- The Defendant Costs Specialists

Costs Law Update – 11/12/08

Accident Line Protect

Earlier today judgment was handed down in the long-awaited Accident Line Protect (ALP) Test Cases (reported as *Tankard v John Fredricks Plastics Ltd* [2008] EWCA Civ 1375. In previous Costs Law Updates we have been following the progress of these cases but will outline again the main issues.

These challenges centred around the issue of whether there had been a breach of Regulation 4(2)(e)(ii) of the now revoked CFA Regulations 2000, which required the legal representative to inform the client before a CFA was entered into:

> "(e) whether the legal representative considers that any particular method or methods of financing any or all of those costs is appropriate and, if he considers that a contract of insurance is appropriate or recommends a particular such contract -
>
> (ii) whether he has an interest in doing so."

In *Garrett v Halton Borough Council* [2006] EWCA Civ 1017 the Court of Appeal had held to be invalid a CFA where the solicitors had failed to inform the client that they had an interest in recommending an insurance policy. This was on the basis that, although the solicitors had told their client that they were on a claims management company's panel (Ashley Ainsworth), they had failed to inform the client that they thereby had an indirect financial interest in recommending the policy, because if they did not recommend the particular insurance policy they would have their panel membership withdrawn. The Court concluded that the profit generated by cases referred was likely to be of greater significance to the solicitors than any commissions that might be paid on insurance premiums. It was this failure to disclose to the client that they had a financial interest in remaining on the panel, which would be lost if the client did not accept their recommendation that they enter into this specific After-the-Event (ATE) policy, that amounted to a material breach of the Regulations, as the client did not know that the solicitors were recommending the policy because this was dictated by their financial interest.

Under the ALP Scheme, the standardised CFAs recommended that the client obtain an ATE policy with Accident Line Protect and stated that the solicitor did "not have an interest in recommending this particular insurance agreement".

The relevant facts of the Scheme were that:

- The Scheme included a referral service of potential clients to the solicitors.

- The Scheme's operating manual required the solicitors to comply with all requirements in the manual.

- The manual required the solicitors to issue an Accident Line Protect insurance policy in all eligible CFA cases, whether or not the client had been referred by the Scheme.

- The solicitors could have their membership terminated if they breached any of the procedures in the operating manual.

- The solicitors were entitled to a discount on their ALP membership fee if they issued more than a certain number of ALP policies each year.

The similarities with the facts in *Garrett* can be seen in that solicitors failed to notify their clients of the financial interest they had in the recommending the particular ATE policy, namely their continued membership of the Scheme and the future referrals that might be lost if they did not use this policy. Nor had they informed the clients that they were obliged to recommend the policy in all cases.

The crucial issue the Court of Appeal had to decide was what amounted to an "interest" within the meaning of Regulation 4(2)(e)(ii). The Court concluded that the proper test was that: "a solicitor has an interest if a reasonable person with knowledge of the relevant facts would think that the existence of the interest might affect the advice given by the solicitor to his client". The regulation was:

> "concerned with giving the client who is considering entering into a CFA sufficient information and advice to enable him to take a properly informed and considered decision. He can only do so if he is given information and advice which are not in any way affected by the solicitor's self-interest."

Applying this test to the facts in the test cases, the Court distinguished the ALP Scheme from the claims management scheme in *Garrett*.

- They concluded that mere membership of a panel would not necessarily amount to an interest.

- Ashley Ainsworth, in *Garrett*, were "claims farmers", unlike the ALP Scheme.

- The solicitors in *Garrett* had a "substantial" dependency on Ashley Ainsworth through the referrals they received from them, unlike the solicitors in these test cases.

- In the three cases considered in the ALP Test Cases the overriding consideration for the ATE recommendation was "the quality of the Accident Line ATE policy. That was why the solicitors subscribed to the scheme and recommended the policy to their clients." The prospect of referrals was "an incidental matter".

- It was accepted that the requirement in the ALP Scheme to recommend the ATE policy in all cases was to avoid adverse selection in relation to the underwriter rather than as a "hidden *quid pro quo* for a referral of a case". Therefore, the fact that no other policy could be recommended did not, in itself, amount to a declarable interest.

The Court concluded that "in the absence of particular facts, such as, say, very significant dependence on the scheme for a firm's revenue (which would have to be examined on the facts of the particular case), there is no conflict of interest between the client and his or her solicitors if the test set out above is applied".

Although the Court did not expressly endorse the "*de minimis*" approach that had been adopted by some of the lower courts, they did comment on the low level of fee income/turnover that the ALP referrals represented to the firms involved in these test cases (ranging from 0.15% to 4.57%). Given their other comments concerning "substantial" and "significant" dependence, it does seem clear that an interest would not be a declarable interest if it did not reach a certain level. This aspect of the judgment is the most unsatisfactory:

- How large does the interest have to be to become declarable?

- Are detailed assessments now going to descend into the same kind of analysis as appeared to have happened in some of these test cases, with firms producing detailed accountancy evidence as to the relative value of the referrals? Will teams of forensic accounts now start poring over the evidence?

- Does this mean that two different clients can obtain identical advice on the same scheme from two different firms and that there may have been a breach by one firm but not the other because of the firms' relative "dependency" on the scheme?

- At what date is the size of the interest to be determined?

    - If a firm had only just joined a panel at the time the CFA was entered into, surely it cannot be right that the interest is to be judged simply by the value of any claims received at that point.

    - If the value of the interest is to be determined as at the date of any detailed assessment, that would make the validity of the CFA dependant on facts that occurred after the CFA was entered into. The Court of Appeal has expressly rejected that approach on previous occasions. The date for determining the validity of a CFA is when it is entered into.

    - It seems that the size of the interest is actually the potential value of the future referrals that the firm hope to achieve as a result of membership of any scheme. Whether the hoped for numbers actually materialised should be irrelevant. However, here lies the problem. How is the

> Court, often several years later, meant to attempt to analyse what was in the mind of the solicitors at the time? No doubt many self-serving witness statements will be produced but only limited weight can be attached to these. The fact that a firm did decide to join a particular claim management scheme can only have been on the basis that they thought it was in their financial interest to do so. At that stage, surely, all cases will fail the "reasonable person" test. It seems that the ALP Scheme, the Court having accepted that its main purpose was the ability to offer a good ATE policy, will possibly be the only scheme that would satisfy this test.

Given their findings, the Court held that there had been no interest to declare, there was no breach of the regulation and the CFAs were therefore valid.

Despite these conclusions, the Court did give further, obiter, observations on what is necessary disclosure where there is an interest:

- It is not sufficient to simply state that an interest exists. "The client needs to know more about the nature of the interest before being able to judge whether the solicitor has a motive for making his recommendation. … The purpose of the sub-paragraph is to put the client in a position where he can make an informed decision. … This entails explaining to the client the nature of the benefits to the solicitor in remaining on the [scheme] with sufficient clarity for the client to understand what they are and to be able to assess their significance."

- For the same reason, it would not be sufficient simply to say that the solicitor was obliged to recommend that policy without giving further details as to the nature of the firm's dependency of the scheme.

- The Court also considered the situation where there is a separate document which contains a statement that the policy is recommended because it is the only one, consistent with the solicitors' membership of the panel, that they are allowed to recommend, but the CFA itself states they do not have an interest in recommending the insurance. They concluded that "the inclusion in the CFA of the confirmation that the solicitor has no interest in recommending the insurance means that there is no *clear* disclosure of the interest. In our view, the Regulations require clear disclosure of the interest. Anything less would mean that they fail in their objective of providing consumer protection."

Despite the Court making a number of adverse comments in relation to the "costs wars", this decision will have done little to end this type of challenge. Although a collective sigh of relief will have gone up from panel members of the ALP Scheme (and no doubt the Law Society's insurers given this was a Law Society approved scheme) as future challenges to this scheme, even if the facts were somewhat different, will have no real prospects of success, challenges to other schemes remain open.

Other cases run under claims management schemes remain vulnerable following this judgment. However, the prospects of success or failure are now potentially less certain. Each scheme will not have to be examined on its own facts. Worse, challenges may depend on the facts of the individual firm of solicitors concerned and even vary from time to time within the same firm. This decision may generate more, rather than less, costs litigation.

15th Annual Solicitors Costs Conference

We are pleased to be able to announce that Simon Gibbs of GWS as been invited for the second year running to be a speaker at the prestigious CLT *Annual Solicitors Costs Conference*. He will be speaking on the subject of "Personal Injury – The New Claims Process". The event will be held on 30th January 2009 in London. For a copy of the Conference Brochure use this link: Brochure.

We are able to arrange a 20% discount on the normal delegate fees to any of our clients. Please contact us if you would like to take advantage of this discount.

Contact

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