ECONOMY, JOBS AND FAIR WORK COMMITTEE

DAMAGES (INVESTMENT RETURNS AND PERIODICAL PAYMENTS) (SCOTLAND) BILL

SUBMISSION FROM - AXA Insurance

Damages (Investment Returns and Periodical Payments) (Scotland) Bill

General

1. What are your views on the Bill overall? Is legislation in this area required? How far do you think the Bill will achieve what it sets out to do?

The proposals of the Scottish Government are broadly welcomed as there is a need for a fairer approach for compensators and victims than the artificial approach imposed by the decision in Wells v Wells (1999). Because of this decision, the law has become defective in respect of the interpretation of Wells and its inter relationship with the Damages Act. We believe that Wells has outlived its usefulness in that voluntary periodic payment orders provide a satisfactory vehicle to protect the most vulnerable claimants. In addition, Wells by establishing that the discount rate should be set solely by reference to ILGS, does not reflect the reality of how claimants invest. Therefore, claimants may become over compensated.

AXA supports the 100% principle where the injured party should be placed in the same financial position as they were before the accident, no more and no less. However, it needs to be recognised that assessment of damages is, by its nature, an inexact science. Damages are agreed or determined by the courts at a given point in time. Even with the best skill and diligence life is uncertain and an individual pursuer’s medical circumstances and needs may change over time. They may need more or less care; they may decide that they do not want the intrusion of a paid care regime or case manager that were allowed for in the damages award and make do with family and friends. They may die far earlier than anticipated. In these instances, they will be over compensated and the converse is also true. Nevertheless, the principle must be central to any change in the law as it currently stands.

Evidence from two specialist Court of Protection law firms who administer severely injured claimants’ affairs post settlement, confirm that in their experience claimants rarely run out of money and where they do it is either because the medical condition has worsened or because damages were reduced in the first place by contributory negligence.

We have been advised by Court of Protection solicitors that their investment portfolios have yielded approx. 4% p.a growth and 2% income after fees. We would suggest that this gives a real rate of return in the region of 2-3%. Similarly, Seven Investment Management Personal injury fund has delivered approx. 20% gross return.

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cumulative growth over a five-year period. This again would give a real rate of return of approx. 1.5%. Details of this fund are attached to this submission. These examples would provide for a discount for accelerated receipt and, in practice, are more likely to deliver 100% compensation than the current negative rate which will over compensate claimants. In short, the current minus 0.75% discount rate is not a discount rate; it acts as a bonus for early receipt of damages by pursuers.

Part 1

2. Part 1 of the Bill aims “to reform the law on the setting of the personal injury discount rate in order to make provision for a method and process which is clear, certain, fair, regular, transparent and credible”. Is it an aim with which you agree? And to what extent do you believe the reform will achieve all these things – a clear, certain, fair, regular, transparent and credible method and process?

AXA welcomes the Scottish Government’s aims to make provision for a method and process which is clear, certain, fair, regular, transparent and credible. However, while the concept of a notional portfolio is transparent, we wonder if it might militate against 100% compensation and might prove to be inflexible.

We are led to believe that the majority of claimants will invest in mixed portfolios which will include equities, the proportion of which will vary between 30% and 70% of the portfolio. The precise mix will depend on individual need and circumstance. The table below provides some data provided by Charles Stanley Investment Management who administer a number of personal injury awards for clients:

<table>
<thead>
<tr>
<th>Asset Allocation</th>
<th>Acceptable level of Risk</th>
<th>Clients as at Sept 2012</th>
<th>Clients as at March 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>CO1 100% Cash Investment</td>
<td>Lower</td>
<td>12</td>
<td>2</td>
</tr>
<tr>
<td>CO2 Up to 30% Equity</td>
<td>Lower</td>
<td>69</td>
<td>88</td>
</tr>
<tr>
<td>CO3 Up to 50% Equity</td>
<td>Medium/Low</td>
<td>72</td>
<td>107</td>
</tr>
<tr>
<td>CO4 Up to 70% Equity</td>
<td>Medium/Low</td>
<td>116</td>
<td>106</td>
</tr>
</tbody>
</table>

We believe that the proposed mix of the notional portfolio is light on equities and heavy on fixed investments and cash.
It is accepted that the charges applied by fund managers needs to be considered, but sometimes these include periodic investment advice. The cost of initial investment advice is not a recoverable head of damage. Indeed, with a prescribed notional portfolio, such advice is unnecessary. While the impact of taxation and fund management fees need to be taken into account, we do not understand the need for 'a further margin' as set out in clause 10(2)(b) of the Bill. This seems unnecessary, particularly as the proposed notional portfolio is cautious. The provision also seems to undermine certainty and fairness in the process. The 0.5% reductions appear unduly artificial and inflexible and may promote over compensation.

3. In terms of who sets the rate, the Scottish Government proposes to have the rate reviewed by the Government Actuary rather than Scottish ministers (as is the current situation). It believes that this will remove the setting of the rate from the political sphere “where there is the potential for pressure from external interests to attempt to influence the outcome” and “should provide fairness to all parties involved”. What are your views?

We support and adopt the comments made by the ABI in their submission. The accountability for setting the discount rate should be a political and not a judicial one. We do not agree that the Bill as drafted removes the setting of the rate from the political sphere. The Bill sets out the rate-setter's remit very precisely: the decision to specify this portfolio and the additional adjustments is very much a political one. The only area of discretion that the rate-setter has is around the interpretation of "other types" of investment in the notional portfolio.

The Scottish Government retains the power to alter the notional portfolio by way of regulations as well as to alter the adjustments and tax considerations. Our opinion is that it will need to exercise this power before each review, to ensure that the assumptions made remain accurate. The remit, whilst precise, is therefore still open to consideration within the political sphere. In our opinion, Scottish Ministers would need to consider investment practice and the make-up of a suitable portfolio and revise the notional portfolio before each review takes place. The assumptions that are made by Scottish Ministers will therefore largely dictate the outcome. This process does not remove the setting of the rate from the political sphere, nor does it avoid attempts to influence the outcome. Scottish Ministers will need to regularly review the provisions of the Bill, probably before each rate review, to ensure that they remain appropriate.

4. The Scottish Government has chosen to lay down in detail how the rate should be calculated in legislation. Do you support this proposal over the approach taken in England and Wales of leaving much more to the discretion of the Lord Chancellor and an expert panel?

No. We prefer the approach to be adopted in England and Wales of an independent panel. There is a risk that the proposed approach to be adopted in Scotland of a notional portfolio may prove to be over prescriptive and may not provide sufficient
flexibility to consider changing economic conditions and the need to fully consider actual investment practices of pursuers. The approach taken in England & Wales, provides enhanced discretion to the decision makers and to better allow for the 100% compensation principle to be adhered to.

5. With no statutory requirement for the discount rate to be reviewed regularly, currently there can be a 15 year gap between reviews in Scotland. The Government Actuary will start a review of the rate on the date on which the relevant provisions of the Bill are brought into force. Thereafter they will be required to start a regular review every three years and the Scottish Ministers may decide on an additional, out-of-cycle review, but which would not disrupt three-yearly reviews. Do you have any views?

Catastrophic injury claims often take longer than three years to settle, especially in Scotland. There is a risk that applying a three-year review period in respect of the discount rate will lead to both pursuers and defenders ‘gaming the system’ if they perceive that the discount rate is likely to change. This will not help seriously injured pursuers. For this reason, we believe that a five-year review cycle is more appropriate. It is also pertinent to note that the House of Lords secured this amendment in relation to the discount rate provisions in England & Wales on the basis it would provide further certainty and not unduly impede flexibility in the process. Amending the Scottish provisions to ensure consistency would be welcomed.

Any out of cycle reviews, in the interests of certainty for both sides should be exercised only rarely and in exceptional circumstances

6. In changing the methodology to move away from a rate based on Index-Linked Government Stock (ILGS), the Bill makes provision “on the basis of portfolios described as cautious and which we believe would meet the needs of an individual in the position of the hypothetical investor who is described in the legislation”. The Scottish Government also states: “The portfolio does reflect responses to the consultation that investing in a mixed portfolio of assets provides flexibility and is the best way of managing risk”. Do you think the Scottish Government is justified in assuming that injured people have access to the necessary expertise to achieve this?

This question is best answered by pursuers and their legal representatives. However, what information we do have, relating to claimants in England and Wales, confirms investment in mixed portfolios tailored to meet their needs. See table at QA2. above. Where 100% cash investment is chosen it is reflective of limited life expectancy.
The response of the Association of Personal Injury Lawyers to the UK Government’s 2017 consultation on the Discount Rate provides further information as to advice given to pursuers.

**Part 2**

7. Where damages for personal injury are payable, the Scottish courts may make a periodical payments order but only where both parties consent. This differs from England and Wales, where the courts have the power to impose such an order. Part 2 of the Bill will give courts the powers to impose periodical payments orders (PPO) for compensation for future financial loss. Respondents to recent consultations overwhelmingly supported courts in Scotland having the power to impose periodical payment orders, seeing this as a way of reducing uncertainty as well as the risk of over-/under-compensating pursuers. What is your position?

AXA supports the proposed measures to allow courts to impose periodical payments in appropriate cases. They provide for the fairest way of compensating the most seriously injured pursuers. It could also be said that, in catastrophic injury cases, the absence of courts being able to make a periodical payment order could deny pursuers injured in Scotland of full compensation and peace of mind when compared with a resident of Scotland who by chance sustains similar injuries in England. There is also merit in ensuring that the provisions throughout the UK in relation to periodical payment orders (PPOs) are consistent.

The low uptake of PPOs by consent, even in the period when the discount rate was set at 2.5%, may demonstrate that most pursuers prefer a lump sum award and are therefore prepared to take some, albeit limited, investment risk, based on financial advice received. The risk pursuers choose to accept is well above the theoretical "very low risk" construct. Part of the reason for choosing a lump sum may be driven by other factors such as the desire to provide for dependants after death.

The reality is that any pursuer opting for a lump sum award is taking risks in respect of life expectancy, inflation and investment performance and will only do so in a high-value claim following receipt of independent financial and legal advice and, therefore, is making an informed choice to accept a lump sum. In many such cases the pursuer will be advised about the availability and suitability of a periodical payments order.

Nevertheless, while informed pursuer preference and choice is important, the courts should have the ability to award periodical payments in the appropriate cases involving the most seriously injured. Further, any periodical payment order should, in the main, be restricted to cost of care and ancillary costs.
8. How well used do you think the provisions would be in practice? What impact do you think the requirement on the court to ensure the “continuity of payment under such an order would be reasonably secure” would have?

Based on the experience of England and Wales it is likely that up take of PPOs will be slow and it may be several years before they become a regular feature in claims involving the most seriously injured. It is possible that this slow uptake in England and Wales was partly due to a lack of familiarity with PPOs following their introduction. Clearly, that is no longer the case and all UK based insurers are now fully familiar with PPOs. By way of illustration, AXA Insurance agrees some 4-6 PPOs a year. However, as was the case in England and Wales, it is probable that the NHS will be in the forefront of promoting PPOs in Scotland.

Periodical payment orders are not suitable in every maximum severity case. For instance, if there is a high degree of contributory negligence on the part of the pursuer, they may not be suitable as the annual amount paid (net of contributory negligence) may not be enough to meet cost of care. Similarly, in non-motor accident cases, the limit of indemnity of a policy of insurance may inhibit the appropriateness of a PPO. Or the compensator may be a non-UK regulated insurer e.g. arising from an accident involving a foreign lorry.

Additionally, a pursuer may not want a PPO as they want the certainty and closure from the settlement process and do not wish to maintain perceived ties with the compensating insurer. Based on our experience in England and Wales, the uptake of PPOs will be driven by pursuer choice and they will decide, based on financial and legal advice, whether they would prefer a lump sum or a PPO.

Continuity of payment requirements is unlikely to materially affect the take up and operation of PPOs, which seek to mirror those in England & Wales. Most compensators will be able to satisfy the requirements as seen in England & Wales, which the condition has not had an impact on PPO use.

9. The proposals in the Bill would allow the courts to revisit a compensation award where there has been a change of circumstances (although only where this has been identified in advance). This would represent a change to the current law. Do you have any comments?

It will be important to ensure this provision is not abused. Whilst it will promote access to justice, care must be taken that it doesn’t unduly undermine certainty in the litigation process which is important for all stakeholders.

This provision will need to be monitored in practice to see that not misused and there is no gaming of the system and the instances of satellite litigation on this point do not disproportionately increase.

Given the take-up of PPOs is likely to continue to be low, it is not anticipated this will be a significant issue even where problems do arise and this has not been the experience in England and Wales.
Overall

10. The Bill overall is intended to support the Scottish Government’s national outcome that: “We have strong, resilient and supportive communities where people take responsibility for their own actions and how they affect others”. Do you have any comment?

The principle of 100% compensation and of putting the pursuer back in the position they would have been in but for accident should be central to our system of compensation. This means that it must also be fair to both the pursuer and the compensator. The impact on wider society, as payers of tax and insurance premiums, is also an important part of the balance required to create a fair mechanism for setting a discount rate which reflects actual investment practices of pursuers. Without accurately reflecting actual investment practices, the discount rate will lead to significant over-compensation, which is currently the case, and therefore does not meet the 100% compensation principle. The significant costs of over-compensation also create a problem for society at large, not just through pressure on insurance premiums for motorists and businesses but also for those public bodies who have to meet the cost of compensation, including the NHS.

11. In previous consultations in this area, views have tended to be polarised between pursuer and defender interests. Does the Bill, in your view, manage to balance these interests?

We feel that the proposals are a reasonable attempt at creating a fairer system. Improved consistency with the new provisions in England & Wales, which promotes accountability, transparency and reference to the actual investment practices of pursuers are all areas that could be improved in the Bill.

Balancing of interests creates the wrong focus for these proposals; instead, the focus should be on the risk of over- or under-compensation. Whilst the Bill addresses many of the fundamental problems under the current system, more could be done to fully confirm to the 100% compensation principle.

Other comments

12. Are there any other aspects of the Bill you wish to comment on?

We have no further comment or observations on other aspects of the Bill.