

## Legal Services Board

### Referral fees, referral arrangements and fee sharing

#### Summary

**Note** – Aviva has restricted its responses to Personal Injury. Aviva accepts there may be similarities in Conveyancing agreements but has no experience of these and so cannot comment on such.

- Aviva believes that the key underlying issue in this area is the overall level of legal costs. Whether these are fixed fees or hourly rates, they have been calculated to recover referral fees, and are therefore too high. Addressing the consumer detriment caused by excessive legal charges requires control of the overall level of legal costs as well as banning referral fees.
- Aviva disagrees that there is no compelling case for a ban on referral fees. We believe these fees should be banned as they actively harm consumers' interests.
- Aviva accepts that the disclosure and compliance problems identified are real. We do however take a different view from the LSB on their causes and potential remedies.
- Aviva adds a further view that an additional problem with regard to referral fees is a lack of compliance with the existing rules. In Aviva's opinion the Solicitors Regulation Authority has failed to adequately enforce the existing rules which have proven to be detrimental to the market.

These issues are explored in more detail below.

**Submission from:**

Dominic Clayden  
Director of Claims Technical & Supply Chain  
Aviva UK General Insurance  
Rosso 1  
Surrey Street  
Norwich  
NR1 3NS

**For further information please contact:**

Lynsey Todd  
Senior Claims Manager  
Aviva UK General Insurance  
Dixon House  
1 Lloyds Avenue  
London  
EC3N 3DH  
Tel: 0207 1572543  
Email: [lynsey.todd@aviva.co.uk](mailto:lynsey.todd@aviva.co.uk)

#### About Aviva

Aviva is pleased to respond to this consultation. Aviva provides peace of mind for more than 50 million people across the world, protecting their families and possessions and looking after more than £380 billion to help our customers save for the future.

More than 19 million customers rely on us in the UK – one in three of the population – and we insure 1 in 10 private cars. We have one of the largest insurance databases enabling us to use the data from millions of customers and thousands of claims to predict the likelihood of a future claim for any given customer and therefore give customers a fair price in relation to the risk they represent.

## Questions

### 1. Do you agree with our analysis of the operation of referral fees and arrangements?

#### Referral Fees

While Aviva does accept many of the issues raised in the discussion document, Aviva is of the opinion that the analysis is too simplistic and has not looked into all aspects of how referral fees truly operate and the full impact upon legal costs and consumers as a whole.

For example, the discussion document gives no consideration of how referral fees are recovered from a paying party's point of view and gives no objective analysis of the overall impact that referral fees have had in terms of increasing the cost of insurance premiums. The key issue from Aviva's perspective is that referral fees are paid by the losing party and that they have been directly factored into hourly rates and also fixed costs. That is to say that excessive referral fees are directly recovered through inflated charging structures and Aviva is very concerned that the LSB appears to have failed to grasp this important point.

The discussion document has also looked primarily at referral fees in the context of motor personal injury (PI) in the Predictable Fee Regime i.e. pre litigated sub £10K claims (5.10). While these undoubtedly form a large percentage of all personal injury claims, the document excludes litigation, "liability" claims (Employers Liability and Public Liability) and other claims in a non fixed fee environment. Aviva believes referral fees in such environments can far exceed the sums quoted in the discussion document and that these claims raise different issues which the LSB has not considered.

#### **Solutions: Banning referral fees and reducing recoverable costs (as referral fees are already built-in to current inflated fee structures)**

Aviva does not for the reason set out in detail below accept there is no compelling case for a ban on referral fees as suggested by the Consumer Panel and the LSB. We believe that referral fees should be banned. In addition, if any real progress is to be made with regard to referral fees and / or the perception of a 'compensation culture', then simply banning or capping the payment will result in very little change, as referral fees are already built-in to current inflated fee structures. We therefore believe that the LSB should link its recommendations to the recently announced Government consultations on civil litigation funding and the proposed further restriction of Legal Aid and directly tackle cost reduction.

It is Aviva's view (and we believe the view of all paying parties whether insurers, the NHS or a private person) that if a solicitor can afford in many personal injury cases to pay a referral fee of £800, this can only point to the fact that the legal fees, whether fixed or on an hourly rate, are simply too high. This cost is passed on to society as a whole through higher insurance premiums and increased costs to the NHS.

Aviva believes it is highly questionable that fees to the referrer at such a level (which is often as much as half of the total costs recovered by the Solicitor) can be justified when there is, in return, little or no actual service to the consumer. This view was set out clearly by Lord Justice Jackson in his preliminary report and is a side-effect of the failure of the civil litigation system to have delivered proportionate costs in many cases.

Aviva would like to make clear to the LSB that, as a major UK insurer and underwriter of legal expenses insurance, Aviva receives income from the referral of bodily injury claims. If Aviva did not do so the underlying cost of policies would have to rise, making Aviva insurance products un-competitive in a market where referral fees are permissible and increasing the cost to consumers. We therefore operate in line with the commercial realities of the market as it currently operates.

There is much commentary around insurers arguing for a ban on referral fees and yet receiving referral income which may appear to be hypocritical. The Aviva position is that irrespective of any income Aviva receives today it would still welcome a ban **provided** there is a commensurate reduction in the level of recoverable costs.

Aviva, along with other insurers and the ABI have been actively campaigning for legal costs to be more proportionate and controlled. It is widely reported that 40p in every £1 paid out by insurers dealing with compensation claims goes toward legal fees. Referral fees are a major cause of this.

In addition the Oxera Report published by the ABI<sup>i</sup> highlighted that the marketing costs as a proportion of fees are higher in Personal Injury cases than any other sector.

It is Aviva's view that both hourly rates and the fixed costs under the Predictable Fees and MoJ RTA schemes are based on data which included referral fees. Also that the level of these fees are not truly representative of the actual costs the firms operating incur, even allowing for the costs of marketing that may need to be factored back into the fees.

The Advisory Committee on Civil Costs concluded<sup>ii</sup> that referral fees account for the whole of the difference between a claimant and a defendant's costs. When referral fees in Personal Injury claims were no longer banned in 2000 it was common for those fees to be in the region of £150 -£200. These fees are now commonly £800 to £1,000. We can see no justification for this increase.

To support this point, Aviva would like to refer the LSB to the recommendation of Lord Justice Jackson in Chapter 44 3.10 (ii) of his report in respect of the proposed Costs Council:

***“What reductions should there be in hourly rates for personal injury work, if referral fees are banned or capped, as recommended in chapter 20 above? I accept that firms will incur marketing costs, possibly at the rate of about £200 per case. But the present level of referral fees has grossly distorted the costs of personal injuries litigation”***

There has been a massive investment since 2000 and the Woolf Report in simplifying and standardising the handling of low value personal injury claims. These are the simplest of claims and Aviva's view is that the legal costs that are recoverable have not been reduced enough to reflect the level of automation and also reduction in the grade or level of fee earners who process these claims.

The LSB has also not in our view taken into consideration in any adequate detail the views of the Law Society Council who in 2009<sup>iii</sup> reversed the Law Society position and called for a ban on lawyers paying referral fees as they are not in consumers' interests.

Although Aviva agrees, it can see no evidence of solicitors who operate in this market failing to act independently (5.25) or in the best interests of their client. It remains Aviva's view that if up to £800 can be “gifted” by a solicitor to the referral agency, then contrary to the discussion document (5.9) this is clearly an inefficient system which does not serve the consumer who effectively “pays” for this via higher insurance premiums and also cost to the NHS.

Aviva would also like to draw the attention of the LSB to referral fees in EL and PL claims (where there is no fixed cost environment) which can exceed £1,500 per claim. This equates to a large number of solicitor chargeable units before the solicitor even begins to cover their own costs on a claim.

It is obvious to Aviva that this costs systems encourages cost building and we welcome the expansion of fixed costs proposed by Lord Young into this area. We believe that it is crucial however that there should be a proper assessment of the level of those costs excluding or limiting the level of referral fees.

## Disclosure

Aviva also accepts that the disclosure and compliance problems identified are real. We do however take a different view from the LSB as to their causes and potential remedies which are outlined below.

We believe, contrary to the assertions at 5.20, that the forthcoming creation of Alternative Business Structures (ABSs) via the Legal Services Act will result in many commercial / referral fee arrangements becoming “absorbed” into these new business models. As a consequence Aviva believes that the situation may actually become worse from a consumer perspective, in spite of the LSB's proposals for increased transparency and regulation.

If the Legal Services Board intends to control, rather than ban, referral fees then we believe that this will only be possible if the actual **total** legal fees recoverable in all types of claim and litigation are controlled and / or reduced. Only this will result in lower referral fee payments being available and help to reduce the perception of a compensation culture upon which Lord Young has recently reported.

The discussion document fails to note that insurers and the solicitors used for defendant litigation have worked together to actively reduce their costs base and fees. As a result this market is controlled, efficient and profitable for the firms involved.

By contrast, there has been little or no commercial pressure and proportionality applied to claimant solicitors' fees. Lord Justice Jackson in his report of 2010 recommended that a Costs Council be established to review guideline hourly rates and the levels of fixed costs. Aviva notes that this has still not been established and therefore there is effectively no operating body, which should have a key function in controlling costs.

Although Aviva has broadly welcomed the recommendations of Lord Justice Jackson, it remains our view that most of his proposals will, at best, only cap the level of legal costs recoverable going forward. Many of the fixed costs outlined in his report are based on legal costs which the paying party already considers are excessive.

We do however agree with the argument (at 5.15 in the discussion document) that consumers will benefit if given a financial interest in litigation – something which the present Conditional Fee Agreement (CFA) regime removes. We believe that this is likely to increase competition.

Aviva questions the numerical data which the LSB has obtained at 5.30 and 5.31 as being too low. That said however, Aviva agrees that while the number of RTA's has fallen over time and hospital admissions have fallen, associated injuries have increased significantly.

Aviva concurs that referral fees have been partially responsible for this increase but also notes that fraudulent claims are not mentioned in this discussion document. The Insurance Fraud Bureau (IFB) believes that there may have been as many as 30,000 fraudulent RTA claims in 2009 (IFB data). It is Aviva's view that referral fees have clearly influenced this behaviour by encouraging Claims Management Companies to induce solicitors to take on "spurious" claims knowing that their rewards for so doing can be great.

### **Conclusion**

Aviva therefore believes that the LSB should not simply accept that referral fees are in consumers' interest, but should instead be recommending a more balanced review of the payment of referral fees and the level of the underlying costs that are recovered which fund the payment of referral fees.

If the LSB does not look at these issues, we believe it will have only considered half of the equation and will not have tackled the overall compensation culture and rising civil litigation costs which Lord Justice Jackson and Lord Young are currently discussing.

Aviva believes that the LSB has a vital role to play on this issue, but to do so effectively; the LSB must make sure that it is able to demonstrate it is taking an over-arching view. The LSB must then work effectively with all the stakeholders to make substantive progress in this area.

### **2. Do you have additional evidence about the operation of referral fees and arrangements that should be considered by the LSB?**

While Aviva has outlined its main views on the operation of referral fees in response to question 1, Aviva has a further observation it considers should be taken into account.

Aviva considers that there is a general lack of compliance with the existing rules which relate to the disclosure of referral fees and referral arrangements. We believe that the Solicitors Regulation Authority (SRA) has failed to adequately enforce the existing rules and this failure has been to the detriment of the consumer and caused a lack of transparency.

We believe that the existing rules and the guidance are already sufficiently clear for both Introducers and Solicitors. We note there is no reference in the LSB discussion document as to where the existing rules are unclear or any suggestions made as to how they could be made any clearer.

Aviva has taken steps to ensure that any of our referral arrangements comply with The Introduction and Referral Fee Code<sup>iv</sup>. In spite of the Code, we are not aware of any individual Solicitor or firm of Solicitors having ever been disciplined for failure to comply with these rules. It is certainly not a common occurrence. In such a lax atmosphere, it is unsurprising there may be transgressions or at best “borderline” compliance.

While Aviva agrees that the LSB has rightly highlighted issues relating to the rules and enforcement issue, we do not consider the existing rules are necessarily inadequate or lack transparency from a consumer perspective if they were enforced correctly. The LSB makes one of its primary recommendations aimed at increasing regulation and transparency – Aviva however is firmly of the view that the LSB must also send out a clear message to the Solicitors Regulation Authority to immediately improve their monitoring and Solicitors performance around disclosure as otherwise nothing will change.

### **3. Do you agree with our analysis of the operation of referral fees or fee sharing arrangements in criminal advocacy?**

Aviva does not have any experience in this area and is therefore unable to comment upon the discussion.

### **4. Do you have additional evidence about the operation of referral fees or fee sharing arrangements that should be considered by the LSB?**

Please see Aviva’s response to question 2.

Aviva contends that the Solicitors Regulation Authority (SRA) has failed adequately to enforce the existing rules, and it is this failure which has contributed to the market being in its current state.

Although we believe that the existing rules and the guidance are already clear (there is no reference in the LSB discussion document as to where the existing rules are unclear or any suggestions made as to where they could be made any clearer), we are not aware of any individual Solicitor or firm of Solicitors having been disciplined for failure to comply with these rules. In such an atmosphere, it is unsurprising that there may be transgressions or “borderline” compliance.

Aviva agrees that there is a rule enforcement issue and is firmly of the view that the LSB should simply be sending out a clear message to the regulator to improve their performance.

### **5. In particular, do you have evidence about the impact of referral fees or fee sharing arrangements on the quality of criminal advocacy?**

Aviva does not have any experience in this area and is therefore unable to comment upon the discussion.

### **6. Will the proposals assist in improving disclosure to consumers?**

#### **Recommendation 1 - Improving transparency and disclosure for consumers**

Aviva considers that the first two objectives set out in respect of who the referral fee is paid to and the amount in pounds should already be provided to consumers. Aviva believes this is part and parcel of the

existing standards of compliance with the “Introduction and Referral Fee Code”. We believe, as set out in our response to question 2, this is primarily an enforcement issue for the SRA.

In terms of the suggestion that the legal services provider should disclose the right to shop around, this would not be applicable in every situation and may be practically very difficult to implement and apply. To illustrate the problem it is worth looking at the general practice of how and when referrals operate:

- Aviva sells legal expenses insurance and in order to control the cost of the product (and in compliance with the Legal Expenses Regulations 1990) a customer’s right to choose their own lawyer arises at the point of proceedings or where there is a conflict of interest.
- In the majority of referral arrangements this point of a case comes at a later stage long after the initial referral as the discussion document has highlighted at 7.8.
- In other arrangements especially those involving a “no win no fee” arrangement Aviva believes many consumers do not want to shop around because they simply do not know whom to contact and presently have limited financial risk in pursuing a claim.

Aviva considers it is highly unlikely that a “no win no fee” solicitor will recommend or encourage that the consumer shops around. In addition this suggestion realistically fails to appreciate that a consumer has no interest in shopping around as in such cases they have no financial risk (see 5.15). In addition this would become an enforcement issue for the SRA and without a change in the Solicitors Conduct Rules it will not have any affect.

We believe that the critical issue of the lack of any financial risk to the consumer has not been adequately addressed in the LSB Consultation paper, and has also not been properly researched by the Consumer Panel, who concluded that there was no consumer detriment to consumers as a result of referral fees. The conclusion that greater transparency would lead to lower charges for consumers is mis-informed and will not in itself reduce legal costs

The consumer, in our experience, is ultimately not interested in whether his/her solicitor is claiming £100 or £400 an hour because if he wins the insurer pays and if he loses the solicitor cannot recover his fees from the consumer. Therefore normal market pressures do not apply.

In personal injury claims almost all cases are now funded by a legal expenses insurer or on a no win no fee basis and therefore (unless the claim is fraudulent) it is extremely rare for a consumer to have any personal liability for their own or other party’s costs.

### **7. Are there other options for disclosure that Approved Regulators should consider?**

If LSB wishes to ensure that there is full transparency Aviva would suggest that provisions be made to make the payment of a referral fee conditional upon the written consent of the consumer.

### **8. What are the issues relating to the disclosure of referral contracts by firms to approved regulators and their publication by approved regulators?**

#### **Recommendation 2 – Improving transparency and disclosure in the market**

Aviva questions the conclusion of the LSB that publishing all agreements will create any economic efficiency and / or result in any lower charges for consumers. The discussion document has not given any explanation as to how the LSB anticipates that this will be the end result of publishing or how consumers will access this information. The discussion document also does not clarify how it will have any impact on a consumer who does not end up having to pay the referral fee in any event. The referral fees are embedded into the underlying costs that are paid by the paying party.

For the reasons stated above, Aviva therefore remains firmly of the view that as the consumer ultimately has no liability for the referral fee, this would not create any market forces or result in any reduction in the amount of legal costs being claimed from the paying party (defendant).

Many of the commercial agreements will be commercially sensitive and the level of referral fees paid in the market is already well known. There appears to be little benefit in actual specific arrangements being published. In our view the only realistic route is to improve disclosure and transparency on a case by case basis with each and every consumer of legal services, where a referral fee is involved.

In Aviva's view if referral fees are not banned with a commensurate reduction in legal costs, the better approach is for a mandatory form of words and even stricter disclosure to be applied as part of a revision to Rule 9<sup>v</sup> combined with template documents if necessary.

---

<sup>i</sup> Oxera Report 2009 ABI

<sup>ii</sup> Advisory Committee on Civil Costs 2009

<sup>iii</sup> Law Society Council Memorandum 2009

<sup>iv</sup> Introduction & Referral Fees Code 2008

<sup>v</sup> Rule 9 – Introduction and Referral Fee Code 1990