



## **FOIL CONSULTATION** August 2009

### Regulating Damages Based Agreements (DBAs)

Damages Based Agreements are a type of contingency fee agreement commonly used to fund employment claims and other tribunal cases. They fund around 11% of employment claims. Instead of being based on the level of costs incurred like CFAs, under DBAs legal representatives take a percentage of the damages recovered. There is no regulation of this type of agreement and growing evidence that they are creating consumer protection issues, particularly through a lack of advice to clients on alternative methods of funding and a lack of clarity. Some of the terms included in some agreements are thought to be unfair.

The Government is proposing to regulate this type of agreement, to improve consumer protection. A clause permitting the Lord Chancellor to make an Order governing DBAs will be included in the Coroners and Justice Bill and the Order will then be made by statutory instrument setting out the regulations.

DBAs cannot be used to fund personal injury or other litigation (they are only permitted for employment cases as those claims are defined as 'non-contentious') but there are still reasons for FOIL to express a view: the Government also intends to include in the new legislation a provision allowing an Order to be made in the future, if the Government so wishes, permitting DBAs to be used for litigation. The Government has no plans to allow that at present but such an Order may be considered if a change is recommended by Lord Justice Jackson. Although the consultation indicates that before this happens further consultation would be undertaken, the regime that is established for employment cases is bound to be influential in shaping any regime for litigation. It is therefore important that FOIL's views are heard now.

#### **Consumer issues**

A number of problems are set out in the consultation paper, some of them identified as a result of recent research by Professor Richard Moorhead.

DBAs are used by both solicitors and claims managers as there are no restrictions on rights of audience in employment tribunals. Consumers are at risk as obviously there is no costs shifting in employment cases and successful claimants pay their own costs.

The most common consumer problems identified are:

- No standard practice on the changing of VAT. Some agreements include VAT and disbursements in the 'percentage of damages' figure which the client agrees to pay, some agreements charge these on top of the percentage.
- Alternative methods of funding. Professor Moorhead's research has found that even though solicitors are obliged to discuss with their clients whether funding might be available through existing insurance or from a Trades Union, and claims management companies are also required to consider other methods of funding, in practice those requirements are seldom met and clients therefore do not have the opportunity to make an informed decision on funding.
- Inconsistency of the percentage charged. This can vary from 10% to 50%. The mean fee is between 31% and 33%. The percentage charged on smaller cases may be higher than for larger claims which can result in a claimant on low

earnings receiving a smaller percentage of already low damages. The agreement may or may not charge a lower percentage if there is no hearing. In group litigation, where the cost is spread across many cases, the cost to individuals may be too high.

- Penalty/exit clauses are said to be a common feature. These govern what happens if the client wishes to take the case to another representative or the client rejects the representative's advice on settlement, and can be unfair. For example, there is anecdotal evidence that clients who end their agreement can be charged £500 for each six month period the file has been open, regardless of the work carried out. Professor Moorhead reports that clients do not understand terms surrounding settlement. Some legal representatives take an alternative approach and offer a second opinion without charge if the client does not accept their advice. There are difficult issues here in balancing the client's and the representative's interests.
- At present there is no mechanism to enable clients to challenge the fees changed under a DBA.

### **Consultation questions**

- Research suggests that the present requirements for solicitors and claims managers to provide information to consumers on costs are insufficient. What additional requirements could be included to protect consumers?
- Do you agree that claimants should be able to challenge the overall costs under DBAs and, if so, how?
- Do you agree that representatives should provide a clear indication of whether VAT is included or excluded from the percentage of damages to be charged in fees? How should this requirement be framed (*Professor Moorhead takes the view that VAT and disbursements should be included in the percentage*).
- How should the requirement to give clear information about other charges such as disbursements be framed in the Order?
- How could the requirement for representatives to inform the claimant about alternative options for funding before accepting a case and entering into the agreement be better framed under the Order.
- Do you think that a general cap should be introduced to limit the maximum level of the percentage that could be deducted from the damages? If so, what should the appropriate maximum be?
- Should there be a sliding scale subject to some limits (e.g. where the case was settled prior to a hearing) to reflect the complexity of the case, the work done and the likely level of damages awarded, including a proportionate reduction per case where the individual claim forms part of a large group.
- Research shows that the use of settlement clauses (governing what happens when the client rejects advice on settlement) should be regulated; do you have any views on how this could be done?
- Should clients be able to challenge the charges under penalty/exit clauses and if so, how?
- Are there any other aspects of DBAs that ought to be regulated? If so, please specify what they are and why they need to be regulated, providing relevant evidence as appropriate.
- What should be the position of a DBA that fails to meet all the regulations? Should it be unenforceable? Should minor technical breaches be ignored?

### **Conclusion**

The issues raised in this consultation cover some very difficult ground. Some of the issues create an unpleasant feeling of déjà vu, so akin are they to the problems which beset the CFA regime during the years of the costs wars. Other issues are specific to the particular characteristics of the employment tribunal regime – a forum in which the

general rule of no costs shifting will almost always leave the individual claimant to pay his or her own costs, and therefore where any action to challenge a DBA will have to be recognised as appropriate and be commenced by the claimant; and where the average award is less than £20,000, leaving little room for manoeuvre when deciding how much should be paid in costs.

There would seem to be three major issues raised in this consultation which are of interest to FOIL because of the potential for them to seep into the personal injury regime through an extension of the use of DBAs:

- To what extent should specific regulations on information to be provided to claimants and rules on specific terms in the agreement be introduced? Having been through a prescriptive regime with CFAs and come out the other side with *Hollins v Russell* and the revocation of the CFA regulations, what should be the approach in drafting regulations for DBAs?
- How should the issue of limiting the percentage of damages which can be taken in costs be approached? The old Law Society rule for CFAs, until the issue was swept away by recoverable additional liabilities, was straightforward – the claimant would receive at least 75% of damages. The idea floated in this consultation is that it might be possible to bring together all the different risk factors and issues which impact upon how much the lawyer is paid and create a 'sliding scale'. That would seem a tall order, but are there ways in which some of these factors can be reflected in regulations to protect the consumer?
- How do you balance the interests of the legal representative in wanting to keep the case himself once commenced, to enable him to obtain payment if the case is won; and the interests of the client in wanting to transfer the case if he believes that is more likely to lead to success? How do you handle the inevitable conflict between a legal representative who is not being paid on the basis of the work undertaken but only on the damages received, who will have an interest in wanting to settle at the earliest opportunity; and the interests of the client who is unlikely to know what an appropriate settlement figure is, is relying upon the advice of a representative whose interests do not necessarily accord with his own, and yet who may be acting unreasonably in pushing for a rejection of a settlement? Can the concept of offering a second opinion really work?

If you have any views or comments on the issues please contact Shirley Denyer at [shirley.denyer@foil.org.uk](mailto:shirley.denyer@foil.org.uk) by 11 September.

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