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Your reference

Our reference

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Discussion document on 'Referral fees, referral arrangements and fee sharing'. Zurich response

Zurich Insurance plc

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regularly to improve our service  
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Dear Mr Mackay,

By way of introduction, Zurich's UK General Insurance division is part of Zurich Insurance plc, and supplies personal, commercial and local authority insurance through a variety of distribution channels. Based at locations all across the UK, with large sites in Birmingham, Cardiff, London, Farnborough and Whiteley, the division employs approximately 4,200 people.

Zurich Financial Services Group (Zurich) is an insurance-based financial services provider with a global network of subsidiaries and offices in North America and Europe as well as in Asia Pacific, Latin America and other markets. Founded in 1872, the Group is headquartered in Zurich, Switzerland. It employs approximately 60,000 people serving customers in more than 170 countries.

As a major insurance and risk management provider in the UK, Zurich welcomes the opportunity to respond to this consultation. Please find our response to the questions posed. We hope this feedback assists the review. If you wish to discuss this in further detail with us, please do not hesitate to call me on Tel: 01489 561361.

Yours sincerely,

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of  
our reulation by the Financial

## Response to discussion questions

### Personal Injury Conveyancing

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

No, we do not agree with the analysis, nor conclusions reached in relation to referral fees in the personal injury market.

In his final report, Lord Justice Jackson Chapter 20 page 193 states

*"Referral fees constitute a major head of expenditure in personal injuries litigation, which claimant solicitors have to recover from defendants if they are to operate profitably".*

Zurich endorses the conclusions reached by the Association of British Insurers founded upon the evidence from the Oxera report. We believe that claimant law firms paying referral fees should be banned, and in tandem, legal fees should be reduced by a corresponding amount to ensure that any cost that is intended to reflect a supposed marketing or acquisition spend is adjusted to a more appropriate level. This will ensure that any transactional savings through improved efficiency of process by lawyers that come from banning referral fees are passed on and directly reduce the ultimate legal cost to consumers which has become increasingly disproportionate since 2004 at least.

The fact that the cost of referral fees has increased over time, further indicates that if claimant solicitors have been able to drive efficiencies as they contend, then this has not resulted in any savings to consumers in the form of reduced legal costs, because the present costs structure has referral fees factored into the fixed costs and hourly rates. The existing costs regime has in effect allowed the increase in referral fees/marketing spend, on that basis that the cost is passed on to the other party paying the claim.

The outcome from this business model, as observed by Lord Justice Jackson in his preliminary report on the Review of Civil Litigation Costs, is that there are too many 'middle men' involved, adding no value. In this scenario the following example can become the norm according to Jackson at page 203:

*"Under the present regime, solicitors are not competing to get business on price. Nor are they competing on quality of service. They are usually competing to see who can pay the highest referral fee. Such competition is not beneficial to claimants or indeed to anybody else, apart from the referrers. Where cases fall under the fast track fixed recoverable costs scheme in CPR Part 45, the amount of costs available is a fixed sum. The more of that sum is paid to the referrer, the less are the resources available to devote to the handling of the case. In the context of fixed costs the effect of referral fees is either to drive up the level of **fixed costs** or to **drive down the quality of service or both**".*

We believe that contrary to that reported in the LSB paper at 5.4 and 5.10, what happens in practice is that claimant law firms do not reduce their profits and deliberately attempt to move claims into a higher cost regime. In doing so they negate the function of the fixed cost regimes which is to deliver faster compensation to the injured party and keep legal costs to the minimum amount necessary.

The LSB paper reports at 4.28 that referral fees have probably led to higher insurance prices but that is not detrimental to consumers with valid claims. We believe this conclusion, fails to make the connection between an imperfect market model (such as operates here) continually driving greater legal cost. The ultimate cost is to the consumer as insurers pass that increased cost into their pricing structure raising premium prices across the board, in particular motor insurance because it is a legal requirement to have valid motor insurance. The rising price of motor insurance is of concern to the House of Commons Transport Committee which has recently canvassed the market for views on Motor Insurance premiums.

Motor Insurance is often referred to as one of the most competitive markets in the UK with price being the dominant feature for consumers. Whilst it is acknowledged that many insurers benefit from referral fees, this should not be read as a general acceptance of the model. It has become very difficult for insurers to compete in this market without participating in a referral fee scheme, which simply fuels the spiralling cost being paid by referrers and we see little factual basis for the LSB's view that prices paid will begin to decline.

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

Zurich agrees with the views expressed by Lord Justice Jackson and Lord Young in their respective reports. Both conclude that referral fees do not enhance access to justice.

Referral fees paid as a matter of routine is one of the factors which contribute to the high costs of personal injuries litigation. It is our view that the removal of the ban on referral fees in 2004 has not improved access to justice nor been of benefit either to claimants or to the providers of legal services, in the long term. The winners from the system are those receiving the referral fees, especially the middle man who has no interest in the efficient operation of a motor insurance market essential to the commercial interests of the UK economy.

If the payment of referral fees is banned, this should have the beneficial effect of reducing other undesirable practices including unsolicited targeting of potential claimants and the incidents of fraudulent or spurious claims. Legal firms that bulk buy referral claims with the aim to generate as many claims as possible to meet quotas creates the financial climate and incentive for legal firms to promote claims that have little or no prospect of success.

The Charles River Associates report at page 83 illustrates that whilst, RTA's have been declining, personal injury claims arising from motor accidents has increased from 400,000 in 2000/1 to 625,000 in 2008/9, which we would attribute to the sales technique of claims farmers in sourcing claims for onward transmission. In effect, the foundation for the "Compensation Culture"

**Conclusions - Criminal Advocacy**

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

No comment. Zurich does not have experience in this area.

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

No comment. Zurich does not have experience in this area.

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

No comment. Zurich does not have experience in this area.

**Recommendations For Improving Transparency And Disclosure**

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

Zurich has looked at the current position. In March 2004 the Solicitors Conduct Rules were amended to allow solicitors to pay referral fees, subject to certain conditions and safeguards. Current rules govern the referrals of business to and from solicitors.

- Rule 9.01 provides that, when making or receiving referrals of clients to or from third parties, a solicitor must do nothing which would compromise their independence or ability to act and advise in the best interests of their clients.

- Rule 9.02 includes additional requirements where a solicitor enters into a financial arrangement with an introducer. The agreement between the solicitor and the introducer must be in writing. Before accepting instructions to act for a client referred in these circumstances, the solicitor must give to the client in writing all relevant information concerning the fact that they have a financial arrangement with the introducer and the amount of any payment to the introducer which is calculated by reference to that referral.

Our concern is that there is a clear conflict of interest between the revenue stream generated by being the recipient of, or on, the panel of a Claims Farmer that the consumer interest may be subordinate to the financial income stream and operational process. The greater the cost of the referral fee, the less expertise and time can be devoted to the individual needs of the claimant.

If implemented, the transparency regulations, will give no more than minimal cause for optimism that full disclosure on referral fees would be given, at all or in a uniform way.

The minimum requirement to achieve transparency would be to model the FSA guidance which regulates the requirement for IFA's to provide information upon the financial rewards they obtain from the sale of investment products they recommend or refer to their clients.

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

Whilst we do not agree that referral fees cannot be banned, if they were not banned then we regard it as essential that over time it becomes a statutory requirement to provide information to consumers on the outcomes of compensation claims sold to a particular firm of lawyers by a referrer and the financial aspects of the referral arrangements they operate.

A requirement must be placed upon the lawyer to obtain the written consent from the referred claimant as a condition precedent for payment of the referral fee and as evidence that the claimant has received a full transparent disclosure of these arrangements.

The lawyer must then have a further obligation to maintain disclosable details of all contracts with referrers and the extent of any payments made under those arrangements, to the financial regulator.

This may also be of increasing significance in tightening up the handling procedures in new areas of claims administration such as the Road Traffic Act Portal which looks set to be extended from the motor arena to both Employers and Public Liability claims.

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

We see no legitimate reason as to why disclosure and publication by an approved regulator would be an issue.

#### **9. How should these issues be addressed?**

Please see our response to Q8. We see no reason why a conventional corporate governance regime cannot be established with a referral code of conduct (a series of compulsory obligations) to be enforced by the regulators. Those who do not agree to comply should face sanction, resulting in them being prevented from delivering claims management services.

#### **Recommendations For Delivering Active Regulation**

#### **10. Will the proposals assist in improving compliance and enforcement of referral fee rules?**

Absent a ban then these proposals may improve compliance and enforcement with rules but regulation must also be about achieving outcomes. To do otherwise would be to regulate for regulations sake.

**11. What measures should be the subject of key performance indicators or targets?**

Zurich would suggest using the measures built into the current MOJ process. The consumer needs transparency to compare the market and any metrics should reflect the law firm's performance in the market

**12. What metrics should be used to measure consumer confidence?**

Consumers should be able to view the performance levels of solicitors from the measures built into the MOJ process by the publication of individual performance data.