The Discount Rate and Multipliers: Are We Brave Enough to Care?

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It is time for the insurer's complaints and claimant's gloating to cease and for parties to engage more wholeheartedly in the change to the discount rate and periodical payment orders.

In a recent TED talk by poet, artist and "the millennial Oprah", Cleo Wade asked “Want to change the World? Start by being brave enough to care.” This may seem grandiose in our context, but to those injured through a defendant's breach of duty or negligence, it's very apt.

In February 2017 the Lord Chancellor and Justice Secretary changed the personal injury discount rate from 2.5% to -0.75%. A consultation process was undertaken, primarily because the Insurance Industry were up in arms about the change and its material impact on the valuation of claims, namely that they would increase significantly. The House of Commons Justice Committee published its report, “Pre-Legislative Scrutiny: Draft Personal Injury Discount Rate Clause”, together with the related evidence on 30th November 2017. This Committee was asked to undertake pre-legislative scrutiny of the draft clause in “The Personal Injury Discount Rate: How It Should Be Set in Future: Draft Legislation” Command Paper 9500.

It is clear that the Government and the Insurance Industry are still advocating full compensation for claimants, namely, maintaining “the principle that claimants should receive 100% compensation for losses they incur”. From a cynical standpoint, this is probably because it is politically and legally unattractive to say otherwise. However, whilst purportedly seeking to maintain the 100% compensation principle, it is advocated that the discount rate should not be set by reference to returns from index linked government securities. The discount rate should, it is submitted on behalf of the Insurance Industry, reflect the likely ‘real world’ investment return, which is not -0.75%.

The purpose of this article is to strip away the “fake news” and the information manipulated to support a particular point of view. It has always been the case that when a lump sum award is made, some claimants may be under-compensated, and others over-compensated. For example, this is particularly the case if an individual were to live longer than the statistical life expectancy or conversely for much less. It is our view that everyone should “matter” in a fair society and it must be the aim to seek to achieve fair and full compensation albeit that this may not be truly 100% compensation. We struggle to see how any party can contend that the historical evidence reveals full compensation in all cases. In fact, the reality without some investment risk being taken, utilising the former discount rate of 2.5% is that a claimant would always have been under-compensated save in a few cases. There is also an argument that we as lawyers should be ensuring that proper, and long lasting investment advice is sought to support the claimant into the future. This would also

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be to ensure that 100% compensation is more easily achieved, helping to reduce overall costs, and god forbid, help the insurers too.

The award of damages should, so far as is possible, put a claimant in the position they would have been in had they not been injured due to the defendant's breach of duty/negligence. A claimant is "entitled to be compensated as nearly as possible in full for all pecuniary losses…" (***Wells v Wells*** 1999 AC 435 at page 382). Of course all courts, when deciding whether a head of loss is recoverable, undertakes an assessment of the reasonableness of the head of loss and its amount (***Sowden v Lodge*** 2004 EWCA Civ 1370). Courts have never considered a claimant's case in a vacuum but have always paid regard to a defendant's viewpoint when looking at fair and reasonable compensation.

"… The aim of an award of damages for personal injuries is to provide compensation. The principle is that as near as possible, "full compensation" should be provided … This principle of "full compensation" applies to pecuniary and non-pecuniary damages alike … The compensation must remain fair, reasonable, and just. Fair compensation for the injured persons. The level must also not result in injustice to the defendant, and it must not be out of accord with what society as a whole would perceive as being reasonable." (***Heil v Rankin*** 2001 2QB 272 at page 297)

The question of reasonableness as a society is inevitably a difficult one to judge though. One only needs to look at the vast difference in levels of bereavement awards between England & Wales and Northern Ireland, compared to Scotland. In Scotland, Civil Jury Trials have shown that society considers awards of over £100,000 are reasonable to a bereaved spouse. In England & Wales, the cap is £12,800 to be shared amongst all eligible parties (£14,800 in Northern Ireland). This figure is regularly exceeded in Scotland by bereaved grandchildren, or parents alone. Judicial awards in Scotland were criticised in Hamilton v Ferguson Transport as being markedly undervalued when compared with jury awards. Since that decision a judicial decision in Catherine McGee and others v RJK Building Services Limited, has resulted in the following awards being made:-

Bereaved Party	**Amount**
Wife aged 71	£80,000
Daughter aged 44	£35,000
Daughter aged 37	£35,000
Son aged 43	£27,500
Granddaughter aged 9	£25,000
Grandson aged 17	£20,000
Granddaughter aged 13	£12,000
Granddaughter aged 11	£12,000

When a court is determining what is reasonable, there is clear consideration of all relevant circumstances including the requirement for proportionality as between the cost to the defendant of any individual item and the extent of the benefits which would be derived from that item by the claimant. Reaffirmed by Mrs Justice Swift in ***Whiten v St George's Healthcare Trust*** 2011 EWHC 2066: this continues to receive judicial acknowledgment and agreement.

The discount rate is a set rate used to calculate the amount of compensation to take into account a claimant's age, gender, and working life, and was always intended to be linked to a very low risk investment in accordance with ***Wells v Wells***. It has to be acknowledged by all that rather than setting the discount rate by reference to a "very low risk" investment, the time has now come to reference any discount rate for the purpose of compensation to "low risk"; this will be the subject of regular review by an independent person or body.

It has been studiously ignored by those expressing their horror at the change in the discount rate that it does not in fact make a significant difference to the life expectancy multiplier for a more mature claimant and very little difference at all to the loss of earnings multiplier, as shown in the tables below.

MULTIPLIER EXAMPLE

Discount Rate/Life Expectancy	64-Year Old Male	37-Year-Old Male
Life expectancy	22.5	49.9
Life multiplier		
-0.75%	24.74	60.25
0%	22.28	48.93
0.5%	20.85	43.00
1%	19.55	38.07
2.5%	16.35	27.53

MULTIPLIER EXAMPLE

Discount Rate/Life Expectancy	64-Year Old Male	37-Year-Old Male
Earning to 70 years of age		
-0.75%	5.9	32.06
0%	5.77	28.32
0.5%	5.68	26.16
1%	5.6	24.25
2.5%	5.6	19.55

At a glance, it can be seen that there is very little difference to the earnings multiplier, and some, but not a significant difference to the life expectancy multiplier for a 64-year-old male. For a 37-year-old male, it is a different story.

The Insurance Industry's contention that premiums will increase for the population may be a good "soundbite" but if it occurs at all, it will only be modest. Most of us pay insurance premiums to cover various eventualities, including driving motor vehicles and house contents insurance, with the hope of never having to rely upon such policies. The same applies with professional indemnity premiums where most professionals pay significant sums throughout their professional career without reliance upon such policies. If however there is fault on the part of the tortfeasor, the premiums paid are not to provide damages as a reward for an injured individual but as true compensation, which if not agreed, is determined by a judge. The Justice Select Committee heard evidence from Professor Victoria Wass who argued that claimants earning a higher rate of return than the discount rate aren't "over-compensated"; they are earning a premium for taking on more risk:

"If… the claimant accepts a greater risk in return for the opportunity for financial gain, that is up to the claimant. S/he are not to be required to do so and it is of no concern to the court or the defendant whether or not this is subsequently chosen." (Paragraph 30.)

It seems to us that the Insurance Industry are misguidedly seeking to shift the investment risk to claimants who are not true speculative investors seeking to increase the financial pot but are investors seeking to maintain the financial pot in order to fund necessary costs, such as support workers, care and assistance, case management, and the like. As above, it could be for claimant's representatives to put more in place to safeguard a pot, whilst providing adequate risk, as risk is inherent in everyday life prior to an accident. We should be helping to raise the rate as much as is necessary whilst the insurance industry should be giving the 100%.

In essence, we have to be brave enough to acknowledge that 100% compensation for 100% of claimants is not possible by way of a conventional lump sum award unless the discount rate remains at -0.75%. In effect, Professor Wass and others are saying that the Government has to decide how it intends to resolve a conflict between full compensation and affordable compensation. The two concepts cannot co-exist if there is a conventional lump sum damages award. We will set out two alternatives to this later in the article.

As the Select Committee sets out at paragraph 33:

"It is possible that claimants may be "under-compensated" even when the discount rate is set at a "risk-free" rate because compensation may be inadequate for their accommodation needs; they may be living longer than expected or there may be real increases in their cost of care over time. We recommend that the Government find a means of assessing whether the legislative framework is compensating claimants fairly for their losses; otherwise by increasing the discount rate to remove what it sees as one type of "over-compensation" (primarily over-compensation due to greater than anticipated earnings from lump-sum investment), it may be simply increasing levels of under-compensation for claimants who were already under-compensated."

On behalf of claimants, Professor Wass is determined in her view that the Government's impact assessment leads to clear and obvious "losses of equity and efficiency", stating that,

"The Government's impact assessment indicates that the legislation will lead to greater equity (fairness) if there is a reduction in over-compensation." Whilst also highlighting that

> "There is inequity when you transfer risk from the claimant to the defendant. There is also inefficiency, because claimants are going to be much less efficient than the Government and the insurance industry in bearing and managing that risk."

"Professor Wass also told us:

> "In distributional terms, it is preferable to spread the cost of risk across society (tax payers and consumers of insurance) than to concentrate it on a few claimants."

As part of the "fake news" it is clear that the periodical payments orders, the reserve is currently -0.8%. This is currently what the Government reserve in any clinical negligence cases.

Richard Cropper of PFP argued that the impact of the discount rate on clinical negligence costs was mitigated by the fact that for most large claims, PPOs were used and the Government currently must reserve for them at a negative rate of -0.8%, saying that:

> "Changing the discount rate, which would have the greatest impact on care, case management and loss of earnings, if they continue to be paid in periodical payment terms, will not save the NHS a penny from an accounting perspective, because they will still be reserved for at negative 0.8%."

Realistically, the discount rate is going to change again from -0.75% to a rate between 0% - 1%. Even now, however, the Government seems to be trying to backtrack on their initial indication of a band 0% - 1%. In our view the net discount rate should be no higher than 0.5%, namely a gross return of 1%, if it is being acknowledged by all that the costs of investment and fees are 0.5%.

Proposed Solutions

Split Discount Rate

This option was used in the Guernsey case of ***Helmot v Simon*** 2012 UKPC 5 This case was not bound by the discount rate as it would have been on the mainland, but is a useful example of what could be. At first instance, the court applied a single discount rate of 1% with the defendant contending for 2.5% and the claimant for 0.5% for non-earnings related losses and -1.5% for earnings-related losses. On appeal, including Sumption JJ, he allowed the appeal and substituted a discount rate of -1.5% for earnings-related losses and 0.5% for other losses. The Privy Council dismissed the appeal. So why do we not consider splitting the discount rate for heads of loss in individual cases? It is perhaps relevant to note that the loss of earnings related losses in ***Helmot v Simon*** had a discount rate ultimately of -1.5%. As can be seen from the tables above, that does not impact to the same extent in loss of earnings awards as opposed to those heads of loss utilising life multipliers. In ***Helmot v Simon***, all those other losses, applying the life multiplier, the discount rate used was 0.5%. Obviously, sound cogent actuarial evidence would be needed in individual cases to support such options. We do not consider that a split multiplier approach should be side-lined in favour of a rate applicable to all heads of loss, especially if there is a temptation to move the discount rate back to 1% or more. There is in our view no sensible material that could properly be relied upon to move the discount rate to 1% or even nearer to the original 2.5%. The Insurance Industry know full well the disingenuous nature of their approach when requesting the investment statistics for claimants over the past 10 years or so. They know full well that because the discount rate of 2.5% was wrong and resulted in, or would have resulted in, significant under-compensation for claimants, that appropriate financial and investment advice was needed to move away from very low risk to low risk in order to minimise such under-compensation. Even then, it has always been understood that there was a real prospect of many claimants not being able to fund the necessary heads of loss.

Periodical Payments Orders

The main answer in our opinion, alongside the split rates, was studiously sidestepped or ignored by the Government and the Insurance Industry, is a periodical payment order.

Law Applicable in England and Wales:

Periodical Payments Orders

- Under Section 2(1) of the Damages Act 1996 the court has power to order that “all of part of an award of damages in respect of personal injuries to take the form of periodical payments.”
- CPR 41.7 “… The court shall have regard to all the circumstances of the case and in particular the form of award which best meets the claimant’s needs, having regard to the factors set out in Practice Direction 41B.”

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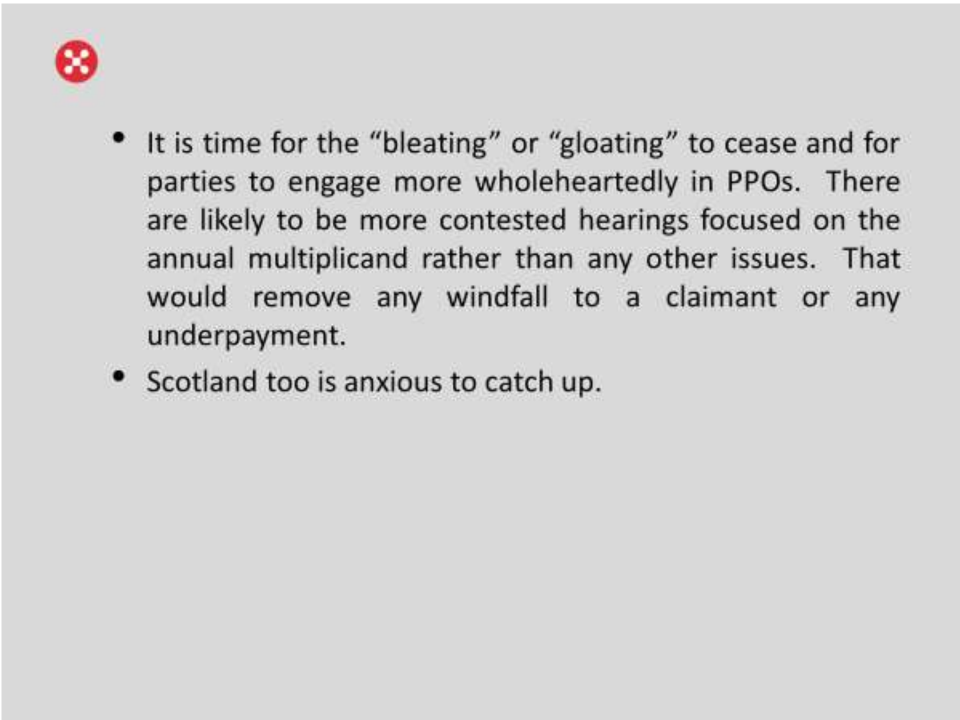
- The Indices accepted care and assistance/support/ case management is ASHE 6115 (ONS Annual Survey for Hours and Earnings).
- Of course the Average Earnings Index could be utilised for a PPO for loss of earnings but more often than not this is capitalised.
- The Retail Price Index should never be forgotten particularly moving forwards and the fact that ASHE 6115 is simply retained for the purpose of the legal process.

New Dawn



In our opinion, there should be a rebuttable presumption that a periodical payments order is required in all cases. It would then be for a claimant (or defendant) to adduce evidence and arguments applicable to individual heads of loss or the case as a whole as to why it would be inappropriate.

This would particularly applicable in clinical negligence actions. It is “fake news” to focus on the increase in lump sum payments in any clinical negligence action without having regard to a periodical payments order, which as outlined, we believe should become the norm and automatic, subject to court approval or court determination.

We are unimpressed by the information provided to the Justice Select Committee at paragraphs 95 and 96:

“The impact assessment noted that “defendants, including public sector bodies (such as NHS Resolution) and insurers, will benefit from lower lump sum payments”. The former Lord Chancellor, when announcing the recent reduction in discount rate, drew attention to the repercussions it would have on clinical negligence costs.

We were told that the discount rate reduction has sharply increased clinical negligence pay-outs. The Medical Protection Society explained that the recent change in the rate from 2.5% to -0.75% would result in a sharp increase in clinical negligence costs. They pointed out that, in 2016–17 alone, the NHS paid out £1.7bn for clinical negligence claims. Emma Hallinan from the MPS told us this “could have an impact on subscription rates, but [they] would have to weigh that with other factors”.

Further we are of the opinion that in cases where a claimant lacks capacity to manage their affairs within the meaning of the Mental Capacity Act 2005 that the cost or funding of the Deputy’s fees after Year 2 should always be a periodical payments order, linked to an appropriate indices, save in exceptional circumstances which can only be permitted by order of the court. In such cases, the court’s approval would be required of any settlement.

Law applicable in Scotland:

To date, Scots Law has required both parties to be in agreement for periodical payments orders to be used, and they are used rarely in court proceedings for that reason. The Scottish Government though have put in motion a new Damages Bill which would bring Scotland onto a level with England & Wales on PPO’s. This has been slated to come in at some stage during 2018 and ensures that the court “a) must consider whether to make an order under which those damages wholly or partly take the form of periodical payments, and b) may take such an order with or without the consent of the parties.” We would say that this is an important step and will be the best way for both sides to achieve full compensation with fewer risks of over or under-compensating. This draft wording allows the court greater scope for awards, and only time will tell whether that results in greater uptake. In any event, it is a positive step, and those acting for the various parties must embrace this as a positive opportunity.

At present, the historical approach to the valuation of accommodation claims pursuant to ***Roberts v Johnstone*** 1989 QB 878 results in a nil award if applying -0.75% discount rate. This has now been revisited by litigators and courts over the past 12 months (such as in JR v Sheffield Teaching Hospital 2017 EWHC 1245 QB). In our view, this is a topic that stands on its own irrespective of any change in the discount rate, and should be separately decided, rather than linked to the discount rate. This is to maintain the ability of a claimant to make appropriate amendments to, or to purchase suitable accommodation to suit their new circumstances. (see our article entitled "Accommodation Claims: Roberts v Johnstone is old hat and no longer applicable").

Conclusions

Are you brave enough to care? If so, we would say that you should engage wholeheartedly in every case with a periodical payments order unless there is a specific reason for not doing so. There has to be a presumption for a PPO. That removes, so far as it is possible to do so, the risk of over/under-compensation. The split multiplier should also be appropriate in all cases for earnings-related losses and then a different rate for other losses. That again would minimise the risk of over/under-compensation whilst still seeking to achieve full compensation for a claimant. This would also benefit the insurance industry, as it would allow for more certainty than the present state of affairs, where huge lump sums could be paid out only every now and again. This would allow for insurers to budget for these matters and reduces the risk regarding life expectancies and overcompensation.

What should the discount rate be? Probably, in a vacuum and without political pressure, no higher than 0%. Realistically however we are of the view that 0.5% would be appropriate for all heads of loss save for earnings-related losses which should remain at -0.75%, or alternatively, -0.50%. In any event, whatever the discount rate, this must be revisited frequently by an independent arbiter so that we never are in a position as litigators of maintaining an inappropriate discount rate (such as 2.5%) for many years with no structure in place for reviews. We feel that these reviews shouldn't be telegraphed, giving either party a chance to drag their heels and hold out for better rates, or to rush through litigation resulting in a less than satisfactory award.

As we go to print Lord Keen has introduced the Civil Liability Bill into the House of Lords, which promises "to modernise the way the discount rate is set". The MOJ have promised that the 100% compensation principle will be supported by the Bill, which will set up reviews "at least every 3 years" and create "an independent expert panel" to advise on the appropriate rate. The Government's response to the Judicial Select Committee pre legislative scrutiny, again "hot off the press", still fails to engage with many of the matters we have set out in this article, in particular periodical payments and split multipliers. This Bill will indeed modernise the process by ensuring more frequent and compulsory scrutiny, however if the panel and Lord Chancellor fail to engage with the background of 100% compensation, then the end product will be lacking. The suggestions made in this article should still be taken into account by those in practice in order to give both sides the best outcome on average, reducing the risks of over, or under, compensation, and to reduce the strain on the rate consultations moving forwards.

We do care, and the brave decision would be to approach this from a starting point where periodical payment orders should be the norm, split multipliers should be considered in individual cases, but with a discount rate not increasing in 2018 higher than 0.5% with a regulatory structure for review thereafter.

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