Costs law brief

The costs team at **Kings Chambers** in Manchester and Leeds discusses two important Court of Appeal decisions on costs challenges under the Conditional Fee Agreements Regulations

Qualitative breaches

On 18 July 2006 the Court of Appeal handed down judgment in *Myatt v National Coal Board* and *Garrett v Halton Borough Council* [2006] EWCA Civ 1017, [2006] All ER (D) 239 (Jul). The Court of Appeal permitted the Law Society to appear as interveners.

The appeals involved reg 4(2)(c) in *Myatt*, and reg 4(2)(e)(ii) in *Garrett*, of the Conditional Fee Agreements Regulations 2000 (SI 2000/692) (the regulations).

Myatt

Regulation 4(2)(c) of the regulations requires the legal representative to inform the client whether he considers that the client's risk of incurring a liability for costs is insured under an existing contract of insurance. In *Myatt*, solicitors were instructed to represent ex-miners who wished to bring claims for damages for noise-induced hearing loss against their former employers. The inquiries that the solicitors made were limited to telephone inquiries.

> *"In Myatt, the Court of Appeal found that the solicitors had asked the wrong questions"*

The clients were not asked to produce their policy documents, but they were asked whether they had before the event (BTE) insurance. While there was a dispute about the exact effect of the questions, the court found that the solicitors required their clients to form a view about whether they had BTE insurance, ie they were asked whether they had any BTE insurance that could be used to fund their claims.

In so far as reg 4(2)(c) of the regulations is concerned, the Court of Appeal gave the following guidance:

- The solicitor must take steps to ascertain what the insurance position is, to be in a position to say whether he considers that the client's risk of costs is already insured.
- To some extent, the solicitor is bound to rely on the client for this purpose. A solicitor is required to do no more than take reasonable steps. What is reasonable will depend on all the circumstances of the case.
- Regulation 4(2)(c) does not require solicitors slavishly to follow the detailed guidance given in *Sarwar v Alam* [2001] EWCA Civ 1401, [2001] 4 All ER 541. In particular, the statement at para 45 of *Sarwar* that a solicitor should normally invite a client to bring to the first interview any relevant policy should be treated with considerable caution. It has no application in high-volume low-value litigation conducted by solicitors on referral by claims management companies.
- A number of factors are relevant when considering whether a solicitor has discharged his obligation under reg 4(2)(c) of the regulations:
  - The nature of the client. If the client is evidently intelligent and has a real knowledge and understanding of insurance matters, it may be reasonable for the solicitor to ask him the ultimate question of whether his insurance covers the proposed claim and, if so, whether it does so to a sufficient extent. Few clients will fall into this category. If the solicitor does ask such questions, he will have to form a view about whether the client's answers to the questions can reasonably be relied upon.
  - The circumstances in which the solicitor is instructed may be relevant to the nature of the inquiries that it is reasonable to expect the solicitor to undertake to establish the BTE insurance position. A good example of the application of this factor is to be found in *Pratt v Bull* 32 LJ Ch 144 in which an 80-year-old claimant was injured in a road accident. A solicitor visited her while she was in hospital and a conditional fee agreement (CFA) was made. For obvious reasons, it was not practicable to carry out extensive inquiries. In these circumstances, it was sufficient that the solicitor had discussed it with her and formed a view on the funding options.
  - The nature of the claim may be relevant. If the claim is one in respect of which it is unlikely that standard insurance policies would provide legal expenses cover, this may be a further reason why it may be reasonable for the solicitor to take fewer steps to ascertain the position than might otherwise be the case.
  - The cost of the after the event (ATE) premium may be a relevant factor.
  - If the claim has been referred to solicitors who are on a panel, it may be relevant that the referring body has already investigated the question of the availability of BTE insurance. Whether it is reasonable to rely on any conclusion already reached will be a matter on which the panel solicitor must exercise his own judgment.

In *Myatt*, the Court of Appeal found that the solicitors had asked the wrong questions. They should not have asked the clients—who were not sophisticated litigants—to decide whether they had BTE insurance which would cover their risk to costs in respect of their claims. Since they asked the wrong question, they did not take reasonable steps to ascertain the true insurance position to enable them to inform their clients whether they considered that the risk was already insured.

Garrett

Regulation 4(2)(e)(ii) of the regulations requires a legal representative who recommends a particular policy of insurance to declare whether he has any interest in doing so. Garrett's claim had been referred to Websters solicitors by a claims management company; that company also offered ATE insurance. The court found that referrals were dependent on the solicitors being members of the claims management company's panel, and that panel membership was dependent on the solicitors continuing to recommend the company's ATE product. No commission was payable to the solicitors.

The solicitors did tell Garrett that they were on the panel, but they did not declare the fact that their panel membership—and hence their source of referrals—was dependent on recommending the company's ATE product.

In so far as reg 4(2)(e)(ii) of the regulations is concerned, the Court of Appeal found that the word "interest" was not ambiguous. They found that an interest would include membership of a panel of a claims management company.

The Court of Appeal found that the obligation in reg 4(2)(e)(ii) is to inform the client if he recommends a particular insurance contract "whether he has an interest in doing so". The obligation is not to inform the client whether he believes that he has an interest in doing so; it is to inform the client whether he has an interest in doing so in fact.

It was held that the statement that Garrett's solicitors had no interest in the insurance premium "although we are on the [claims management company's] panel" did not disclose to Garrett that they had a financial interest in remaining on the panel which might be lost if they did not recommend particular ATE insurance. It was held that Garrett could not have known from what she had been told that her solicitors were recommending the ATE policy because this was dictated by their financial interests.

The Court of Appeal found that disclosable interests were not confined to commission arrangements. Moreover, disclosing the fact of panel membership, without disclosing its implications, was insufficient. Many laypeople would see panel membership as an indication of quality control.

A word of warning for paying parties

The Court of Appeal has, however, made it clear that there is nothing in its judgment that displaces the need for paying parties to justify a compliance inquiry. Dyson said:

"[The court's judgment ought] not be interpreted as giving encouragement to defendants to embark on fishing expeditions in the hope that, if they ask a sufficient number of questions, they may be able to show that the claimant's solicitor did not discharge his… duty. We refer to the salutary words of this court in *Hollins v Russell* [[2003] EWCA Civ 718, [2003] 4 All ER 590] at para 81 that the court should not require further disclosure unless there is a genuine issue as to whether there has been compliance with reg 4."

Materiality

In addition to dealing with breach of the regulations, the Court of Appeal also dealt (at length) with materiality. Dyson LJ summarised the issues as follows:

"The principal question that arises is whether the test of 'materiality' referred to in para 107 of *Hollins v Russell* requires the court to consider whether the client has suffered actual prejudice as a result of an alleged failure to satisfy the conditions referred to (in) s 58(3) of the [Courts and Legal Services Act 1990]. A related question is whether the enforceability of a CFA is to be judged by reference to the circumstances existing at the time when it is entered into, or by reference to the circumstances known to exist at the time when the question arises for decision."

The Law Society argued that these issues had been dealt with in *Hollins v Russell*, in which it was decided that one has to show actual detriment rather than merely the possibility of detriment. The Court of Appeal rejected these submissions.

The society and the receiving parties argued that only serious breaches of the regulations should result in the CFA being found to be unenforceable. The Court of Appeal rejected this submission:

"Parliament was painting with a broad brush. It must be taken to have deliberately decided not to distinguish between cases of non-compliance which are innocent and those which are negligent or committed in bad faith, nor between those which cause prejudice (in the sense of actual loss) and those which do not. It would have been open to Parliament to distinguish between such cases, but it chose not to do so.

"Parliament considered that the need to safeguard the interests of clients was so important that it should be secured by providing that, if any of the conditions were not satisfied, the CFA would not be enforceable and the solicitor would not be paid. [T]his is an approach of punishing solicitors *pour encourager les autres*. Such a policy is tough, but it is not irrational."

As to the supposed need to show actual detriment, the Court of Appeal said:

"Difficulties of causation and loss are inherent in the common law. But there is no warrant for importing these difficulties into a statutory scheme which states in terms that breaches of the requirements render a CFA unenforceable. On the face of it, the statutory scheme is straightforward. It provides that, if a solicitor fails to comply with the obligation to inform the client of any of the matters set out in reg 4(2), the CFA will be unenforceable. That is clear and stark. At first sight, there is no room here for any consideration of the actual consequences of the failure to comply. To adopt language appropriate to a breach of contract, the statutory language refers only to breach, and not to causation or loss. Subject to the principle that the law is not concerned with very small things, a breach of contract is a breach even if it causes no loss."

> *"The Court of Appeal found that disclosable interests were not confined to commission agreements"*

That is not to say, however, that the court should totally disregard what actually happened. In this regard, Dyson LJ added:

"In some cases, it may be helpful to have regard to what actually happened, because that may shed light on the potential consequences of a breach (if the matter is judged at the date of the CFA) and therefore on the extent to which the breach had a material adverse effect on the protection afforded to the client. In our view, however, in most cases the court should focus its attention principally on the terms of the CFA and the advice and information given by the solicitor and other relevant circumstances which existed at the date of the CFA and make a judgment as to whether, in the light of that material, the departure from the requirement in question had a material adverse effect on the protection afforded to the client."

A final word

Practitioners would do well to note the contents of the penultimate paragraph of the judgment, where the Court of Appeal made some *obiter* comments about the obligations imposed by the Solicitors' Financial Services (Conduct of Business) Rules 2001, *www.lawsociety.org.uk/documents/downloads/FSA_amended_%20COB.pdf*. If any practitioners are unsure about their obligations in this regard, they would do well to cast an eye over 155 NLJ 7189, p 1242.

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