of £15,000. This appears to be somewhat higher than the rate which most ATE insurers apply for RTA cases.

After it has been indicated that the claim is to be contested

26. The anonymous ATE provider just mentioned would recommend a premium of 12% of the amount of insurance cover required, but states that the defendant's decision to contest the claim would be a vital factor in whether the insurer would accept the insurance proposal. Other ATE providers make similar points, for example, DAS (the premium should double), X L Brockbank (the premium should double or treble). Other insurers (eg Keystone) and APIL take the view that many insurers would consider each such case on merit only and may well decline to offer cover

once there is a clear indication that the defendant would fight the claim. Alternatively, limited cover might be offered on very expensive terms, eg, 15% of the amount of cover required. Temple states that if "it is clear that the case would be contested" the premiums will be considerably higher than usual; however, a "clear contest" will lead to cover being refused in approximately 70% of cases. I infer from this that Temple, and perhaps, other ATE providers, draw a distinction between court proceedings which are being vigorously defended and court proceedings in which the claimant is merely being put to proof of his claim, possibly as a delaying tactic. Vigorously defended proceedings have less chance of reaching a negotiated settlement. It is said on behalf of the ABI that the distinction these providers draw is out of date: it harks back to a pre-CPR era before the pre action protocol existed. They say that insurers' claims handling systems are now geared to meeting protocol deadlines in order to settle claims as quickly and as efficiently as possible.

27. Several submissions dwelt upon the long term effects of the decision of His Honour Judge Halbert in the case ***Sarwar v Alam***. That case concerned a road accident claim in which the claimant was a passenger in the defendant's car. The claimant was disallowed the cost of the ATE insurance he had taken out because the Defendant's motor insurance provided before the event (BTE) insurance not only for the defendant but also for his passengers. Some commentators may wish to dispute that the Judge was right to treat the existence of such insurance as something which the solicitor in that case should have anticipated or dispute that the BTE insurance in that case was suitable for the claimant. However, whether the learned Judge was right or wrong on those points it should now be accepted that, unless the case is reversed on appeal, in future, solicitors will have to increase the enquiries they make about existing insurance cover. If that is right this case poses two problems for ATE insurance providers. First, in claims by passengers against drivers, the need to undertake enquiries will postpone the date of issue of the ATE insurance. The case restricts the ability of providers of compulsory insurance schemes to insist that policies be taken out at the outset (see para 16, above). Secondly, the potential for growth of BTE insurance shown by this case may cause immense instability for the ATE insurance providers. The size of the ATE business may diminish so forcing premiums higher. The increasing premiums and the need to make enquiries will encourage more claimants to dispense with insurance altogether, so exacerbating the problem.

28. Other aspects of ***Sarwar v Alam*** which have been dwelt upon at some length in several of the submissions I have received are as follows: a fear which some ATE insurers express that the volume of BTE cover is likely to be increased by one section of the insurance industry (liability insurers) mainly for the purpose of destabilising and destroying another section (the ATE insurance): and arguments about the independence of solicitors acting for BTE insurers and the possibilities of conflict if the same insurer covers both claimant and defendant. Counter submissions have been made and I have been taken to Regulations 4 and 5 of the Insurance Companies (Legal Expenses Insurance) Regulations 1990. Interesting as these topics are I am in no doubt that the submissions I have received upon them are not matters which should

influence my report. They are not relevant on questions concerning the reasonableness of premiums.

After the conclusion of the protocol period

29. Several of the submissions do not distinguish between the commencement of court proceedings and the declaration by a defendant that the claim is to be contested. The willingness to write policies after the commencement of court proceedings must be set against the unwillingness to offer cover at all in contested cases.

QUESTION 4

What does the premium cover?

30. In most if not all off the peg policies the limit of indemnity cover will be standardised; £25,000, £50,000 or £100,000. Several ATE providers argue that the vast majority of cases will not require this level, but a reduction of it would not substantially affect the premiums (see "burning cost" in para. 36, below). Having one limit of indemnity keeps the administrative costs down. Also, I am impressed by the argument (raised by Abbey and Litigation Protection Ltd) that it is a basic premise of good underwriting practice that all risks are adequately insured.

31. Most CFI policies provide benefits which are additional to the cover in respect of the other side's costs. Most, but not all, of them are "own cost" benefits. This raises questions of recoverability which will be affected by any decision made by the Court of Appeal on 24 July 2001. The list of additional benefits I will consider in some detail is as follows:

(a) own counsel's fees;

(b) other disbursements (such as court fees and own experts' fees);

(c) cover for appeals

(d) liability for costs following an offer to settle or Part 36 payment

(e) option to buy "top up cover" later at the same premium rate;

(f) interest foregone on deferred premiums;

(g) full indemnity in respect of the premium if the claim is lost;

(h) partial indemnity in respect of the premium if the full premium is not successfully recovered;

(i) any premium loading because of the claims record of the insured's solicitor;

(j) interest payable on disbursement loans where the claim fails;

(k) advice and help supplied by claims managers.

32. As to most of these benefits I have raised supplementary questions as to their recoverability and also enquired into the percentage of a premium which it would be fair to attribute to all or any of them. My purpose in asking these questions was to identify if I could a fair discount to make if any of these benefits were included in the policy and are to be regarded as irrecoverable from an opposing party ordered to pay costs. Guidance on values would also be of use when comparing different policies which offered different benefits. The third, fourth and final items in the list above were not included in my supplementary questions but were raised in submissions thereon. They indicate that a list such as this can never be exhaustive. The ability of the industry to create new additional benefits, whilst not infinite, is extremely great.

33. In their submissions the Appellants challenged the recoverability of all of these benefits not only on the grounds that they were "own costs" benefits but also on the ground that, by purchasing a policy with some or all of these benefits, the insured is purchasing more than just insurance. They place reliance upon the House of Lords decision in ***Dimond v Lovell*** [2000] 2 WLR 1121. The opposing argument is that that case is a ruling on damages only and is therefore irrelevant on this question of costs. I am invited instead to concentrate upon the wording of Section 29 and upon the definition of "insurance premium" in CPR rule 43.2(1)(m). The Appellants also rely on those provisions and place emphasis on the words "insurance [policy] against the risk of incurring a liability in [those] [the] proceedings". In my view the provision of the benefit by way of an insurance contract does not by itself make the cost of the benefit recoverable. In my view I ought to look at each benefit in turn and decide (subject to the "own costs"question) whether it is an item of legal expenses insurance, or is of and incidental to such insurance, or whether it is an extraneous benefit in respect of which some discount should be made. I am in no doubt that a discount would be appropriate in the case of policies which rewarded each insured with valuable gift tokens, discounts on holidays purchased or similar benefits. I note from a Datamonitor report submitted to me by one interested party a suggestion that at least one case management company offers customers a free telephone help line for advice on any legal question. It seems to me that there is no difference in principle between this benefit and the gift tokens mentioned above but there may obviously be a difference as to the size of the discount appropriate. If the take up rate for a legal telephone helpline were extremely small the cost to the insurer per policy would be negligible.

34. Working through the list of additional benefits I shall, as promised in paragraph 8 above, endeavour to identify the reasonable cost of the item expressed as a percentage of the premium. There are three comments I must make about that by way of explanation and introduction.

(a) Many interested parties deny that I have received sufficient information and argument in order to make such assessments. While I accept that that is true I doubt whether, on these topics especially, any court conducting a detailed assessment would be given more information than I have received. Costs Judges are frequently left to "do the best they can" on sketchy information.

(b) The discounts I shall identify assume a policy which contains most if not all of the additional benefits listed and no others. Although I shall look at each one separately I believe that, when conducting a detailed assessment, the court should take the so-called broad-brush approach, ie, value the collection of relevant items as if they were a single item rather than a collection.

(c) Before embarking upon this task it is convenient to report on the next question. My report on the additional benefits therefore begins in paragraph 41.

QUESTION 5

How are premiums in general terms calculated?

35. Several ATE providers identify four main elements in the calculation of the premium: the burning cost, the risk/profit cost, the administrative costs and the distribution commission.

36. The burning cost is the frequency of loss (ie. the percentage of policies in which a claim is made) multiplied by the average cost of each claim. If the frequency of loss is 10% and the average cost of each claim is £3,000, the burning cost in each policy is £300. These figures are given for illustration only. They are not intended to represent real figures. Their inclusion in my draft report caused one interested party to describe them as overly optimistic and another interested party to say that, in its opinion, the real figures are 20% and £2,000 (ie a burning cost of £400). £400 exceeds the cost of several total premiums quoted to me.

37. The risk/profit cost is the sum to represent the profit looked for by the underwriter and also a safety margin for the underwriter should the cost of claims become higher than the burning cost predicted. There is much dispute about how this should be calculated. Abbey suggests that it is usually calculated as 25% of the burning cost. Litigation Protection Ltd suggests that this approach massively under-estimates the underwriter's costs and ignores altogether reinsurance costs. They suggest a figure nearer 40%. The Appellants submit that it should be calculated as a percentage of the premium income. They then give various worked examples in which the largest underwriting profit shown is 10% of the gross premium. X L Brockbank and NIG give it as their opinion that a 10% profit margin is, in all the circumstances, ludicrous.

38. The administrative costs cover items such as personnel, premises, policy issue and processing and claims administration. What if any advertising cost should be included as administrative costs? I shall deal with this question in paragraphs 59 to 63.

39. The distribution commission is a sum payable to brokers and other intermediaries. As with the first two ingredients there is much dispute as to the amount of commissions normally found. I shall give further details when reporting on the answers to Question 6 (see para 52, below).

40. FOIL and the Appellants argue that the distribution commission, although properly regarded as a constituent element in premium calculation, is not something that can be legitimately claimed from an opposing party ordered to pay costs.

> *" ... as it is purely a commercial arrangement between the contracting parties." (FOIL)*
>
> *"The court ... is respectfully reminded of paragraph 11.10 of the Costs Practice Direction. Costs Judges assessing the recoverable premium should obtain details of any commission paid or payable and exclude this from the premium to be paid by the losing party." (Appellants)*

In my view the arguments raised by FOIL and the Appellants on this point are not correct. I do not think the Practice Direction provision referred to should normally lead the Costs Judge to disallow the whole of any commission included in a premium. The paragraph lists "the amount of commission payable" as one of the factors to be taken into account in deciding whether the cost of insurance cover is reasonable. This factor like the first two mentioned in the paragraph (a comparison with other funding arrangements and the level and extent of cover provided) describes matters of degree not items for deletion. Thus, if distribution commissions amounting to, say, 10% of the overall premium were the insurance industry's standard, the Practice Direction enables the Costs Judge to require a receiving party to justify a commission payment exceeding 10%.

41. In the next ten paragraphs I will comment upon each of the additional benefits listed in para 31, above.

(a) Own counsel's fees
(b) Other disbursements (such as court fees and own experts' fees)

42. There can be little doubt that these are ordinary items of legal expenses insurance and therefore a discount in respect of them will be appropriate only if it is ruled that the own cost element of CFI policies is irrecoverable (see further, para 8, above). In my view, in a claim which fails, the reasonable costs incurred by the claimant on counsel's fees and other disbursements are unlikely to exceed one half of the total costs payable to the opponent. Accordingly, they comprise less than one third of the burning cost of a policy covering both of them. Bearing in mind the other ingredients in gross

premiums, the discount should not exceed 20% of the total. If, as is more usual, the policy does not cover counsel's fees but does cover other disbursements, the discount would be nominal, a few pounds.

(c) Cover for appeals
(d) Liability for costs following an offer to settle or Part 36 payment

43. As with the first two, these two are pre-eminently ordinary items of legal expenses insurance. I do not have sufficient information to make any attempt to value these benefits. I suspect that the reasonable cost of (c) would be negligible but the reasonable costs of (d) would be substantial. It should be noted that these two items, unlike the first two items, may not be limited to own cost protection: they may include protection in respect of the other sides' costs.

(e) Option to buy top up cover later at the same premium rate

44. This item, like the first four listed, seems to me plainly a standard ingredient of legal expenses insurance or at least is plainly of and incidental to such insurance. Like the last two listed it may well comprise protection not only for own costs but also in respect of the other sides costs. Top up cover is the subject matter of Question 8. Such cover is not normally needed in standard insurance policies (see further, para 30, above). I have received no information upon which I could base any attempt to put a value on this benefit. Presumably one would have to start by trying to identify as at the time the policy was taken out, what premium rate would the insured anticipate as payable had he not had such an option and then try to identify what was then the reasonable likelihood of his needing to exercise the option.

(f) Interest foregone on deferred premiums
(g) Full indemnity in respect of the premium if the claim is lost

45. These benefits are to be found in virtually all off the peg insurance policies. Several ATE providers submit that their inclusion in the policy makes the policies cheaper. In their submission many litigants would be strongly discouraged from litigating and from buying insurance if they had to pay the insurance premiums at the outset or if they had to risk paying them (or part of them) later. Of those who do proceed to litigation the litigants least likely to buy insurance would be those who have the strongest cases. From this it is argued that (subject to the ruling upon the own cost question) allowing recovery of these items falls within the policy underlying the new legislation. This is a matter discussed in para 99 of the Court of Appeal judgment (note especially para 99 (viii)). The opposing argument is that the "no win no fee" principle which applies to profit costs and counsel's fees does not apply to insurance premiums. The new legislation replaces the old legal aid regime. Under that scheme it was expected that there would be "legal aid only" items payable by the claimant out of his compensation. It is said that claimants in the new regime should similarly expect to shoulder the cost of premium loss cover. There are other items in

the new law which they must shoulder, eg, the fee deferment element of a success fee under a CFA (see CPR rule 44.3B(1)(a)). In my view if the legislative policy does not justify the recovery of these items, the effect they are likely to have on most prospective claimants is such as to make the discount appropriate to them zero. However, I note that, in some policies premium loss protection is available on payment of a substantial sum (see, for example, the premiums quoted for the following policies issued by Litigation Protection Ltd, "conditional fee protection plan" and "conditional fee protection plan plus".

(h) Partial indemnity in respect of the premium if the full premium is not successfully recovered

46. This benefit covers the insured who obtains an order for costs against his opponent but, on detailed assessment, part of the premium is disallowed as unreasonable or the whole premium is disallowed as unreasonable because, for example, of some pre-existing cover which the claimant had. The benefit sometimes takes the form of a ring fencing of some of the damages recovered.

47. This benefit clearly provides own costs protection and therefore a premium containing it is at risk of discount on that score. In my view a discount should be attempted in any event. I do not think the legislative policy argument sought to justify the last two items can be extended to this item. This item protects the policyholder against the risk of loss of taking out insurance which, if he has or might have taken it out, would not have been recoverable from the opposing party. In my view this item is best regarded as extraneous to the legal expenses insurance contemplated by Section 29.

48. It should be noted that the value of this benefit increases in proportion to the unreasonableness of the sum unrecovered. As to valuation the only information I am aware of relates to the increase in premiums made by Claims Direct (a BSC insurance provider) when it decided to ring fence the first £1,000 of compensation payable to customers who take out the new policy. In the Datamonitor report referred to above (see para 33) the increase is said to have cost over £200 per policy (ie, over 15% of the old premium).

(i) Any premium loading because of the claims record of the insured's solicitor

49. Whilst the cost of this benefit may have to be discounted as an own costs protection, most parties and interested parties submitted that it should be discounted in any event if it can be identified. Like (h) this benefit has a spiralling effect: the worse the solicitor's claims record appears to be the greater the cost of insurance. Presumably, it is to be excluded as being extraneous to ordinary legal expenses insurance. Several ATE providers commented that rather than load a premium because of perceived incompetence by the solicitor, the insurer should not issue the policy in the first place. Indeed, most of the major players operate through panels of solicitors and, presumably, a firm's membership of a panel can be restricted. I am aware that at least one provider

does require solicitors to complete a comprehensive proposal form giving details about the firm's past litigation experience and losses.

> *"This enables us to try to match the right premiums to the firm and that firm's profile of risks. We ask the Court to not take that ability away from us. The solicitors who have a very low rate of claims against the ATE policy have been snapped up (unfairly we believe) by [other providers]."*

Two other interested parties point out that it is wrong to suggest that a poor claims record reflects poor levels of competence. The claims record is more likely to reflect the type of case taken on. Both of these parties state that it would be contrary to the public interest to discourage solicitors from taking on worthy cases which might adversely affect their claims record. This would mean that potential claimants might be unable to pursue their cases or at least be unable to pursue them with the solicitor of their choice. In my view the public interest they identify (and which I accept) would not justify the recovery of the cost of this benefit. The same public interest element arises in respect of the operation of panels of solicitors.

(j) Interest payable on disbursement loan where the claim fails

50. Many interested parties, including APIL and several ATE providers concede that it is necessary to discount a premium for a policy including this benefit whichever way the ruling as to own costs element goes. This benefit is extraneous to legal expenses insurance. It relates more to funding costs. I am unable to give guidance on valuation save to say that, in some policies, a price for it may be shown separately. If it is not, it would presumably be necessary to take into account the following factors as they reasonably appeared to be at the time the policy was taken out; the likely rates of interest, the size of the loan in question and the likely duration of the proceedings and the risk of loss.

(k) Advice and help supplied by claims managers

51. The work done which I have in mind is work done handling and negotiating the claim (whether or not it duplicates what the solicitor may do), and work done to comfort or reassure the insured and/or his family (eg practical help in the home, counselling, helping in the arrangement of business matters and accompanying the insured on hospital appointments and other appointments). In my view these benefits are extraneous to legal expenses insurance and a substantial discount on the recoverable premium should be made in respect of them. I have received no information or valuation of these services so far as CFI policies are concerned. This will have to be valued on a case by case basis but, in respect of major ATE providers, benchmarks will no doubt develop quite quickly.

QUESTION 6

Of the premium, what percentages are attributable to, administration, advertising and other matters?

52. Most of the ATE providers who answered this question have sought confidentiality as to their answers. Several of them have given me very specific details of commercially sensitive information including the amount of risk premiums paid and their commission arrangements. I will not of course repeat that information and, indeed will strive to maintain the confidentiality claimed for it. In respect of Question 6 there are five matters upon which I must report: definition of premium, expenses and commissions, assessment fees, referral fees and advertising.

Definition of premium

53. In my view the premium to be assessed by the Court is that sum paid or payable by the litigant. The sum to be allowed should include (to the extent that they are recoverable and reasonable) the four main elements identified in para 35, above: the first two (burning cost and risk/profit cost) comprise the pure risk premium and are usually retained by the underwriter; most if not all of the work of issuing policies, supervising the conduct of cases and handling claims will be dealt with by brokers and other intermediaries. Thus they will receive most but not all of the administrative costs and of course their commissions. The total sum paid or payable by the insured is the sum upon which insurance premium tax (IPT) is calculated.

Expenses and Commissions

54. I have been given a copy of the ABI Insurance Statistics Year Book for 1989-1999 (the latest available) and have been invited to consider four tables setting out average commission and expenses ratios for certain types of insurance. The figures for commissions and expenses which I am about to quote are expressed as percentages of the retained premium, ie, that part of the gross premium which is net of reinsurance. For 1999 the commission and expenses ratio for each of the following types of insurance are shown as follows:

UK motor insurance	24.1%
UK accident and health insurance	37.4%
UK general liability insurance	35.8%
UK property insurance	37.3%

55. Having now received submissions from other interested parties (in particular, the Accident Group, Claims Direct and DAS) I do not accept that statistics such as these are a useful yardstick to apply. No statistics have yet been given for ATE insurance and I am told that, as a specialist sector of the market, the commission and expenses ratios are likely to be much higher. I am invited instead to treat as a comparable the "extended warranties" market where, it is said, commission and expenses ratios often equal or exceed 70% of premium. Other specialist areas which are not

included in the statistics are said to be "creditor premiums" and legal expenses insurance which, I am told, have rates much higher than those shown in the Yearbook.

Assessment fees

56. In policies issued with the delegated authority of the insurer (see Question 10) the risk assessment will be made by the solicitor not the insurer and the insurer can therefore make no charge for it. In other cases the underwriter, or, more likely, an intermediary, will make a risk assessment. The cost of that assessment may be included in the premium (when it will bear IPT) or levied as a separate assessment fee. In the latter case the fee may attract VAT. In my view, although such an assessment fee is not a premium, the insured can recover it (subject to assessment) under an order for costs if it is a fee paid or payable by him. The reasonable cost of the policy is itself recoverable. In my view reasonable costs expended in obtaining such a policy are of and incidental to it. I would apply the same approach to time spent by the solicitor in completing the proposal forms and obtaining the policy and also to time spent in complying with policy terms (eg reporting matters or obtaining authority to reject an offer to settle or Part 36 payment). The compliance work must not, of course, be extraneous to the policy.

Referral fees

57. The overwhelming majority of parties and interested parties agree that referral fees paid by a solicitor to the ATE provider are not recoverable as such by the solicitor from his client and therefore by the client from an opposing party. The cost to the solicitor is a typical overhead expense of his firm. They replace or comprise part of any budget the solicitor has for advertising and marketing. Being part of the solicitor's overhead costs, it will form a legitimate component in the calculation of hourly rates by that solicitor.

58. Another, and much more contentious, use of the expression "referral fee" is in the context of fees paid by ATE providers to claims managers. The cost of these fees will be passed to the insured as part of the gross premium he must pay. In my view that part of the premium which is fairly attributable to work which is extraneous to the legal expenses insurance is not recoverable (see further para 51, above). It is immaterial whether the work is done by an agent of the claims management company or by an employee.

Advertising

59. Many submissions have been made to me in answer to Question 6 and a supplementary question I raised about this topic. There is a perception that some market leaders in ATE insurance spend far more than is reasonable on advertising the products they sell. In fairness to the persons attacked, such as The Accident Group, I think I should spell out more exactly what is being said against them.

(i) Abbey acknowledges that it is perfectly reasonable to include in the premium an element for marketing and advertising but implies that the absence of controls may cause advertising budgets to spiral towards infinity.

(ii) APIL express the belief that that part of a premium which is attributable to:

> *"large commissions on sale to the client and the cost of marketing cases (claims farming) should be stripped out from the premium and should not be recovered. Otherwise all insurers could add this to their premium and could all run expensive television advertising campaigns, all ultimately paid for by the liability insurers."*

(iii) The Appellants, like Abbey, accept that:

> *"a reasonable premium will include a <u>modest</u> percentage in respect of commissions and other payments to brokers and intermediaries, including payments for advertising. However excessive or disproportionate percentages should obviously be irrecoverable. Given the widely differing amounts currently being spent it would not be appropriate to allow or disallow a set percentage in all cases. Rather, a view should be taken now as to the current average percentage in a range of reasonable premiums and that percentage not exceeded when assessing maximum guideline premium figures."*

60. The converse case is put by The Accident Group and Claims Direct. One denies a point (which I do not think has actually been alleged) that any slice or percentage of its premium is calculated specifically to raise an advertising budget. Both emphasise that advertising is a legitimate part of any insurance business and both suspect that the accusations made are:

> *"prompted by the commercial ambitions of our competitors. The small ... providers have every reason to claim that they can prosper without heavy advertising or marketing overheads; they fail to acknowledge that the very market in which they operate has very largely been created, at no cost to them, by the big providers ... the smaller providers are now looking to increase their market share at the expense of those who have created it."*

61. I have set out the arguments as fully as I can so as to enable the Court of Appeal to take this issue from me and make their own ruling upon it if they so wish. I respectfully record here my own view that the court has neither the jurisdiction nor the means by which to regulate the advertising budgets of insurers. If regulation is needed it must be extra judicial regulation. I respectfully suggest that the proper function for the court when deciding questions of reasonableness concerning insurance premiums, is to consider the conduct of the insured, not the conduct of the insurer. In other words the proper question to ask is whether the choice of policy made by the insured was a

reasonable one. If it was the premium paid or payable is recoverable (possibly subject to certain deductions such as those described above). A choice may be regarded as reasonable even if the insured did not in fact make the best choice available.

62. There is however another aspect to the advertising issue which may merit a reduction in premium recoverability. There are two pre-requisites to the case which I have in mind:

(i) the policy in question must have been issued by an ATE insurance provider who, at the time of issue, conducted a high volume advertising and marketing programme in order to attract customers; and

(ii) the court must have already decided to make a substantial reduction in the premium recoverable on the basis that it included substantial extraneous benefits, including the non recoverable benefits of work done by a claims manager or the like.

63. I respectfully suggest that the premium to be allowed should be further reduced to take account of the fact that the advertising costs recouped in the full premium are properly regarded as attributable not only to selling the standard insurance products but also to selling the disallowed extraneous benefits. In the likely absence of evidence of the cost of advertising per policy I would make the reduction the same as the reduction in respect of the extraneous benefits.

QUESTION 7

Is it practicable to obtain a policy in which premiums are rebated in the event of early settlement and are there any policies on the market which provide for this?

64. The existence or non-existence of rebates is one of the factors listed in para 11.10 of the Costs Practice Direction to be taken into account when considering the reasonableness of insurance. However the general consensus of most interested parties, including ATE providers, APIL and FOIL is firmly against rebates of premium on early settlement. Such a scheme runs counter to the calculation of "burning cost" explained in paragraph 36 above. If such policies were introduced it would be necessary to increase the premium in every policy in order to provide for a rebate in some of them. Such a system would also give rise to increased administrative costs and, for the insured or his funder costs increased funding charges. Some parties are unaware of any such policies. Some parties report seeing such policies in some commercial cases. Litigation Protection Ltd makes the point that rebates would become viable only in exceptional cases involving very large amounts of indemnity and accordingly a very high level of premium. In RTA claims the average costs of claims rarely exceeds £15,000.

65. There is in fact a CFI policy (issued by Temple) which is applicable in RTA cases and which has a three-step premium, ie, a premium the amount of which

depends on the procedural stage reached by the time the case is concluded. The first stage covers the period up to issue of court proceedings. The second period covers the stage from there to a date at least 45 days before trial. In cases which conclude at stage 1 or stage 2 the policy has a limit of indemnity of £25,000. In cases which do not conclude until stage 3 the highest premium is payable and the limit of indemnity is £50,000. The advantage to the insurer of a reduced limit of indemnity in the earlier stages is obvious. The advantage of the three step premium to the insured is not obvious to me given that the policy includes premium loss protection.

QUESTION 8

What are the advantages and disadvantages of policies permitting the purchase of further cover as a claim proceeds?

66. Most interested parties felt that the disadvantages would outweigh the advantages. The position is clearly stated by the Law Society whom I quote in full:

> "Some policies permit the purchase of further cover as the claim proceeds. It may be that in these cases the cost of the initial cover may be less than if cover is purchased for the maximum reasonable exposure for costs. The disadvantage is that the inception of further cover at a later stage will require reference back to the ATE insurer. There is unlikely to be any guarantee that further cover will be provided. It is likely that the provision of an initial amount of cover followed by the provision of further cover when a claim has not settled at an earlier stage would be considered to be high risk to the insurer. Insurers may fear that claimants will only take out the further cover if the case becomes more complex and more risky. The cost of further cover may therefore be expensive. The <u>overall</u> cost of insurance under a model of this sort is likely to be greater than at present because of the administrative costs involved in giving individual consideration to "second stage" cover."

It was in relation to this question that Litigation Protection Ltd made the remark I quoted in para 30 above that it is a basic premise of good underwriting practice that all risks are adequately insured.

67. Two interested parties made submissions which run in favour of "top-up cover", FOIL and Greystoke. As to FOIL I respectfully doubt that the advantages they list do in fact outweigh the disadvantages they note (higher administrative costs for the ATE insurer and the need for more detailed explanation of the policy by the solicitor). I shall state my doubts alongside each of the advantages listed.

(a) Ensures that the amount of cover at any stage of the case will relate more closely to the extent of the risks involved (this runs counter to the burning cost principle explained in paragraph 36 above).

(b) Encourages the defendant to settle claims where appropriate before the level of premium increases (this assumes that the claimant informs the defendant of the limited cover bought so far; such a disclosure might encourage the defendant to sit tight until the cover was exhausted).

(c) Reduces the scope for dispute between the parties in respect of the quantum of the policy taken out (so would not taking out any insurance at all).

However, I do find merit in FOIL's suggestion that ATE insurers will not be disinclined to provide further cover unless of course the merits of the claim have substantially deteriorated: they point out that if a claim now has no reasonable prospects of success the insurer would be entitled to cease cover even if a large limit of indemnity had been taken out originally. Nevertheless, it seems to me reasonable for an intending insured to take out adequate cover from the outset of the policy. Delay will not bring peace of mind and, if the defendant is aware of it, may encourage the defendant to play a waiting game. Cover bought late is almost bound to be more expensive than if it had been bought at the outset (cf the policy described in para 65, above).

68. The written submissions made on the original questions by the ABI included a copy of the BSC comparison chart published in "Litigation Funding" in January 2001. The chart covers 11 ATE providers. In answer to the question "can limit of indemnity be topped up later?" the answer most frequently given is "yes, subject to approval". The exception is at Greystoke where the answer given is "yes, guaranteed option available". In Greystoke's written submissions on the original questions a brief explanation is given of their "Lawassist starter policy". I am told that, for a premium of £175 plus IPT for RTA cases, the initial level of cover is sufficient to investigate the case up to settlement during the protocol period. "If the limit of indemnity is exhausted without the claim being resolved, then it is possible, subject to the continuing merits of the case, to obtain additional ATE cover under our standard Lawassist ATE policy with the option to increase that additional level of indemnity at a later stage." So far as I am aware no other insurer offers a similar policy. This policy is not mentioned in the Litigation Funding comparison chart mentioned above but is mentioned in the search result produced to me by APIL from the website www.thejudge.co.uk. I presume that a policy such as this would find favour with the liability insurers. If it thrives it may well solve some of the problems raised in this Inquiry. However, it is, of course, too early to know whether it will thrive. The policy is a form of BSC although, because it covers the pre issue period the question of adverse costs orders does not arise. A CFI version of this policy (which presumably would cover little more than experts' fees) would be even cheaper.

QUESTION 9

How is the insurance marketed or sold?

69. ATE policies are sold to policyholders in two main ways:

(i) via firms of solicitors throughout the UK, and

(ii) via various claims agencies including claims management companies.

In (i) the solicitor meets the intending insured first and introduces him to the insurer. In (ii) the claims agency or claims management company meets the intending insured first and introduces him to a solicitor. I use the term claims agency here to refer to organisations which simply act as the advertising arm of the solicitors they deal with. Claims management companies may investigate and screen cases to a greater or lesser extent and provide supervision and a point of contact for the insured/claimant throughout the litigation (see further, para 51). Some claims agencies and claims management companies charge membership fees and referral fees to the solicitors they deal with (see further, paras 56 and 57).

70. In paragraph 20, above, I have referred to FOIL's submission that there is no true market for ATE insurance. It does seem fair to say that, with policies sold via claims agencies and claims management companies, the intending claimants do not shop around on the basis of premium. Moreover, in those cases and in cases sold via solicitors, clauses in the policies which indemnify the insured for the loss of the premium itself removes any incentive for that insured to seek a reasonably priced policy.

71. In its submissions, Abbey draws attention to the solicitor's professional duties, which include an obligation to examine how the claimant's case can be funded. I am in no doubt that a solicitor must not cause a client to enter into an arrangement which he knows to be unsuitable and must not negligently overlook other forms of funding (eg existing legal expenses cover which the client may have). However I respectfully doubt whether, in cases in which ATE insurance is appropriate, the solicitor must act as an insurance broker advising his client upon the best deal available.

QUESTION 10

Do any insurers give solicitors delegated authority to issue policies, and, if so, on what terms?

72. I cannot improve upon the answer given to this question by APIL which I quote and adopt in full.

"A few insurers give delegated authority to solicitors who have been admitted to their panel. It will almost certainly be a requirement of delegated authority that the solicitor puts all his claims through the system and at the earliest moment – i.e. receipt of instructions. The following insurers offer delegated authority:

- *Abbey Legal Protection with accident line protect relaunched and which came into effect on 1 October 2000. The membership fee is £3750 + VAT. An*

annual fee [and] a £50 referral fee is charged. Members have to put all their CFA cases through the Abbey scheme. This is a common requirement.

- *DAS/ Law Insure*
- *Claims Advance*
- *Law Club Legal Protection*
- *Temple*

Temple has two insurance schemes – one a delegated authority basis and one where premiums are quoted for individual cases. With the delegated authority scheme (which is not available for all cases) the solicitor can issue certificates in respect of any case taken on using a premium table supplied by Temple. The solicitor rates the case and then applies a corresponding premium. Temple also does not interfere with the way in which the case is run leaving the solicitor free to take all decisions."

QUESTION 11

To what extent are the insured and his lawyers affected by the amount of the premium payable;

(a) In cases which later settle (i.e. the great majority of cases)?
(b) If the insured succeeds at the trial?
(c) If the insured is unsuccessful at the trial?

73. Answers to this question did not make much distinction between (a), (b) and (c). The real questions here are who pays for the insurance if the insured loses and who pays in whole or in part if the insured wins. Most considered it immaterial whether the loss or win occurred at trial or before trial.

74. If the insured loses, the insured must pay the premium unless the policy contains an indemnity against such loss (as to which, see further, para 45).

75. If the insured wins, the opponent will be liable to pay the premium to the extent that it is reasonable. If some part of it is disallowed as unreasonable, the insured will suffer the shortfall unless, again, he has some indemnity against such loss (as to which, see further, para 46).

76. Several interested parties have pointed out that the solicitor cannot or, at any rate, should not make any offer to cover any shortfall or loss on premium since to do so would breach the indemnity principle. A breach of the indemnity principle would endanger the recovery of any sum of costs from an opposing party.

77. It is appropriate to repeat here the submissions made by several interested parties that one must not overlook the deleterious effect on most litigants which an

obligation to pay or finance any costs will have. Many litigants, including those with strong claims, would be strongly disinclined to proceed if they had to pay insurance premiums at the outset (most premiums are funded by disbursement loans) or if they had the risk of paying them or part of them later (see further para 45).

CONCLUSIONS

78. The Court of Appeal directions which set up this Inquiry stated that its purpose is "to enable the Court of Appeal to give guidance in its judgment as to the practice to be adopted in future when taking out [ATE] insurance [in RTA cases]." In the light of the information and submissions which I have received I would respectfully recommend the Court of Appeal to consider what if any guidance to give on the following points:

(a) Guidance upon the recoverability of the own cost element in a CFI policy (see paras 8 and 31 to 34).

(b) Whether, in future, further guidance should be published by the Senior Costs Judge after arranging consultations with interested parties from time to time unless and until such guidance becomes unnecessary (see para 3(b)).

(c) Guidance upon the recoverability of additional benefits included in ATE policies (see paras 31 to 34 and 41 to 51).

(d) Whether it is ever appropriate to reduce the amount claimed for ATE insurance because of the advertising policy of the ATE provider at the time the policy was issued (see paras 59 to 63).

(e) Whether to give guidance to Costs Judges and District Judges now conducting detailed assessments in which claims are made for the recovery of ATE premiums (see below).

79. As to the conduct of detailed assessments I conclude by setting out the approach which I would recommend when determining the reasonableness of an ATE premium claimed in RTA proceedings:

(a) The range of variation between policies issued by different providers makes it inappropriate for the time being to think in terms of benchmarks for premiums. However, with more experience of cases, a Judge may develop a sufficient feel to set individual benchmarks for policies issued by the major ATE providers (see para 23).

(b) In the case of a standard "off the peg" policy, a high limit of indemnity does not by itself indicate that the receiving party paid too much (see para 30).

(c) As a general rule the choice of an off the peg policy which covers all risks (eg an accident group policy) can be regarded as a reasonable choice even though other policies limited to RTA cases may have been cheaper (see para 15).

(d) Recent history of the ATE insurance industry makes it reasonable to presume as a starting point that the premium charged is reasonable (subject to any necessary reductions to be made) unless the contrary is shown (see para 19).

(e) The premium to be allowed (subject to reasonableness) is the total premium paid or payable by the receiving party, not the pure underwriting risk premium (see para 53).

(f) Reasonable sums paid as assessment fees and profit costs in respect of obtaining and complying with the ATE policy may also be recoverable (see para 56).

(g) In proving the reasonableness of a premium the receiving party only has to show that he made a reasonable choice. He does not have to show that he made the best choice (see para 61).

(h) A paying party who claims that the premium claimed exceeds the maximum premium it was reasonable to pay at the time should make available to the court and the receiving party charts or tables from the relevant issue of "Litigation Funding" or similar information (see para 11).

(i) It may well be reasonable to take out ATE insurance before sending a letter before claim. Also, it is usually reasonable for an intending claimant to delay taking out ATE insurance until the defendant has given an indication whether the claim will be contested. The later the insurance is taken out the more expensive it is likely to be (see para 26).

(j) A receiving party who purchased a policy the cost of which lies at or above the top of the range of other polices available at the time of purchase should explain why (see para 17).

(k) A high cost premium is easier to justify in cases in which the court has already held that a high success fee is reasonable (see para 17).

(l) Consider what if any reductions should be made in respect of any irrecoverable elements in the premium (see paras 41 to 51).

(m) In valuing any such reductions, adopt a broad brush approach (see para 34(b)).

MASTER O''HARE
COSTS JUDGE

23rd July 2001

Annex 1: List of Parties and Interested Parties who have made written submissions

1. Abbey Legal Protection.
2. Accident Group Ltd
3. Amelans (solicitors for the Respondent).
4. APIL.
5. Association of British Insurers.
6. ATE Grouping
7. Beachcroft Wansbroughs (solicitors for the Appellant).
8. Claims Direct.
9. Christian Fisher (Solicitors)
10. DAS.
11. FOIL.
12. Greystoke Legal Services.
13. Keystone.
14. Lawclub Legal Protection.
15. Law Society.
16. Litigation Protection Ltd.
17. NIG.
18. Saturn Professional Risks
19. Temple Legal Protection
20. XL Brockbank

Annex 2: List of Parties and Interested Parties who attended the hearing on 6 July 2001

1. Abbey Legal Protection.
2. Accident Group Ltd
3. Amelans (solicitors for the Respondent).
4. APIL.
5. Association of British Insurers.
6. ATE Grouping
7. Beachcroft Wansbroughs (solicitors for the Appellant).
8. Claims Direct.
9. DAS Group
10. FOIL.
11. Greystoke Legal Services.
12. Keystone.
13. Lawclub Legal Protection.
14. Law Society.
15. Litigation Protection Ltd.
16. Temple.
17. XL Brockbank

Annex 3: Full Text of Supplementary Questions and Further Questions

SUPPLEMENTARY QUESTIONS

(a) Does the "many paying for the few" principle justify the spreading of premium costs:

Over all categories of personal injury claims?

Over all cases which are borderline or stronger, without differentiating the strength of each case?

(b) Views are sought on premium protections, ie, premium indemnity in respect of loss of claim and premium indemnity in respect of unsuccessful recovery of premium. The latter indemnity sometimes takes the form of a ring-fencing of damages. Should such costs be regarded as additional benefits which are not recoverable against parties ordered to pay costs (cf Dimond v Lovell [2000] 2 WLR 1121)?

(c) Which, if any, of the following should be regarded as additional benefits not recoverable from a party ordered to pay costs:

Interest payable or interest foregone because the payment of premium was deferred?

Interest on other disbursement loans?

If the answer to (a) is in the negative, the top slice of the premium paid in an RTA case where the same premium applies to all categories of personal injury claim?

If the answer to (a) is negative, the top slice of a premium payable in a strong case where the same premium applies to all claims, including borderline claims?

Any right to increase cover in certain circumstances.

Any premium loading because of the claims record of the insured solicitor?

(d) What percentage of a premium is it fair to attribute to all or any of the benefits listed in (b) and (c) above?

(e) Views are sought upon referral fees, assessment fees and similar expenses. Are these properly regarded as part of the administrative costs of issuing policies? Do they attract IPT? Are they recoverable (subject to assessment) from an opposing party ordered to pay costs?

(f) Views are sought on commissions and other payments made to brokers and intermediaries, which include heavy advertising costs. Given the growing market for policies without such payments, is the excess percentage irrecoverable from an opposing party ordered to pay costs? If so, what percentage of the gross premium should be

allowed: should it be assessed on a case by case basis, or should there be a percentage reduction (and if so what percentage) in all relevant cases?

(g) Is it appropriate for the court to fix guidelines as to the maximum premium recoverable in all RTA cases where the policy is taken out prior to 2001, and prior to communicating with the proposed defendant or his insurer? If so, are the following guidelines appropriate:

Fast track £400 Multi-track £800

(These figures are proposed as including IPT and the additional benefits described in (b) and (c) above, and it may therefore be appropriate to discount them accordingly. In any particular case, the guidelines may give way to the particular facts of that case.)

(h) If the answer to the first part of (g) is affirmative, what adjustment should be made to the guidelines in each of the following circumstances:

Where the policy relates to other categories of personal injury claim (eg. employer liability claims or slip and trip claims)?

Where the policy is taken out in an RTA case after the proposed defendant or his insurer has indicated that the claim is to be contested?

Where the policy is taken out in an non-RTA case after the proposed defendant or his insurer has indicated that the claim is to be contested?

Where the policy includes own counsel's fees?

Where the policy covers both sides' costs?

(i) Views differ as to whether it would be cheaper for the liability insurance industry (in overall costs terms as opposed to costs per policy) if fewer policies were issued at a stage later than the letter before claim stage. Is the economic advantage of the liability insurance industry (rather than the individual defendant) an appropriate factor to be taken into account?

FURTHER QUESTIONS FOR CLAIMS DIRECT

(1) Of the 150,000 cases mentioned in your oral submissions, of such of them as are Claims Direct cases, please classify them by percentage under the following headings:

RTA
Slip and trip
Injuries at work
Occupational disease
Clinical negligence
Other personal injury claims

(2) With each classification, please further classify them into fast track cases and multi track cases.

(3) Does Claims Direct accept the submission that, in deciding what percentage of a premium to allow in respect of expenses and commissions, the court should have regard to the tables set out in the ABI Insurance Statistics Year Book for 1989-99 which are quoted in the draft report (para 25)?

(4) Is it correct to say that when Claims Direct introduced ring fencing of damages, it inflated all future premiums in order to off-set the additional burning costs which the ring fencing would cause?

FURTHER QUESTIONS FOR THE APPELLANT

(1) Is it accepted that, to date, ATE insurance has not been profitable? Does this indicate that the premiums charged may be too low?

(2) Is it accepted that many insurers (including Norwich Union) spend substantial sums on advertising?

(3) Comments are sought on the submissions made orally by Anthony Mowatt of Keystone that the decision of His Honour Judge Halbert in *Sarwar v Alam* has significantly altered the dynamics of the legal expenses insurance industry.

ORDER:

1. **Appeal dismissed.**
2. **Respondents to have 100 per cent of their costs.**
3. **Leave to appeal to the House of Lords refused.**

(Order does not form part of approved Judgment)