

# Damage-Based Contingency Fees in Employment Cases

## A Survey of Practitioners

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## Executive Summary

‘American-style’ contingency fees are often thought not to exist in the legal system of England and Wales, but in fact have existed for many years in employment tribunals (and other areas defined as ‘non-contentious’ business). Similarity with the American system is two-fold. Firstly, in employment tribunals there is generally no ‘loser-pays’ costs rule: each party normally bears their own costs. Secondly, in employment tribunals contingency fees can be ‘damages-based’: the adviser’s fee can be calculated as a percentage of damages.

The development of damage-based contingency fees (DBCFs) has been vigorously resisted in civil litigation for fear that American-style fees would open a floodgate of dubious litigation which corrupted the quality and ethics of our legal system. Intriguingly, whilst tacitly permitted, the introduction of DBCFs outside of court-based litigation has escaped regulatory attention. As such, employment tribunals present an interesting example of the apparent Americanisation of a significant element of our justice system. It is also an area that is significantly under-researched. We know very little about how DBCFs operate in England and Wales.

This Study aims to go some way towards rectifying that absence of knowledge. It provides in-depth data on the use of ‘American-style’ DBCFs amongst employment practitioners based on a telephone survey of 191 employment specialists working in solicitors firms and claims consultancies. It also reviews existing literature and conducts original analysis of the Survey of Tribunal Applications (SETA) data 2003. It concludes that:

- Access to justice in employment tribunals has long been subject to criticism. Inequalities in representation are well established. This study further deepens our understanding, estimating that within our sample the level of specialist resources devoted to assisting and representing employers is roughly three times of that devoted to employees.
- The impact of DBCFs on the overall number of employment claims pursued is uncertain. Increases in employment tribunal applications are significantly related to other underlying factors.
- DBCFs have probably made a modest contribution to access to justice in employment tribunals ensuring that some applicants have access to advice and representation when they would otherwise not be able to afford it.
- The situation in equal pay cases is more complex. The number of cases linked to DBCFs is probably much higher but the evidence is not consistent with DBCFs giving rise to more claims of poor merit. DBCFs have exposed significant tensions between the individual and collective resolution of complex pay situations.
- Any contribution to access to justice is not uniform: lower value claims and claims with high levels of risk or cost associated with them are less likely to be brought.
- The claim that DBCFs lead to an increase in spurious or weak claims is not borne out by the weight of evidence currently available.
- There is no evidence to support the view that the percentage fees charged under DBCFs are generally excessive.

- There is evidence, however, that approaches to charging DBCFs are not consistent and may be likely to lead to consumer confusion and detriment, particularly as regards VAT, disbursements and recoupment.
- DBCFs appear to encourage earlier settlement of cases and, in particular, may encourage settlement as opposed to pursuance of claims to tribunal. Whilst there are often benefits in earlier settlement, which may ensure settlement is proportionate, it is debatable whether the ‘pressure to settle’ inherent in DBCFs leads to cases being compromised inappropriately. There is some evidence that on occasion it may do so.
- Firms’ contractual arrangements, particularly around settlement decisions in DBCF cases, generally effectively ‘handcuff’ the client to their lawyer’s advice. The consequences of rejecting such advice can be serious both in terms of the impact on their representation and in respect of debts that fall due. Conversely, firms have a legitimate interest in protecting their financial position.
- Whether the protections taken are appropriate is open to debate and should in particular be debated by the professions, their regulators and consumer groups. A solicitors’ duty not to place themselves in a conflict situation with their client; the apparent risk that DBCFs *may* give rise to such conflicts; and, the tendency of such ‘handcuff’ clauses to reinforce the power of advisers (in situations of potential conflict) require scrutiny of such rules to be searching.
- The survey did not provide evidence that the marketing practices used by DBCF practitioners was generally more aggressive than other practitioners.
- Solicitors raised issues about the competence and practices of claims consultants. This would benefit from fuller scrutiny.

It is important to acknowledge that survey data has limitations. In particular, what people say they do and what they actually do can differ, sometimes significantly. We have sought to address this through triangulating our findings with SETA data and the broader literature on contingency fees where possible. Additional work, funded by the Nuffield Foundation, is being carried out on funding in employment cases. This is looking at claimant perceptions of different funding arrangements. The Ministry of Justice are also considering conducting work looking more generally at the role of no win no fee agreements, which may include further work on DBCFs. Similarly, save where we specifically indicate otherwise, our study does not directly address all the issues associated with the use of DBCFs in equal pay cases. This is an area where the multi-party nature of the claims and the apparent fact that the majority of claims appear to remain unresolved mean we would be warier about applying our general findings to the specific dynamics of equal pay cases without further research.

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# 1. Introduction

1. In England and Wales, contingency fees are an increasingly important, and persistently controversial, element of the funding landscape for legal services. Colloquially known as ‘no win, no fee’ agreements, contingency fee agreements fall into two types:
  - 1.1. Conditional Fee Agreements (CFAs) are permitted in most areas of litigation other than family and criminal law. Defined in more detail at para 10, the distinguishing characteristic of this species of contingency fee is that costs are calculated on the basis of the work done by lawyers (in terms of hours spent on a case).
  - 1.2. Damage-based contingency fees (DBCFs) are equivalent to American-style contingency fees. Here the distinguishing characteristic is that the fee is calculated on the basis of a percentage of compensation awarded or paid.
2. Whilst ‘no win, no fee’ implies a services that is without charge, it is important to emphasise that ‘no fee’ has a specific meaning which depends on the approach of the advisers involved. The phrase does not specify the charges that may be levied if one *does* win. Further, even if one loses, certain charges may be levied which are not defined as a ‘fee’ (see para. 16 and para 154 onward). An apparently simple system can lead to nasty surprises for those who think that no win no fee means there will always be nothing to pay.
3. Interestingly, when CFAs were being introduced, DBCFs were ruled out as a form of funding for litigation conducted through the courts. Nonetheless, their use has occurred outside of litigation. Importantly, this has arisen without significant or specific regulatory oversight (see further para. 12 onwards). In policy terms, this is peculiar: litigation through the courts cannot be funded by paying lawyers damage-based contingency fees, proceedings through the tribunal system, however, can be funded by paying lawyers damage-based contingency fees.
4. This ‘back-door’ entry of DBCFs into the English system is doubly interesting because, in spite of the proclaimed controversies of American-style DBCFs, there has been remarkably little research on their use. Capable of being used in a wide-range of contexts, including benefits and child support cases, they appear (on anecdotal evidence) to be most common in the context of employment cases. Latterly, their use in equal pay cases has become particularly controversial.

## **The Focus of this Study**

5. As a result, this study takes as its focus the use of DBCFs in employment cases. As will be discussed in the next section, the research done to date in the area concentrates on claimants. This research takes a different approach, looking at practitioner perspectives. It does so from both a claimant and defendant angle.
6. We interviewed 191 employment advisers: those working in solicitors firms and in non-solicitor settings (where they do claimant work we refer to these generically, for convenience, as claims management consultants (CMCs)). The study aimed to look at a number of issues:
  - 6.1. To provide data from practitioners on the extent to which they use damage-based contingency fees in employment cases;
  - 6.2. To provide data from practitioners on the nature of the agreements they use;
  - 6.3. To understand the types of cases in which damage-based contingency fees are (or are not) used;
  - 6.4. To consider the pros- and cons- of using damage-based contingency fees from the perspective of practitioners; and,
  - 6.5. To consider any broader issues practitioners believe damage-based contingency fees raise in practice.
7. This survey contains information across a range of firm sizes and practice types and looks at issues of general interest to those looking at employment work or legal practice. The issue of marketing, a particularly vexed topic in the context of no win no fee, and ethical issues (e.g. around conflicts of interest, the charging information provided to clients and settlement) are also covered.
8. As far as we are aware, it is the first study of its kind and it contains detailed and valuable information on employment practice generally and DBCF practice in particular. As ever, there is potential for much more to be done both in terms of gaining objective information about costs and outcomes on such cases and in understanding client, practitioner and other stakeholder viewpoints. The authors are currently engaged in a study looking at claimant viewpoints and at the time of writing the Ministry of Justice are considering whether to

commission work on no win no fee agreements more generally, which may include further work on employment cases.



## 2. Some definitions and context

9. To simplify somewhat, no win no fee agreements are principally of two kinds. Whilst both kinds are formally ‘contingency fees’ we refer to the first kind as conditional fees and the second kind as ‘damage-based contingency fees’. We use the generic phrase ‘no win no fee’ (NWNF) to refer to these two collectively.
10. **Conditional fee agreements** operate on the basis that the lawyer is paid nothing by the client if they lose and their full (hourly rate) fee plus an uplift (based on a percentage of the hourly fee) if they win. Under our civil litigation rules, the unsuccessful opponent would usually pay these fees, plus insurance (see below) and the client’s damages would be paid, often without deduction.
11. We define **damage-based contingency fees** as the lawyer being paid nothing for their costs if they lose and a fee based on the percentage of damages recovered or awarded for the client if they win. This is the common model of funding in the United States (and other jurisdictions). The damage-based contingency fee is usually paid from the client’s damages.
12. In England and Wales, damage-based contingency fees are not permitted in civil litigation for lawyers fees.<sup>1</sup> The reasons principally derive from a concern that damage-based contingency fees provide lawyers with too strong an interest in the result. This may have particular impacts on the cases they take on (the suggested likelihood that they may bring too many weak cases, for instance) and how they process those cases (with damage-based contingency fees being more likely, at least in theory, to lead to lower settling of claims). There are also European professional code obligations, which bind (for example) the Law Society and forbid a *pactum de quota litis* (cases where the lawyer takes a share of the result).<sup>2</sup>
13. Whilst, in principle, the same concerns apply equally to employment tribunal cases, some practitioners have developed a damage-based contingency fee-based element to their practice.

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<sup>1</sup> They are permitted for third party funding arrangements. See, Mulheron, Rachael and Peter Cashman (2008) *Third party funding: a changing landscape* 27 (3) Civil Justice Quarterly 312-341. The impact on the client may be similar but incentives on the funded lawyers may be quite different.

<sup>2</sup> CCBE (2006) *Code of Conduct for European Lawyers* (Brussels: Conseil des barreaux européens - Council of Bars and Law Societies of Europe), para. 3.3.1.

Initially questioned on professional ethics grounds, the Law Society permits such arrangements on the basis that tribunals are ‘non-contentious’ business and so the use of DBCFs is not prohibited either by Statute or by professional rules. Barristers appear to be prohibited from accepting work on the basis that tribunal work is litigation.<sup>3</sup>

14. The provenance of damage-based contingency fees in employment cases is an interesting contrast to the origin of CFAs. DBCFs developed through a somewhat contentious definition of non-contentious and without any significant regulatory attention. In contrast, the ‘legalisation’ of conditional fees was accompanied by much debate. Significant and onerous rules were put in place to regulate these agreements and, in particular, the information provided to clients. The rules, themselves designed to protect claimants from inadequate costs advice from their lawyers, were utilised by defendants in challenges to the enforceability of the agreements, anxious to avoid responsibility for fees in cases they had lost. These rules have subsequently been relaxed and largely shifted into the sphere of professional regulation. Nevertheless, it is fair to say CFAs have been highly visible and regulated and the opposite is true of DBCFs.
15. That is not to say that DBCFs have been without controversy. Commentators have accused them of, amongst other things: causing nuisance claims;<sup>4</sup> restricting access to justice only to the quick and easy cases;<sup>5</sup> creating a conflict of interest between lawyer and client (particularly in relation to settlement);<sup>6</sup> encouraging non-solicitors to become involved in employment claims;<sup>7</sup> and, promoting the use of aggressive advertising.<sup>8</sup>

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<sup>3</sup> <http://www.barcouncil.org.uk/about/instructingabarrister/fees/> and private communication with Bar Standards Board on file with author.

<sup>4</sup> Avery Katz, *The effect of frivolous lawsuits on the settlement of litigation* (1990) 10(1) *International Review of Law and Economics* 3; B. Clement, *Tribunals to crack down on ‘compensation culture’* *The Independent* (London 8<sup>th</sup> May 2000); B. Clement, *‘Compensation culture’ sweeping Britain* *The Independent* (London 13<sup>th</sup> September 2004).

<sup>5</sup> Jane Johnson and Geraldine Hammersley, *Access to justice: employment tribunal contingency fees, what chance of justice?* (2005) 14 *Nottingham L.J.* 19, pp.25, 28; H.M. Kritzer, *Contingency fee lawyers as gatekeepers in the civil justice system* (1997) 81(1) *Judicature* 22.

<sup>6</sup> Geraldine Hammersley & Jane Johnson (2004) *The Experiences & Perceptions of Applicants Who Pursue Claims at Employment Tribunals*, paper presented at Work, Employment & Society Conference, UMIST, 1-3 September 2004, [http://www.britisoc.co.uk/user\\_doc/Hammersley.pdf](http://www.britisoc.co.uk/user_doc/Hammersley.pdf) last downloaded 11 July 2008 pp.12-13; Geraldine Hammersley, Jane Johnson and David Morris (2007) *The influence of legal representation at Employment Tribunals on case outcome* (London: BERR) p.15 (though see also observations at p.18); Johnson and Hammersley (2005) cited note 5, pp.26-7; G.P. Miller, *Some agency problems in settlement* (1987) 16 *Journal of Legal Studies* 189; P.L. Latreille, J.A.

16. On the other hand, the arrangements have been credited with increasing access to justice.<sup>9</sup>

On the face of it, DBCFs are also considerably simpler than CFAs. There are not the complications engendered by ATE premiums and the associated costs recovery and success fees are calculated by reference to a clear outcome (a percentage of compensation) not some unpredictable ‘base cost’ based on hours worked. Nevertheless, the idea that a client pays nothing if they lose and only pays costs out of compensation of a fixed proportion (say 30%) if they win, can also be wide of the mark. There remain issues around the funding of disbursements and deductions from compensation payments. VAT may also complicate the picture.

17. As an example, let us assume the damage-based contingency fee is defined as “30% of compensation”. The following questions might arise: is this inclusive or exclusive of VAT? Is it 30% of compensation awarded/agreed or 30% of compensation actually paid to the client? What happens if deductions are made for benefits for example? What is the situation with disbursements? Are they paid out of the 30% paid to the lawyer or out of the remaining 70%? This research seeks to establish data on employment lawyers' common practices on these issues. Similarly, we examine the extent to which the agreement structures decisions to proceed with or settle cases by looking at the extent to which DBCFs use clauses to bind the client to their lawyer’s decision on settlement (sometimes referred to as ‘handcuff’ clauses).<sup>10</sup>

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Latreille and K.G. Knight, *Making a difference? Legal representation in employment tribunal cases: evidence from a survey of representatives* (2005) 34(4) I.L.J. 308, at 310, quoting B. Hay and K.E. Spier, *Settlement of Litigation* in P. Newman (ed.), *The New Palgrave Dictionary of Economics and the Law* (Macmillan, Basingstoke 2002) p.442 (see also pp.444-6).

<sup>7</sup> See, for example, R. Jones, *Cowboy advisers targeted: Inquiry into claims malpractice* *The Guardian* (London 13<sup>th</sup> August 1999); S. Webster, *Age of the no win, no fee outfits*, *The Times* (London 4<sup>th</sup> October 1994) (these articles are predominantly concerned with personal injury cases but there is some reference to employment cases).

<sup>8</sup> See, for example, Hammersley and Johnson (2004) cited n6, p.14; J. Sherman, *Men are to pay a high price for sexual equality* *The Times* (London 12<sup>th</sup> March 2007).

<sup>9</sup> Hammersley *et al* (2007) cited n6, p.20-21; Johnson and Hammersley (2005) cited note 5 , p.28.

<sup>10</sup> Clauses that bind the DBCF client to their lawyer take a number of forms: e.g. requiring compensation payments to be paid over to the lawyer rather than the claimant; requiring clients to accept reasonable advice on settlement; requiring certain payments be made when advice on settlement is rejected; and termination of retainer.

## Cost rules

18. There is a further important characteristic of cases brought in employment tribunals that distinguishes them from cases brought in the courts of England and Wales. In court cases, costs usually follow the event and many of the costs associated with CFAs are recoverable from unsuccessful opponents. In tribunal cases, the situation is that ordinarily each party bears their own costs. This means that any compensation recovered by a claimant will be reduced by any payments made to their lawyer. In respect of costs, the situation is more analogous to tort cases in the United States than it is to civil cases in our courts.

## The research base on damage-based contingency fees

19. It has already been suggested that a regulatory focus on DBCFs has been lacking. The same is true of research in this jurisdiction. When first introduced, conditional fees were controversial. Research looked in detail at the extent to which consumers were fairly treated by lawyers under the agreements and could understand the agreements they were being asked to sign up to. The general thrust of this work was that they were not fairly treated and they could not understand the costs situation.<sup>11</sup> Fenn and Rickman employed econometric approaches to assess whether the lawyer's behaviour under conditional fees (in particular the cases they were willing to take on and the damages they would settle for) changed in any way.<sup>12</sup> Moorhead examined the implications of replacing legal aid with CFAs.<sup>13</sup>

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<sup>11</sup> Yarrow, Stella and Pamela Abrams (1999) *Nothing to Lose: Clients' experiences of using conditional fees* (London: University of Westminster); Yarrow, Stella (2000) *Just rewards: The outcome of conditional fee cases* (London: University of Westminster).

<sup>12</sup> Fenn Paul and Neil Rickman (2003) *Costs of low value RTA claims 1997 – 2002*. A report prepared for the civil justice council. And Fenn, Paul, Dev Vencappa, Chris O'Brien Stephen Diacon (2005) *Is there a "compensation culture" in the UK? Trends in employer's liability claim frequency and severity*, paper presented to the Association of British Insurers, December 8<sup>th</sup>, 2005: [http://www.nottingham.ac.uk/business/cris/papers/ABI\\_presentation\\_011205%20.doc](http://www.nottingham.ac.uk/business/cris/papers/ABI_presentation_011205%20.doc) last downloaded 23<sup>rd</sup> September 2008; Fenn, Paul and Neil Rickman (1999) *Delay and settlement in litigation*. 109 *The Economic Journal* 476 – 491; Fenn, Paul and Rickman, Neil (2003) *Calculating reasonable success fees, Report to the CJC*, September 2003; Fenn, Paul and Rickman, Neil (2003) *Costs of Low Value RTA Claims, 1997-2002*, Report to the CJC, January 2003 and Fenn, Paul and Rickman, Neil (2007) *Monitoring the Fixed Recoverable Costs Scheme, Parts I and II*, Report to the CJC, September; Fenn, Paul, Alastair Gray, Neil Rickman and Howard Carrier (2002), *The Impact of Conditional Fees on the Selection, Handling and Outcomes of Personal Injury Litigation*, Lord Chancellor's Department Research Series No. 6/02; Fenn, Paul, Dev Vencappa, Chris O'Brien Stephen Diacon (2005) *Is there a "compensation culture" in the UK? Trends in employer's liability claim frequency and severity*, paper presented to the Association of British Insurers, December 8<sup>th</sup>, 2005: [http://www.nottingham.ac.uk/business/cris/papers/ABI\\_presentation\\_011205%20.doc](http://www.nottingham.ac.uk/business/cris/papers/ABI_presentation_011205%20.doc) last downloaded 23<sup>rd</sup> September 2008; Fenn, Paul, Gray, Alastair, Rickman, Neil and Mansur, Yasmeen (2005) *The Funding of Personal Injury Litigation: Comparisons Over Time and Across Jurisdictions*, Report to the DCA, October 2005.

20. The research base on DBCFs in this country is much smaller but worth commenting on in some detail. What little empirical work that has been done on DBCFs in employment cases has concentrated on limited data from clients.<sup>14</sup> In particular, this has suggested that damage-based contingency fee clients are not generally more dissatisfied with their case outcomes than other clients; may have overly-optimistic views about the prospects of success of their cases; may be less satisfied with settlement (and more likely to settle than under other funding mechanisms); but are not more likely to have instructed an adviser because of cold-calling. There are also some interesting indicative findings around what one might call the moral economy of damage-based contingency fees. Damage-based contingency fee claimants did not appear to be more likely to be motivated by monetary concerns in making a claim. There is also interesting evidence that DBCFs are more likely to be taken on in higher financial value cases.<sup>15</sup> The authors of that study are judiciously cautious about their findings, using forms of analysis which are “exploratory” and which have, “done little more than identify some of the key variables in the choice of contingent fee arrangements.”
21. The same data source, the (then) DTI’s Survey of Employment Tribunal Applications (SETA), has given rise to a limited<sup>16</sup> estimate of the prevalence of damage-based contingency fees in employment tribunal cases of 11% and some indication of the cases where damage-based contingency fees are likely to be more prevalent (discrimination, unfair dismissal and standard conciliation period cases). They also provide data on the level and proportion of costs which is deducted from damages, although their reporting of this is not clear.<sup>17</sup> Hammersley and Johnson also conducted a small postal questionnaire based study of employment tribunal applicants, which found that those represented under no win no fee agreements were put under pressure to settle and were generally unhappy with the quality of
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<sup>13</sup> Moorhead, Richard (2002) *CFAs: A Weightless Reform of Legal Aid?* (2002) 53/2 Northern Ireland Law Quarterly 153-166.

<sup>14</sup> Geraldine Hammersley & Jane Johnson (2004) and Hammersley *et al* (2007) both cited note 6.

<sup>15</sup> See Hammersley *et al* (2007) (cited note 6) pp. vi, 14.

<sup>16</sup> The estimate is based on a problematic definition of damage-based contingency fee, see Hammersley *et al* (2007) (cited note 6) for details. It is also now significantly out of date. At the time of writing, fresh data is being collected by BMRB for the DTI’s successor body BERR.

<sup>17</sup> Hayward, Bruce, Mark Peters, Nicola Rousseau and Ken Seeds (2004) *Findings from the Survey of Employment Tribunal Applications 2003* (London: DTI) pages 40-41

their representation as well as only tending to have claims for £15,000 or higher (the latter finding in apparently contradicted by the Heyward et al study).<sup>18</sup> The study, however, is limited by reason of a low response rate and evidence that the survey had a response-bias towards those that felt aggrieved at the service they had received.<sup>19</sup>

22. Even in the Unites States, work on DBCFs is dominated by theoretical economic modelling rather than empirical data and it concentrates almost exclusively on medical malpractice and tort cases.<sup>20</sup>

23. It follows that the research base on the operation of damage-based contingency fees in employment cases is meagre. Very basic questions about the extent to which damage-based contingency fees are used in employment cases; the terms on which they are used; their impact on settlement and the like are unanswered. Because DBCFs may entail substantial deductions from claimant compensation a number of client protection issues arise. Further, because the client is paying for the services out of their damages, questions about the fairness and clarity of the arrangements are raised alongside issues of consumer understanding and perspectives on fairness. We turn to these issues in Chapter 4 and beyond. First we set out our methods.

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<sup>18</sup> Hammersley and Johnson (2004) cited note 6

<sup>19</sup> Hammersley and Johnson 2004 cited note 6, pp.11-12 and 14

<sup>20</sup> See generally the references at the end of this report. The works of Bert Kritzer, Stephen Daniels, Joanne Martin and Eric Helland and Alexander Tabarrok provide notable exceptions in that they rely on empirical data.

### 3. Methods

24. The project was based on conducting short, structured telephone interviews with practitioners who specialised in handling employment cases. We interviewed solicitors and non-solicitor providers of employment advice.
25. We contacted 400 employment lawyers working in solicitors firms. In identifying employment solicitors, we used the Employment Lawyers' Association web directory of members.<sup>21</sup> Members were randomly sampled from these lists, with one modification: where a member was sampled and a member from their office had already been interviewed the next member of the list was sampled. This ensured that we approached a wider range of solicitors' offices than would otherwise have been the case. Of the 400 lawyers, 62 were failed contacts: lawyers who had changed firms, who were on extended leave (typically maternity leave), or were otherwise untraceable.<sup>22</sup> Of the 338 remaining contacts, 170 either declined to participate or were impossible to contact.<sup>23</sup>
26. The response rate (excluding the failed contacts) was 50%, a very respectable figure for a telephone survey of busy professionals. Nevertheless, it was clear to us that some of those declining to take part in the survey did so on the basis that they do not do damage-based contingency fees (even though we made them aware we were nevertheless interested in their input). This is likely to mean that we have a bias towards those who *do* have some experience of damage-based contingency fees in our sample. We do not claim, therefore, that this sample is necessarily representative of all employment firms, but it does represent a wide and significant range of practice within the employment advice sector.
27. Those Claims Management Consultants that represent claimants have been subject to Part 2 of the Compensation Act 2006 and therefore required to be authorised and regulated by the

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<sup>21</sup> We investigated the Law Society directory but it was clear that this was going to give rise to us contacting a large number of lawyers whose firms held themselves out as doing employment law but were non-specialist. An advantage of the Employment Lawyers Association list was that they named individual lawyers who we could then contact direct.

<sup>22</sup> E.g. the ELA directory gave incorrect contact details and correct details could not be found.

<sup>23</sup> We rang 8 times before considering the practitioner impossible to contact, unless it became clear before this point that the practitioner was not going to respond.

Ministry of Justice since April 2007. Because we did not have telephone numbers for them, we contacted 124 Claims Management Consultants (registered on the Claims Management Companies register with the Ministry of Justice) by post. They were asked to return a slip indicating willingness to participate and also asked to provide their telephone numbers.<sup>24</sup> We contacted companies based in England and Wales claiming 'employment matters' as an area of work.<sup>25</sup>

28. We received 23 responses; 20 agreeing to participate and 3 declining; a response rate of 16% (including those who did not respond to the letter, although a proportion of these would not have actually conducted significant levels of employment work).
29. All those who participated were sent a letter and information sheet<sup>26</sup> setting out the research aims and inviting them to participate, making clear their participation was voluntary and that they could withdraw from an interview at any time. Their consent to participation was confirmed on the telephone before any interview commenced.
30. All interviews were conducted on the telephone according to the structured interview schedule (Appendix A: Interview Schedule). This mainly quantitative data has been analysed using SPSS. Some questions required, and all permitted, more free-flowing discussion. These discussions were contemporaneously recorded and have been analysed using NUD\*IST N6, a qualitative data analysis package, to ensure the themes emerging during these conversations are properly reflected in our analysis.
31. It is important to acknowledge that survey data has limitations. Whilst we had high response rates and our reading of the data suggests practitioners generally discussed their approaches with candour, there are limits. Practitioners may not always be able to describe accurately what they do and may also not wish to reveal particularly aberrant behaviour. We have been mindful of this in conducting our analysis and further address this through triangulating our

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<sup>24</sup> Telephone numbers were not available without this process.

<sup>25</sup> Entries were discarded where it was apparent that it was a company dealing solely with work-related personal injury cases. Repeated entries were also discarded, including where different branches of the same organisation were listed separately.

<sup>26</sup> On file with the lead author.

findings with SETA data (see below) and the broader literature on contingency fees where possible. We also recommend further research in this area and are conducting work on the perceptions of claimants funded by the Nuffield Foundation.

### **SETA data**

32. In addition to our data collection via the interviews we have conducted some original analysis of survey data collected for the (then) Department for Trade and Industry (DTI). This Survey of Employment Tribunal Applications (SETA) data dates from 2003 and covers a large random sample of completed employment tribunal applications. SETA data on employment tribunal applications contains data on case types, advice/representation and outcomes. It identifies claimants who appear to have brought cases using DBCFs and other sources of funding, albeit with some error (see below para. 228). That said, it may provide important insights into the impact of DBCFs on actual outcomes. It is important to emphasise that, unlike our interviews, the data is confined to cases where an employment tribunal application is issued: the results may not be typical of all employment claims.



## 4. Overview data on participants

33. This Chapter gives information on those who participated in the study. It also provides interesting data on the way employment work is structured within the sector. Furthermore it explains the basis on which we distinguish between size of solicitors' firm in subsequent analysis; team size and mix of work (claimant-respondent mix and contentious/non-contentious balance).

### Size of firm

34. Our data on size of firm is based on estimates given by interviewees for the number of partners (or owners, if the interviewee worked outside of a partnership);<sup>27</sup> solicitors; and other fee earners working within their organisation. It was clear that these figures were often estimates, particularly when asking those in larger firms about the numbers of solicitors and other fee earners they worked with. Nevertheless, the data provides a useful indication of the general size of practices we spoke to.

### Size of supplier organisations

35. Some indication of the nature of firms practising employment law who responded to the survey can be gained from Table 1 which compares the size of solicitors firms, as reported by respondents, with the size of solicitors' firms (whether or not they did employment law) as reported in the Law Society's Annual Statistical Reports.<sup>28</sup>

**Table 1: Size of Solicitors' Firms (as indicated by numbers of partners) responding**

|                  | Sole  | 2–4   | 5–10 | 11–25 | 26+ | All    |
|------------------|-------|-------|------|-------|-----|--------|
| Respondent firms | 10%   | 9%    | 22%  | 21%   | 38% | 100%   |
|                  | 15    | 13    | 33   | 32    | 56  | 149    |
| All Solicitors   | 44%   | 42%   | 9%   | 3%    | 2%  | 100%   |
|                  | 4,446 | 4,237 | 916  | 328   | 185 | 10,114 |

<sup>27</sup> Directors in LLPs, for instance, were treated as partners or owners.

<sup>28</sup> Cole, Bill (2007) *Annual Statistical Reports 2007* (London: Law Society).

36. 90 (47%) of our respondents were partners in law firms and 164 (86%) were solicitors. Of those who were not solicitors, 2 were trainee solicitors and 2 were qualified members of ILEX. Of the remaining 23 respondents, six had qualified as solicitors or barristers but were ‘non-practising’, five had legal training to degree or LPC level, and one was a practising barrister.
37. The Claims Management Consultants we interviewed were generally small. Three quarters were solely owned and the remainder had two owners. Most did not employ solicitors (two firms employed a solicitor and one employed six solicitors). Similarly in many firms the respondents were the sole fee earner. One CMC consisted of 200 fee-earners (including several solicitors). The next largest was 7 fee-earners in total.
38. Because partners/owners operate their organisations on very different gearing ratios, a more accurate indication of the size of the organisation is gained by looking at all fee earning employees within an organisation, be they partners, solicitors or other fee earners. A comparative indication of size can be seen in Table 2.

**Table 2: Size of claims consultants and solicitors’ compared (numbers of fee earners)**

|                       | Claims Consultants |     | Solicitors |     |
|-----------------------|--------------------|-----|------------|-----|
|                       | n                  | %   | n          | %   |
| Sole fee earner       | 11                 | 55% | 5          | 3%  |
| 2-7 fee earners       | 8                  | 40% | 21         | 13% |
| 8 or more fee earners | 1                  | 5%  | 136        | 84% |
| N                     | 20                 |     | 162        |     |

39. Solicitors clearly tended to be practising in larger organisations.
40. Missing from the above data are 9 solicitor respondents who were working in-house within, for example, businesses, trades unions, local authorities, advice agencies and the like. Given the heterogeneity of this group, we do not have data on the size of these organisations.

41. In the remainder of the report we talk about organisations in terms of their size, and this is based on splitting the sample of 182 organisations for which we do have size data into four groups:<sup>29</sup>

- 41.1. Those with 1 or 2 fee earners are identified as ‘tiny firms’.
- 41.2. Those with between 3 and 10 fee earners are identified as ‘small firms’.
- 41.3. Those with between 11 and 50 fee earners are identified as ‘medium-sized firms’.
- 41.4. Those with more than 50 fee earners are identified as ‘large firms’.

**Table 3: Firm Sizes Categorised**

|        | Claims Consultant |    | Solicitors |    |
|--------|-------------------|----|------------|----|
|        | N                 | %  | N          | %  |
| Tiny   | 15                | 75 | 12         | 7  |
| Small  | 4                 | 20 | 22         | 14 |
| Medium | 0                 | 0  | 54         | 33 |
| Large  | 1                 | 5  | 74         | 46 |
|        | 20                |    | 162        |    |

### How specialist were our respondents?

42. We had approached interviewees on the basis of some specialisation in employment law. To indicate how specialist they were respondents were asked how much time they spend doing employment work (in percentage terms). It was clear respondents were predominantly employment specialists. Most respondents were highly specialised. Three quarters spent 90% or more of their fee earning time doing employment work. Only 7% of respondents spent 40% or less of their fee earning time doing employment work. Unsurprisingly, given that most respondents were strongly specialised in employment, the profiles for claims consultants and solicitors were similar.

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<sup>29</sup> The labelling of firms as small (or whatever) is somewhat arbitrary and simply aids us in the analysis of data.

43. Most interviewees tended to concentrate on contentious work (half did 60% or more contentious work and about a quarter did 80% or more contentious work) although the profile of claims consultants and solicitors was somewhat different in this regard. All but one of the claims consultants spent 70% or more of their time doing contentious work. Only about 40% of the solicitors we interviewed spent 70% or more of their time doing contentious work. The average (mean) amount of time spent on contentious work by claims consultant respondents was 90%. For solicitors, the mean was 60%.

### **Team size**

44. As a proxy for team size, we asked respondents how many other fee-earners in their office did employment work. As with size, there were clear differences between Claims Management Consultants and solicitors. 12 (60%) of the CMC respondents had no other fee-earners who did employment cases. 29 (17%) of solicitor respondents were the only ones doing employment work. The remaining CMC respondents worked in teams of between 2 and 7 people. 93 (54%) solicitor respondents had a similar number of employment law colleagues. 49 (29%) had a larger number of colleagues. 15 (9%) had more than 15 employment law colleagues.

45. Team size may provide an interesting framework for analysis. With firms tending to monitor the profitability of departments, it is conceivable that approaches to the risks posed by DBCFs might relate to the size of team across which risks could be spread. To analyse this we categorised respondents as follows:

- 45.1. Solo 'team' of one person
- 45.2. Small Team (2 to 4 members in a team)
- 45.3. Medium-sized Teams (5 to 9 members in a team)
- 45.4. Large teams (10 plus members)

Table 4: Team Size

|                   | Claims Consultant |    | Solicitors |    |
|-------------------|-------------------|----|------------|----|
|                   | N                 | %  | N          | %  |
| Solo specialist   | 3                 | 38 | 25         | 18 |
| Small Team (2-4)  | 3                 | 38 | 37         | 26 |
| Medium Team (5-9) | 2                 | 25 | 38         | 27 |
| Large Team (10+)  | 0                 | 0  | 42         | 30 |
|                   | 8                 |    | 142        |    |

### Client mix: do they specialise in claimant or respondent work?

46. Another factor which we anticipated might affect approaches to employment work was client mix. 25 (13% of) firms said they solely did respondent work, and 10 (5%) specialised solely in claimant work. We are able to categorise firms on the basis of the level to which they concentrate on one type of work or the other and do so as follows:

46.1. Mainly claimant work (70-100% claimant work)

46.2. Mainly respondent work (70-100% respondent work)

46.3. Mixed practices (the rest)

47. Solicitors tended to concentrate on respondent work (Table 5). Claims Management Consultants were more likely to specialise in claimant work, but even so indicated that they did significant volumes of work for respondents.

Table 5: Mix of work by claims consultant and solcitors

|                                    | Claims Consultants | Solicitors |
|------------------------------------|--------------------|------------|
|                                    | %                  | %          |
| Mainly Respondent Work             | 25                 | 61         |
| Mixed Claimant and Respondent Work | 35                 | 25         |
| Mainly Claimant Work               | 40                 | 13         |
| N                                  | 20                 | 171        |

**Relative resources devoted to claimant and respondent work**

48. As firm size increases, there is a noticeable trend upwards in the proportion of firms doing mainly respondent work and a similar reduction in the proportion of those doing mainly claimant work.

**Table 6: Mix of work by firm size**

|                                    | Tiny | Small | Medium | Large |
|------------------------------------|------|-------|--------|-------|
|                                    | %    | %     | %      | %     |
| Mainly Respondent Work             | 26   | 35    | 43     | 87    |
| Mixed Claimant and Respondent Work | 44   | 42    | 37     | 8     |
| Mainly Claimant Work               | 30   | 23    | 20     | 5     |
| N                                  | 27   | 26    | 54     | 75    |

49. It is reasonably well-known that claimants are less likely to have representation than defendants. Hayward et al indicate:<sup>30</sup>

*Two fifths of applicants nominated a representative on the [then] IT1 form, compared with 55 per cent of employers on the [then] IT3. The most common source of help for both parties when completing the claim and response forms was a solicitor (44 per cent of applicants compared to 71 per cent of employers).*

*Fifty-five per cent of applicants and 59 per cent of employers used a representative to help with their case on a day-to-day basis. Employers were, however, more likely than applicants to be represented at a full tribunal hearing (72 versus 42 per cent).*

50. Information on the depth of advice and assistance provided to the two groups is less readily available. We were able to estimate the resources devoted within these firms to respondents and claimants respectively by multiplying the estimated proportion of work that is done for claimants by the number of team members. A similar calculation is then done for respondent work. From this it can be estimated that, within our sample firms, the equivalent of 117 fee earners were engaged in claimant work and 334 fee earners were engaged in respondent work.

<sup>30</sup> Hayward et al cited note 17, page xix

51. If we assume that these personnel were specialists and representative of employment specialists generally, this is a very significant differential in the extent to which specialist personnel are devoted to the work of respondents over claimants.
52. The analysis can be taken one step further by looking at the chargeable costs incurred on the two types of work by multiplying the fee earner equivalents above by 1100 hours (as an assumed number of chargeable hours per annum) and the hourly rate given by firms in estimating costs (see below). If claimant hourly rates are lower generally than respondent hourly rates this is likely to overestimate the fees generated by claimant work. Within this sample this suggests more than three times as much is spent on respondent work.
- 52.1.       £21.5m would be estimated as devoted to claimant work
- 52.2.       £70.7m would be estimated as devoted to respondent work
53. It should be emphasised that these are estimates only. A number of assumptions would have to hold true for them to be fully accurate. Nevertheless they provide an interesting indication of the legal resources being made available currently to claimants and respondents.

### **Summary**

54. As one would expect, the sample of employment lawyers we interviewed worked within a variety of practice settings and in a variety of team sizes. The mix of work also differed: solicitors were more likely to do non-contentious work than claims consultants. Respondent work is done across the sector but (again unsurprisingly) gravitates towards larger firms, which are more likely to solely or mostly do respondent work.
55. Concerns about access to justice are commonly reflected in concerns about the extent to which claimants are represented in employment tribunal hearings. Hayward et al's data indicates applicants are less likely to have nominated a representative; they are considerably less likely to get the help of a solicitor and be represented at a full tribunal hearing.<sup>31</sup> We were able to look at this issue in a different way by comparing specialist legal resources devoted to claimants and respondents in our samples. In our sample, the amount of resources we can

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<sup>31</sup> Hayward et al cited note 17

estimate as being spent on representing defendants outweighs that spent on claimants by roughly three times. This suggests a larger differential in support for claimants and defendants than is shown by simple indicators of whether or not someone has assistance or is represented.

## 5. Prevalence and use of DBCFs

56. This chapter looks at data on the prevalence and use of DBCFs; why firms do (or don't) use them; how long they've been using them for and other sorts of funding used for clients unable to pay privately.

### How many practitioners use DBCFs?

57. 127 respondents (66%) said they did not use damage-based contingency fees; the remainder did use damage-based contingency fees. Only 11% of those we interviewed used them in more than 50% of their cases. Although it is technically possible to devise a damage-based contingency fee for respondents, those we spoke to only used them with claimants. Use differs significantly for firm size, team size and emphasis of work (see Table 7 to Table 9).<sup>32</sup> Interestingly, whilst firms that are smaller and concentrate on claimant work appear more likely to do damage-based contingency fee work, it appears to be firms with small teams rather than solo specialists (or larger teams) which are most likely to use damage-based contingency fees. Conversely, some level of damage-based contingency fee work is prevalent in about half of all firms save in the largest firm category.

Table 7: Use of damage-based contingency fees by Firm Size

|  | Tiny | Small | Medium | Large | All |
|--|------|-------|--------|-------|-----|
|  | %    | %     | %      | %     | %   |
| No use   | 48   | 58    | 52     | 85    | 66  |
| Up to 25% use of damage-based contingency fees     | 22   | 23    | 37     | 13    | 23  |
| More than 50% use of damage-based contingency fees | 30   | 19    | 11     | 1     | 11  |
|  | 27   | 26    | 54     | 75    | 191 |

<sup>32</sup> Kruskal-Wallis,  $p = .000$  for each of these three variables.

**Table 8: Use of damage-based contingency fees by Team Size**

|  | Sole Team | Small Team | Medium Team | Large Team | All |
|--|-----------|------------|-------------|------------|-----|
|  | %         | %          | %           | %          | %   |
| No use   | 54        | 50         | 83          | 86         | 66  |
| Up to 25% use of damage-based contingency fees     | 43        | 30         | 15          | 14         | 23  |
| More than 50% use of damage-based contingency fees | 4         | 20         | 3           |            | 11  |
|  | 28        | 40         | 40          | 42         | 191 |

**Table 9: Use of damage-based contingency fees by Client Mix**

|  | Mainly Respondent Work | Mixed Claimant and Defendant Work | Mainly Claimant Work | All |
|--|------------------------|-----------------------------------|----------------------|-----|
|  | %                      | %                                 | %                    | %   |
| No use   | 85                     | 46                                | 35                   | 66  |
| Up to 25% use of damage-based contingency fees     | 13                     | 38                                | 32                   | 23  |
| More than 50% use of damage-based contingency fees | 3                      | 16                                | 32                   | 11  |
|  | 110                    | 50                                | 31                   | 191 |

### **Do barristers use DBCFs?**

58. We did not approach barristers to be involved in the survey. However, two participants commented that sometimes the barristers they instruct will work on a no win no fee basis, meaning that the client does not pay extra for counsels' fees where the case is lost. Presumably they mean that counsel uses a conditional fee agreement, as the Bar Council's guidance for barristers states that they cannot use damage-based contingency fees.<sup>33</sup>

<sup>33</sup> <http://www.barcouncil.org.uk/about/instructingabarrister/fees/>

However, another interviewee suggested that he works with a barrister who does conduct cases on a damage-base contingency fee; they will work on the case together and share the percentage fee.

### **How long have firms been doing damage-based contingency fee work?**

59. Our data suggests that damage-based contingency fees are not generally a new phenomenon. One respondent indicated that his firm had been using them for 20 years and over half of those who used them had been doing so for over five years. Although firms in the sample who used damage-based contingency fees in more than 50% of cases had been using damage-based contingency fees for longer on average (7 years) than firms using them up to 25% (5.5 years), the differences did not appear to be significant.<sup>34</sup>

**Table 10: How long have firms been doing damage-based contingency fee work?**

|                    | N  | %  |
|--------------------|----|----|
| 2 years or less    | 10 | 19 |
| 3-5 years          | 15 | 28 |
| 6-10 years         | 24 | 44 |
| More than 10 years | 5  | 9  |
| Valid responses    | 54 |    |

### **Importance of damage-based contingency fees to the firm**

60. We were interested in the importance of damage-based contingency fees to firm workload.

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<sup>34</sup> Two-tailed t-test,  $p = .230$

**Table 11: If it was not possible to use damage-based contingency fees, would firm's workload decrease?**

|                  | n  | %  |
|------------------|----|----|
| No not at all    | 14 | 23 |
| No not really    | 22 | 36 |
| Yes slightly     | 13 | 21 |
| Yes dramatically | 12 | 20 |
| Valid responses  | 61 |    |

61. The difference in results between firm sizes was not significant.<sup>35</sup> The same was true for team size<sup>36</sup> and balance of work.<sup>37</sup> Unsurprisingly where use of damage-based contingency fees was high the importance to the business (as indicated by impact on firm workload) was also high.<sup>38</sup>

**Other sources of funding**

62. Only 8 respondents (4%) reported doing work funded by Trade Unions, 6 respondents (3%) did some legal aid work with several pointing to the limited scope for funding of representation under the legal aid scheme.

**Why do firms not offer damage-based contingency fees?**

63. As already noted, the majority of firms (127) did not do damage-based contingency fee work. We discussed with them why they did not offer the arrangements, and the most common responses were as follows:

- 63.1. doing mainly/solely respondent work and considering DBCFs inappropriate for such a client base (mentioned by almost half of those not offering DBCFs);<sup>39</sup>

<sup>35</sup> Kruskal-Wallis, p = .140

<sup>36</sup> Kruskal-Wallis, p = .612

<sup>37</sup> Kruskal-Wallis, p = .239

<sup>38</sup> Mann-Whitney, p = .000

<sup>39</sup> 93 of the 110 firms that did mainly or solely respondent work made no use of DBCFs.

- 63.2. that the firm only acts for high net worth individuals who pay by the hour (mentioned by about a quarter);
  - 63.3. damage-based contingency fees present too great a risk (about a quarter);
  - 63.4. insufficient profit (about a fifth);
  - 63.5. lack of demand (that is clients were not asking for it, about a fifth); and,
  - 63.6. damage-based contingency fees gave rise to client relationship issues (about one in ten).
64. Cash flow, unfair profit, conflicts of interest, the widespread availability of legal expenses insurance (as an alternative) and reputation/image were also mentioned as reasons for not offering DBCFs.
65. This data suggests that the predominant reason for not conducting damage-based contingency fee business is the lack of any need to do so on a commercial basis. Whilst ethical, client relationship and other issues feature highly in debate, the main reasons given by our respondents were to do with the nature of the client base, the normal approach to funding respondent work and concerns about profitability and riskiness of damage-based contingency fee cases. However, there was also a strong underlying sense that lawyers ought, in a normative sense, to be paid for the time they put into a case. We discuss some of their reasons in more detail in what follows.

### **Respondent focused practices**

66. Unsurprisingly, one of the most common reasons for not using damage-based contingency fees was that the practice was solely or predominantly focused on respondents and therefore damage-based contingency fees were simply not considered.
67. Whilst we did not rule out the possibility that respondent damage-based contingency fees could exist in practice,<sup>40</sup> we did not expect the practice to be widespread. No interviewees used such arrangements with respondent clients and only one claimed to have come up

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<sup>40</sup> We are aware that there are the beginnings of such schemes in litigation and that they may become more important over time.

against opponents using such arrangements for respondents. The vast majority rejected the idea that respondent damage-based contingency fees could be employed. Where our respondents expressed a view as to why this was, the reasons given were: a presumption amongst respondents and their lawyers that they would be charged (and could afford to pay) on an hourly basis; and the view that damage-based contingency fees would be too complex to calculate on respondent cases (defining 'success' for the defendant in a way that was remunerative for lawyers would be difficult).<sup>41</sup> As one respondent indicated:

*Also, the 'contingency' in respondent cases would not so much be win/lose; you would have to get into debate about how badly you won/lost, which would be a completely different dynamic.*  
(IV261)

### **Use for high net worth claimants**

68. The economics of damage-based contingency fees might suggest that it is for high net worth individuals that DBCF cases might be most likely to be brought (high value compensation claims from which a sizeable fee could be taken as a percentage). It is interesting to note, therefore, that many firms who acted for such individuals stated that the fact that the claimant side of their business was confined to such individuals was a reason for *not* taking cases on a damage-based contingency fee basis. They often stated that the claimants they acted for were high net worth individuals who could afford the fees; the assumption being that such individuals are willing to fund their cases on an hourly rate basis. It did not appear that they routinely requested damage-based contingency fees, or that they were generally offered them.
69. Two interviewees pointed to the economic rationality of such claimants not proceeding on a damage-based contingency fee basis: IV113 gave an example: if you have a case settling for £200,000, 25% would yield £50,000. He considered that this would almost certainly exceed the legal costs they would charge, and so it is not beneficial for such a client to enter into a contingency arrangement. On this view, high net worth clients would be unlikely to accept such a reduction in compensation where this can be avoided through paying by the hour,

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<sup>41</sup> Only two interviewees ventured a specific model. IV76 would do an assessment of the [possible] loss in order to estimate the claim value. If he managed to prevent the claimant getting above a certain threshold then he would charge X% of the damages and if he did not manage to do this he would charge Y% of the damages. IV102 thought that you could use an alternative to damage-based contingency fees for respondents; he suggested charging a lower hourly rate up to the hearing and then charging an uplift fee if the case is successful.

unless their case was particularly risky. In such circumstances the practitioner would be unlikely to accept the risk.

### **Profitability**

70. It was practitioners from mainly claimant firms who said they did not to offer damage-based contingency fees because of insufficient profit. These considered that using an hourly rate was preferable because it provides a better financial return. Almost half of these attributed this in part to employment tribunal claims generally being of low value. Taking a percentage of a low value claim will not cover the effective hourly fees. IV195 suggested a claim worth £6,000 would be uneconomic if a firm is only paid a third (£2,000). This contrasts with the client's position if such cases are to be taken – having to pay an hourly rate at a commercial level presumably in excess of an 'uncommercial' 33% rate. Profitability, it was said, could also be affected by other matters: for example, claimants mitigating their loss by regaining employment would lower their lawyer's fee.

71. It may be that concerns about profitability are more common amongst practitioners working for firms charging higher hourly rates. Four interviewees explicitly mentioned their firms' high hourly rates and related this to the consequent lack of potential profit in contingency cases; another suggested that High Street firms were more likely to use damage-based contingency fees because of their lower rates.

### **No Demand**

72. A fifth of interviewees who did not do damage-based contingency fees noted a lack of demand for such arrangements from their firms' clients. Interviewees giving this answer generally mentioned their respondent and/or high net worth individual client base, although a small minority made no mention of either. As IV108 put it:

*Clients don't ask for contingency fees and so there is no sense in swapping an hourly rate for contingency fee agreements.*

73. These respondents appeared to subscribe to the view that damage-based contingency fees need only be offered where this is necessary to get work in. This was made explicit by IV13, who said that as a successful firm they do not have to offer the arrangements; he thought that only less successful firms needing to attract work would do so.

## **Risk**

74. Many practitioners discussed the uncertainty involved in bringing employment claims as a reason for not doing DBCF work. Many commented that it was impossible to accurately assess a claim's prospects of success. Thus contingency cases posed a significant financial risk, as practitioners could not be confident of winning. A few interviewees commented that prospects of success could only be determined with any accuracy once time and money has already been expended on a case, meaning that if a claim is then found to have low success prospects money has effectively been wasted. A couple of respondents considered that prospects of success constantly fluctuate.
75. Four practitioners noted unpredictability peculiar to employment tribunal decisions. A few other interviewees noted the danger that the client will omit, whether purposefully or not, factors key to assessing the claim's chances of success.
76. Conceptions of risk included the risk of getting nothing or getting low awards/settlements:

*We don't want to gamble on getting paid or on the amount that we will get paid." (IV276)*

*If your hand is chopped off it is clear how it happened and it is clear how much [compensation] is necessary. In contrast, in employment law there is a lack of clarity over how fair or unfair someone has been. (IV94)*

77. Occasionally risk was said to include the difficulty of predicting how long employment cases would last: this impacts on the costs incurred and therefore the net recovery made once a percentage fee is recovered, as well as the time over which the lawyers must incur work in progress costs on a case without getting paid.
78. For some this was not simply about economics but also partly a judgment that the risk present in bringing a claim should not lie with the service provider (the lawyer) but with the person electing to use that service (the client).

## **Client Relationship Issues**

79. One in ten of the practitioners not doing damage-based contingency fee cases mentioned client relationship issues as a factor in their firms' decisions. Interestingly, claims management consultants seemed more likely to mention this as a reason than those working in solicitors firms. Respondents from mainly claimant firms were also more likely to express concerns with client relationship issues than were those from respondent firms.

80. Two main themes emerged from those who did indicate this was a concern. Firstly, some claimed clients preferred the hourly rate fee structure. Offering such a structure, in their view, thus improved client relations. In this vein, some said that clients want cost certainty, i.e. they want to know how much they will pay for the work to be done (although we doubt that these clients would have been given precise estimates or quotations of the amount of time likely to be spent on a case so certainty in this context may be somewhat spurious). In a similar vein, IV109 suggested that clients wanted cost transparency: they liked to see exactly what was done and what they had spent on it. CM22 considered that clients can understand hourly rate fees, but that they find other methods of payment more difficult to grasp. Whether this is an accurate portrayal of client views or is a post-hoc rationalisation of the status quo is open to debate.
81. The second theme discussed was the contingency client's approach to his case. These interviewees considered that such clients were more likely to have an unproductive attitude towards their claims. Three practitioners explicitly noted the contingency client's lack of financial investment in his case and suggested that this would make a client less cooperative and more difficult to deal with. IV272 stated that fee paying clients tended to listen, to return calls and cooperate; he thought that the opposite would be true of contingency clients. IV271 noted that damage-based contingency fees would make settlement difficult; clients would want to proceed to tribunal because they bore no risk in doing so.<sup>42</sup> Two interviewees thought that using the arrangements would provoke a negative reaction from their predominantly respondent client base. IV272 said that if the firm offered damage-based contingency fees then their employer clients would think that they were "part of the [damage-based contingency fee] problem".
82. CM17 was concerned that he would not be able to provide top quality service if using damage-based contingency fees. He suggested that service quality is reduced because the practitioner has the worry of financial loss, thus encouraging him to adopt a policy of "going in for a quick few thousand". Similarly, IV151 considered that in his experience the quality of representation and service provided by contingency practitioners was often poor.

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<sup>42</sup> This is only partly correct. While clients bear little or no costs risk, they still bear the risk of losing outright.

### **Conflicts of Interest**

83. Less than one in ten of the interviewees not using damage-based contingency fees stated that their firms do not use the arrangements because of the conflict of interest they create between client and solicitor. These participants considered that the contingency practitioner has a personal interest in the case; namely that the hours put in and compensation received should balance to ensure a profit. The practitioner may thus take decisions to realise this aim when this may not be in the client's best interests. For more detailed discussion of this issue, see Chapter 10.
84. Most of these respondents suggested a damage-based contingency fee practitioner is likely to seek an early settlement to avoid incurring costs and/or avoid litigation risks. He may push the client to accept a lower amount than that which could be obtained at tribunal. It is clearly in the client's best interests to obtain the maximum possible compensation, and thus the damage-based contingency fee gives rise to a conflict. As IV292 put it:

*When you are deciding whether to carry on or not, the client may well want to carry on for an extra £100 even though it will take an extra £1,000 of work. The solicitor is obviously not going to want to do this.*

85. IV257 noted that the client may be denied the opportunity to continue with the case where a principle is at stake. IV244 was particularly strong in her dislike of the conflict that damage-based contingency fees presented; she considered the arrangements "amoral". She gave an example of a recent case where a well-paid employee was offered a £500,000 settlement. This figure was way under what the claim was actually worth. IV244 pointed out that a damage-based contingency fee practitioner may have been tempted to simply take 40% of the offer: £200,000. However, as she was employing an hourly rate she continued and gained a more appropriate amount for her client.
86. The remaining interviewees simply expressed dislike at having a vested interest in their client's case.

### **Reputation/Image**

87. The number of interviewees mentioning this was very small. Nevertheless, it was notable that claims consultants seemed more sensitive to this as a concern than solicitors. Similarly firms with mixed respondent/claimant practices were apparently most concerned with reputation, suggesting that this group is particularly keen to protect its reputation with its respondent client base.

88. One concern was that damage-based contingency fees were associated with the practice of taking on low merit cases with the aim of trying to force settlement, based on knowledge that it is more cost-effective for the employer to pay out than go to tribunal. IV159 commented that the “general view” amongst respondents is that damage-based contingency fees encourage claims, including these nuisance claims. These practitioners did not want to project such an image to their respondent clients.
89. There were other reputational concerns. IV194 was concerned about “the appearance of inequity” in taking too much of the compensation. IV69 commented that damage-based contingency fees are generally not perceived well by the market, because traditionally they were offered by non-solicitors who would take on huge amounts of cases and not do much work on them in order to make maximum profit.

### **LEI**

90. About a fifth of all interviewees had something to say about LEI. Around a third of these suggested that it is increasing in prevalence and several mentioned that claimants are often unaware that they are covered by it under, for example, house, car or credit card insurance policies. Four respondents explicitly suggested that LEI is preferable to contingency arrangements. However, four other interviewees pointed to problems. IV273 commented that LEI does not cover internal proceedings such as disciplinary or grievance proceedings. IV281 suggested that insurers often do not cover the firm’s full hourly rate and so consequently they have to agree a “top up” with the client. In a similar vein, IV31 suggested that “insurance companies want to pay out the minimum possible”. He thought that there is a perception amongst clients that LEI is unsatisfactory because the bare minimum is offered and clients want a better service. IV55 said that LEI does not kick in until the client is made to go to a tribunal and consequently it “forces contentious tribunal proceedings”.

### **Does firm size impact on reasons for not doing DBCFs?**

91. Although, as we can see from the quantitative data, DBCFs were more common in smaller firms, where such firms did not provide damage-based contingency fees they were more likely than bigger firms to mention cash flow, conflict of interest, insufficiency of profit, client relationship issues, and reputation/image as reasons for not doing damage-based contingency fees.

## Summary

92. 127 respondents (66%) said they did not use damage-based contingency fees; the remainder did use damage-based contingency fees. Although it is technically possible to devise a damage-based contingency fee for respondents, those we spoke to only used them with claimants. Whilst firms that are smaller and concentrate on claimant work appear more likely to do damage-based contingency fee work, it appears to be firms with small rather than solo specialists or larger teams which are most likely to use damage-based contingency fees.
93. Damage-based contingency fees are not generally a new phenomenon. One respondent indicated that his firm had been using them for 20 years and over half of those who responded had been using them for over five years.
94. The predominant reason for not conducting damage-based contingency fee business appears to be the lack of any need to do so on a commercial basis. Whilst ethical, client relationship and other issues feature highly in debate; the main reasons given by our respondents were to do with the nature of the client base, the normal approach to funding respondent work and concerns about profitability and riskiness of damage-based contingency fee cases. However, there was also a strong underlying sense that lawyers ought, in a normative sense, to be paid for the time they put into a case.
95. It is clear from this analysis that opportunity cost is likely to be a major driver behind a firm's decision to take on DBCFs. Where firms have a steady supply of privately paying or other funded work, there is less need for them to look to DBCFs. This partly explains why DBCFs were more common in smaller firms. Interestingly, where such firms did not provide damage-based contingency fees they were more likely than bigger firms to mention cash flow, conflict of interest, insufficiency of profit, client relationship issues, and reputation/image as reasons for not doing damage-based contingency fees. This may suggest that damage-based contingency fees are more common in smaller firms where economic pressures may render ethical dilemmas more acute.

## 6. The cost to the client in using DBCFs

96. This chapter looks at how DBCF fees are calculated, in particular focusing on the level (percentage) fee charged and comparing that with hourly rates. We are able to consider what factors cause variation in the rates and whether the levels charged appear to be disproportionate to the work done on cases. This leads into a discussion of the apparent profitability of DBCF work relative to hourly fee work.
97. The latter parts of the chapter concentrate on the apparent simplicity of DBCFs and looks, in particular, in more detail at the potential for DBCF charges to exceed what the consumer might otherwise assume from a ‘no win no fee’ agreement.

### How are contingency fees calculated?

98. 57 (89%) of those who indicated their firm did contingency fee work also indicated that their normal damage-based contingency fee was calculated and charged as a percentage of compensation. 4 (6%) indicated this was not the case. Three did not answer the question.
99. Three of the four interviewees who did not calculate their damage-based contingency fee as a percentage of compensation based their fee on their hourly rate; the client pays the hourly rate where the case is successful and pays nothing where it is lost. IV99 thought it advantageous to base contingency fees on the hourly rate because it meant that clients “can keep tabs on how much time the lawyer spends on the case”. Two of the practitioners who based their contingency fee on an hourly rate stated that their fee was capped in relation to compensation awarded/agreed. IV99 indicated a cap of 100% and admitted that it was possible for all compensation to be lost in fees.<sup>43</sup>
100. One interviewee indicated that for very complex cases he charges either a percentage or £500, whichever is the greater, with the £500 being payable even if the case is lost.

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<sup>43</sup> He suggested that this is very unlikely to occur and, further, his firm would advise the client against bringing the claim where the fee would exceed the compensation.

### **What level of fee is charged?**

101. Respondents were asked what percentage of compensation normally constituted their fee. 42 (74% of those providing a valid response) indicated they did not have a set rate but charged within a band. Many however had a normal rate, which they only varied in more or less exceptional circumstances. The average (mean) fee was 31% with 33% being the most common (modal) fee. 69% of respondents indicated fees in the 30-40% bracket.<sup>44</sup>
102. There were not generally significant differences in the rates charged according to firm size, client mix or proportion of a firm's work that was done on a DBCF.
103. Variable rates could drop as low as 5-10% but most respondents indicated a lower limit of around 25 or 30%.<sup>45</sup> 34% (16) had an upper band of 30% or less; 21% (10) had an upper limit of 33-35%; and 41% (21) had an upper limit of between of 40 and 50%.

### **Where the percentage fee varies, what factors cause it to vary?**

104. Practitioners indicating they vary their percentage fee cited multiple factors as influencing fee variation. The main reasons given were:
- 104.1. case duration (mentioned by nearly three-quarters of the 42 practitioners);
  - 104.2. level of compensation (two-thirds);
  - 104.3. prospects of success (around half);
  - 104.4. case complexity (over a third); and,
  - 104.5. client characteristics (roughly a fifth).

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<sup>44</sup> Another way of indicating the types of fee charged is by looking at the level of fee actually charged on the last case settled data (see para. 121 onwards). The percentages charged on these cases ranged between 10 and 50%. 17 (36%) were 30% or less; 19 (40%) were between 33 and 35%; and 12 (25%) were between 40 and 50%. The mean figure was 32%. In subsequent analysis we rely on the average figure indicated by respondents rather than the figure given for the example case.

<sup>45</sup> 23 out of 38 responses fell into this band.

### **Case duration and the likelihood of settlement**

105. If a case was expected to last longer than some practitioners would increase the percentage fee to reflect the extra work involved in such cases. Often respondents who indicated that case duration affected their percentage fee based their fees on the point of case completion. Some employed two-tier systems, generally one rate for settled cases and another for cases going to tribunal. Others employed three-tier systems, charging the lowest percentage for settlement prior to issuing a claim, a higher percentage for settlement after issuing a claim, and the highest percentage for cases going to tribunal.
106. For three interviewees, the fee increased with the length of the hearing. One of these charged for extra days on an hourly rate basis, the others increased the percentage fee. A further three interviewees reduced the fee if settlement occurred early on.
107. A handful of interviewees rejected the suggestion that case duration would influence the fee. These practitioners tended to focus on the value of the claim.

### **Level of compensation**

108. Where this was mentioned, most respondents indicated that a low value case would attract a higher percentage; if a claim is worth less a higher percentage needs to be taken to recover for hours worked. A problem with this is that claimants on low incomes are likely to receive a lower proportion of their already lower payouts. A small minority of respondents, however, indicated that lower value claims attracted lower percentage fees.
109. A few interviewees discussed their approach where DBCFs risked overcharging clients. CM10 would reduce his percentage where he had done very little work and the compensation was considerable. IV306 only represented high value claimants and indicated that his firm did not charge high percentages on the basis that large fees would not be justified. CM13 indicated that he would charge nothing where the case was “too small for the client to be charged”.

### **Prospects of success**

110. The practitioner approach generally indicated was that if a case is less likely to succeed then the percentage fee would be higher. In such cases the practitioner takes on extra risk in return for a higher possible award.

111. Only one firm approached this in bands: e.g. IV278 works with two set percentages: 30% for “more straightforward” cases and 40% for cases the firm considers less likely to succeed.
112. Prospects of success was mentioned more frequently by respondents as being a reason for not taking a case on a DBCF (see para. 237 onwards), suggesting that a high risk case is more likely to be refused contingency funding in the first place than taken on but for a higher potential fee. This suggestion was explicitly supported by several interviewees.
113. Solicitors were far more likely than claims management consultants to suggest that prospects of success influenced the percentage fee. Very few claims consultants indicated that they would alter their fee based on likelihood of winning, suggesting that whilst CMCs will simply refuse to use contingency funding in claims unlikely to succeed, solicitors may take on such cases but charge a higher percentage to compensate for the additional risk.

### **Case complexity**

114. More complex cases would attract higher percentages. However, no interviewees based their percentage fee on case complexity alone; all mentioned other relevant factors. Three interviewees gave discrimination as an example of a complex type of case, one commenting that such cases involve vast amounts of documentation.

### **Client characteristics**

115. Around a fifth of those who varied their damage-based contingency fees said that the nature of their client may affect the percentage taken. It is possible that this figure may be higher in practice, as interviewees may have been reluctant to admit to varying fees on this basis. Several interviewees were obviously uncomfortable when responding. IV28 laughed and said “not that I’d ever admit to you” when prompted for client characteristics; she hinted that the nature of the client can affect the fee but appeared worried that this could be seen as discrimination.
116. Three practitioners stated that if the client would make a bad witness then the percentage may have to be increased, although they all related this to the claim’s prospects of success. Other answers indicated that percentages may be decreased for repeat clients; clients in a bad financial position; or clients who were “depressed or very stressed” (IV177). The fee might be increased where the client is untrustworthy; is “known to be constantly on the phone” (IV29); has unrealistic expectations; or is “obsessed with a day in court” (IV60).

**Other reasons**

117. Over a quarter of interviewees who indicated that they vary their percentage fee gave an alternative basis for variation. Half of these talked about percentage reductions where there were multiple claimants. In such cases the representative is receiving a percentage from more than one award but up to a point only needs to prepare one case, making it reasonable that he should charge each claimant a lower percentage. The only other reason for fee increase was having to travel long distances. Other reasons for fee decrease included the client agreeing to cover counsels' fees privately; sympathy for the client; the fact that the claimant has already commenced the claim with a different firm or by himself; and the claimant negotiating a lower percentage, which appeared rare.

**Differences in reasons for variation of fee by firm size and type**

118. There were some patterns in the data which appear related to firm size. Smaller firms appeared less likely to mention prospects of success, but case duration appeared more important. This may reflect stronger concerns about cash flow in such organisations.

119. Firms doing a mixture of claimant and respondent work were by far the most concerned with looking at claim value in assessing the percentage fee: almost nine in ten of the practitioners from mixed firms who varied their fees mentioned level of compensation, compared to over two-thirds of respondent firm practitioners and fewer than half of those doing mainly claimant work.

120. No respondent firm practitioners cited client characteristics as relevant to fee assessment. Conversely, two in five mixed firm practitioners and a third of claimant practitioners considered them relevant. This difference could be due to the fact that respondent firms are less likely to make frequent use of damage-based contingency fees and so will be less aware of issues which probably only arise through using the arrangements regularly (such as client characteristics and their impact on contingency cases).

**Are contingency fees exploitative of clients? Notional hourly rates for damage-based contingency fee cases**

121. Several of our respondents suggested that contingency fee charges were likely to be exploitative because it was possible for lawyers to charge significantly more for cases than their effort would dictate.

122. Interview data on general practices is not the ideal means of exploring this issue. Interviewees are unlikely to reveal grossly-exploitative charging. Conversely, interview data on specific cases may reveal some broad patterns in levels of charging which provide useful evidence on this issue.<sup>46</sup> This is the approach we adopted. We asked practitioners for information on the last contingency fee case they completed:

- 122.1. what level of compensation was paid;
- 122.2. what the fee paid out of that compensation was;
- 122.3. how many chargeable hours they spent on the case; and,
- 122.4. what the normal hourly charge out rate would have been for similar cases.

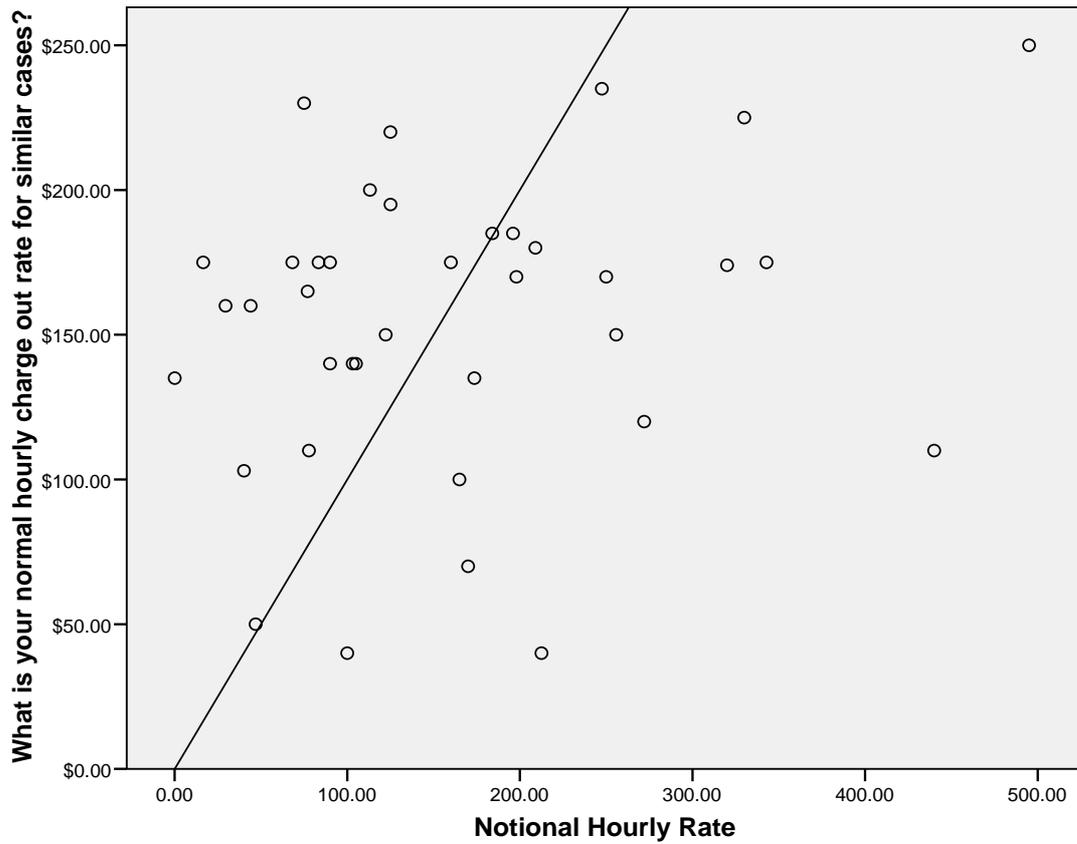
123. Respondents were also asked to indicate their normal hourly rates for similar cases. Because we knew both the compensation, number of chargeable hours worked and the percentage fee charged we could calculate a notional hourly rate for those cases.

124. Figure 1 compares the notional hourly rate with the hourly rate that the practitioner indicated they would charge for an equivalent case by use of a scatterplot graph. The scatterplot reveals considerable variation. All those circles to the right and below the diagonal line indicate cases where the notional hourly rate on the DBCF was higher than the practitioner's equivalent hourly rate. This happened on 17 occasions. Notional (DBCF) hourly rates were lower than equivalent hourly rates on 21 occasions.

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<sup>46</sup> Kritzer used this approach to reveal significantly higher charges on contingency fees than on equivalent hourly rate cases in the United States. See Kritzer HM (2004) *Risks, Reputations and Rewards: Contingency Fee Legal Practice in the United States* (Stanford: Stanford University Press).

Figure 1: Notional and Equivalent Hourly Rates Compared



125. Table 12 provides summary statistics for the two hourly rates.

Table 12: Hourly Rates and Contingency Fees Compared (Notional Hourly Rates)

|         | Contingency Fee<br>(Notional Hourly Rates) | Hourly rates on Equivalent<br>Cases |
|---------|--|-------------------------------------|
| Minimum | £0   | £40                                 |
| Maximum | £495                                       | £250                                |
| Mean    | £162                                       | £155                                |
| Median  | £125                                       | £168                                |
| N       | 38   | 38                                  |

126. The difference in the means of the notional and equivalent hourly rates is very modest and not statistically significant.<sup>47</sup>
127. Of course these figures need to be treated with caution. DBCF Practitioners may have been tempted to underplay the level of fee in contingency cases or, in spite of the exhortation to focus on the most recent case settled, pick a case that was unprofitable. Data was available from 38 practitioners only, further emphasising the need to treat the results with some caution. Nevertheless it is notable that there is considerable variation in hourly rates for DBCF cases (which one would predict whether or not DBCFs were more profitable or not) showing, at the very least, that respondents were not always picking cases that would show DBCFs were less profitable. There are some reasons for placing more confidence in the results. A similar exercise, conducted in the United States by Kritzer, showed up significant increases in notional hourly rates on contingency fees suggesting that practitioners will reveal higher charging where it occurs.<sup>48</sup> Furthermore, published data on costs in Employment Tribunal cases suggests that no win no fee agreement cases cost applicants similar or less than those paying win or lose.<sup>49</sup> It also needs to be emphasised that the hourly rates do not take into account the level of cases being lost under DBCFs. As we see, practitioners on DBCFs would be likely to lose between one in four or one in five cases (para. 228 onwards). This would be likely to mean that DBCFs were significantly less profitable than hourly fees.
128. We collected similar data for those who did not use DBCFs relating to the last contentious case they settled (or lost at tribunal). We asked how many hours they worked on the case, their usual hourly rate for such cases and the compensation paid. Of course this did not include a percentage contingency fee, but we were able to calculate a notional contingency fee (based on a third of the compensation paid). The notional of this figure should be doubly emphasised as many of these firms would be acting for respondents on these cases (where a contingency fee would be difficult or inappropriate). Nevertheless, an

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<sup>47</sup> A paired sample t-test was conducted ( $p = .708$ ). Because a Q-Q plot suggested the distributions of these variables may not be normal a Sign test was also conducted which also did not reveal significant differences ( $p = .626$ )

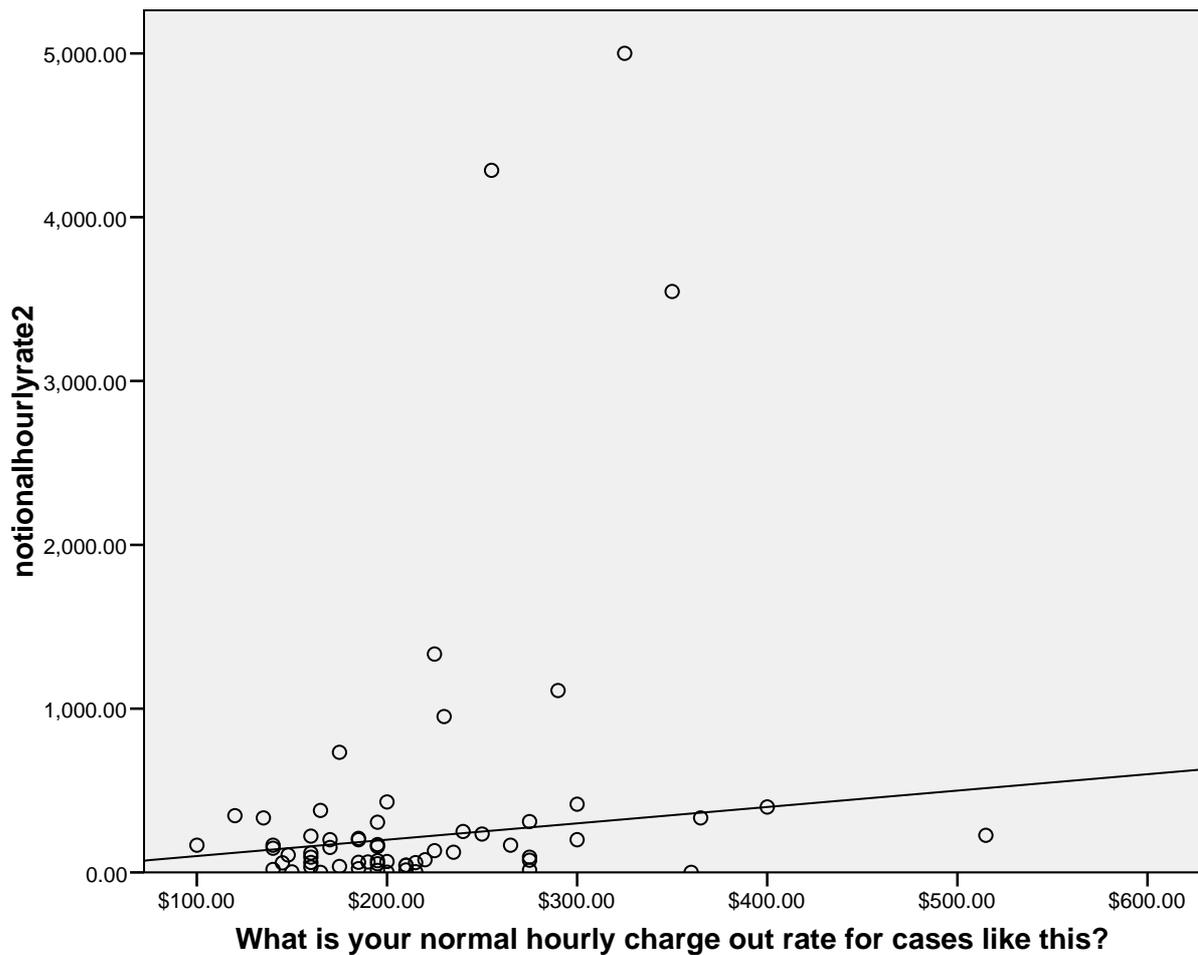
<sup>48</sup> Kritzer cited note 46.

<sup>49</sup> Hayward et al Table 4.23 cited note 30. Further analysis would need to be conducted to establish the robustness of these findings.

analysis of these figures may provide some interesting insights into the different markets within which DBCF and non-DBCF practitioners find themselves operating. We thus calculate a notional DBCF (compensation paid divided by three) and a notional hourly bill (hours worked multiplied by normal hourly rate) and compared the two.

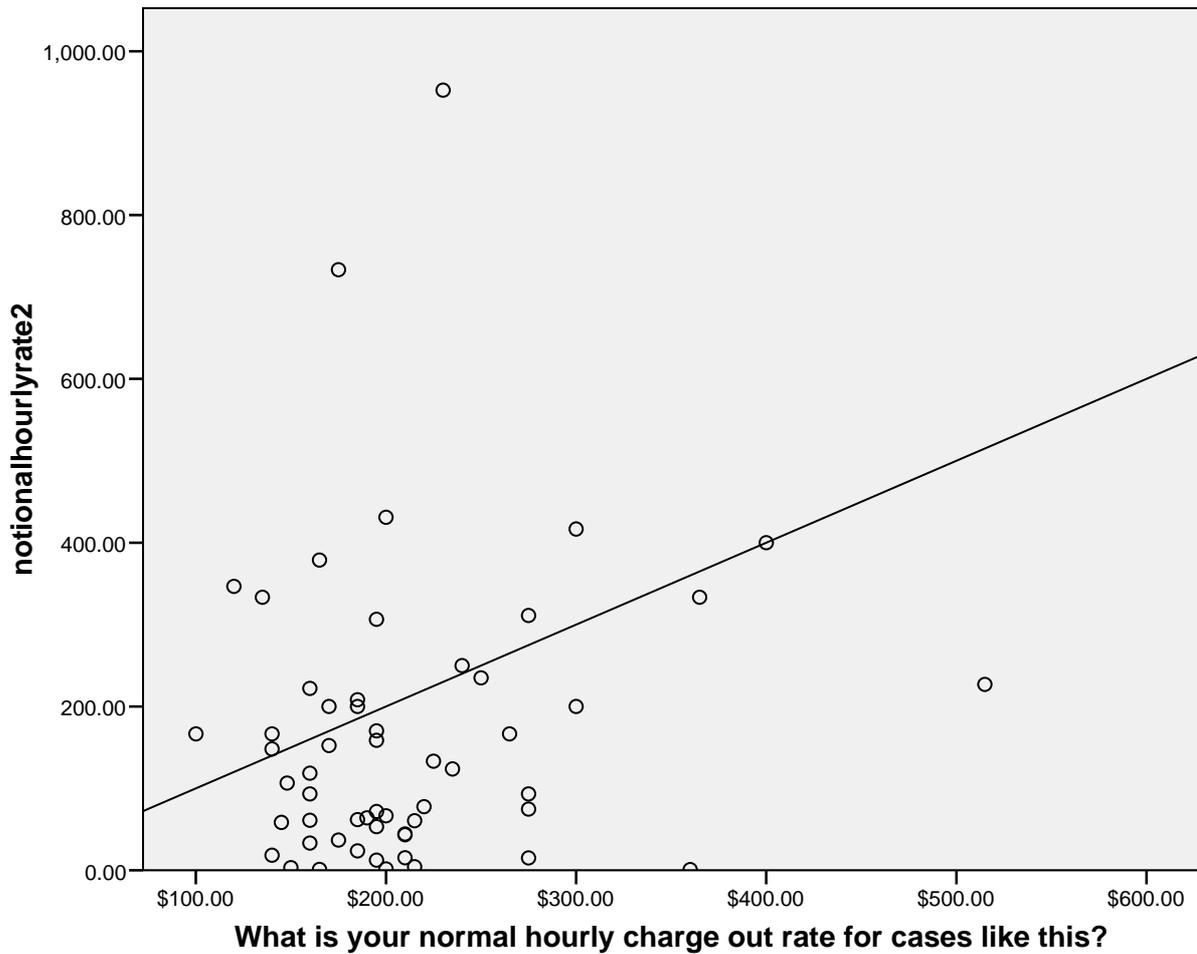
129. We conduct a similar scatterplot to Figure 1 in Figure 2.

**Figure 2: Notional DBCF and Hourly Rates for Non-DBCF cases**



130. For these cases, the potential for outliers (cases that would have yielded very large gains if taken on a DBCF) looks greater. If we exclude all cases where a DBCF would have given rise to an hourly rate of greater than £1,000, the scatterplot looks like this.

Figure 3: Notional DBCF and Hourly Rates for Non-DBCF cases (without outliers)



131. A notional DBCF charge would have yielded lower profit costs in 38 cases and higher profit costs in 22 cases. This may help explain why such firms regarded running cases on a DBCF basis as less profitable than running them on hourly rates. The variation in DBCFs when compared with the equivalent hourly rate fees would explain why they are perceived as more risky (and these figures take no account of the proportion of cases that would be lost under a DBCF yielding no profit costs).<sup>50</sup> However, the mean profit costs on DBCF cases

<sup>50</sup> We could not calculate a notional DBCF on a case that yielded no compensation. In such cases the interviewee indicating the zero payment was acting for a respondent and thus indicating a 'win' for themselves. It was clear from

were dramatically higher than resulted from charging on an hourly rate (£372 per hour compared to £218 per hour) but the differences were not statistically significant.<sup>51</sup> The differences appeared to be largely due to the occasionally very large profit costs that would have been secured if DBCFs had been run on the very large compensation payment cases. Again, it should be emphasised that these figures do not take account of the risk of losing on such cases. Further, as we note elsewhere, such practitioners were wary of DBCFs leading to inappropriately large windfall profits in high value cases: these outliers suggest that, on occasion, such profits would be possible. It is also worth noting that, where such firms were acting for claimants, they had not taken the opportunity to claim windfall profits by acting on a DBCF.<sup>52</sup>

132. At the very least then, this evidence does not support the view that DBCFs are generally more expensive than hourly rate cases, or that across the range of cases, the charges generally exceed the effort put in. Indeed this evidence suggests that comparatively speaking DBCFs are less profitable than hourly fee cases. Interestingly, the evidence points in a slightly different direction for the cases that are not brought on a DBCF. Perhaps because the cases tended to be higher value, the *potential* profit from such cases being run on a DBCF was very variable but potentially higher (although such calculations do not allow for the risk of losing a case).

133. In addition to this quantitative estimate of hourly fees, practitioners commented more directly on profitability.

### **Practitioner opinions on DBCF costs and profitability**

134. Practitioner opinion on this issue was conflicting.

134.1. Over a quarter of participants suggested that damage-based contingency fees are more expensive for clients than paying by the hour. Conversely, a similar

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our data that those acting for respondents were more likely to indicate respondent wins than were those representing claimants, suggesting biased recall by interviewees of their last case.

<sup>51</sup> Paired T-test  $p = .653$  and Sign Test,  $p = .134$ .

<sup>52</sup> In the 20 cases where the interviewee had been acting for a claimant, mean hourly rates under a DBCF would have been £700 per hour compared with the average £196 per hour likely to be charged on such cases.

proportion suggested that the arrangements are financially advantageous to clients (though only four of these suggested that DBCFs actually work out cheaper; the majority focused on other favourable costs implications, namely the lack of upfront payment and the assurance that fees will not exceed compensation).

134.2. Around a quarter of practitioners discussed profitability as a benefit to practitioners in using DBCFs. On the other hand, around a third suggested the arrangements as financially disadvantageous to practitioners.

134.3. We asked contingency practitioners whether they preferred to use hourly rates or contingency fees (discussed further in Chapter 7). Of those indicating a preference for hourly rates, over a third mentioned profitability as an explanation for their preference. Only one participant preferred damage-based contingency fees for the same reason.

135. Practitioners using damage-based contingency fees were much more likely to highlight financial *disadvantages to practitioners* and financial *advantages to clients* than those not using the arrangements.

### **Opinion suggesting that DBCFs are unprofitable**

136. Some practitioners were clearly speaking from experience in labelling DBCFs as unprofitable. For example, two interviewees stated that their firms do not meet targets when contingency work is taken on and another suggested that the best a practitioner ever does using a damage-based contingency fee is to break even with the hourly rate. Further, although over half of the DBCF practitioners who gave profitability as a reason for their hourly rate preference recognised a *possibility* of profiting using damage-based contingency fees, responses tended to suggest that profit is rare or much less likely.

137. Sometimes the lack of profitability was related to the general low value of employment claims, with some practitioners suggesting that profit costs of £2,000 on cases worth £5/6,000 would not be sufficient to make the cases worthwhile. We discuss hard data on this further below (see para. 245 onwards).

138. A few of the practitioners discussing the low value of employment claims suggested it was low value claimants who were most likely to request damage-based contingency fees. As CM17 put it:

*The people coming to you and asking for contingency fees will be low paid, desperate people who will not get much compensation as they are not paid very much. If the claim is only worth £5-6,000 and you are charging a relatively low percentage then what's the point of taking the case?*

139. Profitability may also be vulnerable to changes in the underlying cost-base of employment work. A few participants commented that compensation levels often decrease in employment claims because the claimant mitigates his loss and gains new employment. A couple of respondents observed that costs can be incurred very early on in the claim process. One interviewee commented that tribunal directives mean that practitioners must do a lot more earlier on than was previously the case. Costs are increased meaning that there is “less chance to settle at a decent rate” (IV177). CM20 noted that:

*Employment law is becoming more complex. The complexity of employment cases calls into question the value to representatives of contingency fee charging because of the amount of work involved in relation to the compensation recoverable.*

140. Thus the more complex employment law becomes, the less profitable damage-based contingency fees are likely to be.

141. One interviewee, a respondent practitioner, suggested that damage-based contingency fees are only profitable for firms doing a high volume of damage-based contingency fee work. This may be a comment on multi-party type cases, such as equal pay, where there may be significant economies of scale to claimant solicitors bringing large numbers of similar cases en masse. It seems less likely that simply doing large amounts of claimant work would make DBCFs more profitable: although it would smooth out the risks of losing on some cases. In our data, firms using damage-based contingency fees in over 50% of their cases were the most likely to list profitability as a disadvantage and the least likely to list it as an advantage, perhaps suggesting that extensive use of damage-based contingency fees in fact leads to decreased profits.

### **Opinion suggesting that DBCFs are profitable**

142. Over half of the respondents who suggested profitability as an advantage to practitioners in using DBCFs specifically stated that the arrangements allow practitioners to obtain a better return than they would by charging an hourly rate. Interestingly, it was practitioners not using damage-based contingency fees, or using them in less than 25% of cases, who were the most likely to suggest this. A dozen interviewees went further and suggested that DBCFs *always* lead to increased profit, though the vast majority of these did not in fact use the arrangements themselves. Most of the interviewees who suggested that DBCFs were

financially disadvantageous to clients considered that clients *might* end up paying more than hourly fees, though again around a dozen participants suggested that clients *would be likely* to end up paying more. Some may have confused damage-based contingency fees and CFAs (for example, IV26 commented that damage-based contingency fees can be used to legitimately double a lawyer's fees). Another interviewee commented that often lawyers get more out of contingency cases than clients do. Such an assumption is, however, speculative: no representative in our sample said they charged a damage-based contingency fee of over 50%.

143. A sixth of the interviewees who mentioned profitability as a pro, however, noted that an increased return rarely happens in practice. All used damage-based contingency fees. Contingency practitioners were much more likely to indicate that profit was not common (only four interviewees discussed occasions on which they made good returns) and when it did occur it merely served to balance out losses. IV109, who did not offer damage-based contingency fees, pointed to a swings and roundabouts logic:

*Lawyers must balance against the downside of no fee if no win. They need to charge more than the hourly rate on claims won to make up for claims lost; there is a premium on claims won.*

144. This sentiment was echoed by several of the contingency practitioners elsewhere in the interview. For example, CM13 was once paid £5,000 for 2 hours work and 3 letters. He stated that such windfalls enabled him to take on smaller cases; in his words “the big fish pay for the small fish”. Some interviewees, however, criticised the impact this has on the individual client:

*There is the possibility that settlement will be very early and the client will pay costs disproportionate to the work done. Settlement may occur after one letter to the company and then the client is left paying £10,000 for a letter. (IV60)*

145. IV202 suggested that it was only in around 10% of cases that there was a large settlement for not much work. Nonetheless, IV152 contended that there was the potential for abuse in overcharging clients and that this could happen with unethical practitioners.

146. Some participants made the important point that although clients may end up paying more, at least they are able to claim in the first place:

*If you assume that if he [the client] couldn't use a contingency fee he could not bring a case, then there is no con. The slight negative point is that the client may pay more than he would have on an hourly rate if there is a quick settlement. However, he would have got nothing without the contingency fee and so this is not much of a con. (IV199)*

147. Three interviewees observed that offering damage-based contingency fees allows practitioners to take on more work, which leads to increased profits. As IV66 put it:

*Firms are more likely to get clients and cases to take, which means that profits are increased. For every 10 cases that come through the door 9 will get taken on. This would not be the same if an hourly rate was charged.*

### **Loss of Compensation**

148. Opinion that clients are financially disadvantaged through using DBCFs may be fuelled by an aversion to a funding system whereby the lawyer takes his fee from the compensation. Indeed, over a quarter of participants commented that the client was disadvantaged through loss of damages. Around two in five of these simply suggested the mere loss of compensation as a drawback, for example IV13 who considered it “a nasty sting in the tail”. Around one in ten suggested that clients were not happy when they have to give away some of their winnings.

149. Throughout the answers there seemed to be a general feeling that taking a proportion of someone’s compensation was in some way unfair. This was in spite of the fact that charging by the hour would have a similar net effect on the claimant’s finances. Only three interviewees acknowledged this, including IV219:

*The fee is taken from the client’s compensation but you could say that this is how it works indirectly with private fees.*

150. Indeed, economically the client may be worse off as they are not protected from the risk of losing. It would be interesting to establish whether deferring payment has any genuine effect on how clients perceive their lawyer’s fees: but there is experimental evidence that clients prefer a DBCF arrangement over an hourly-fee approach.<sup>53</sup>

151. Assuming for the sake of argument that hourly rate and DBCF charges are ultimately similar, there are some situations where a client might be better off not instructing on either an hourly basis or a DBCF basis. Interviewees occasionally pointed to these alternatives: self-representation may be an option for some claimants as may be LEI or Trade Union funding.

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<sup>53</sup> Zamir, Eyal and Ilana Ritov, *Neither saints nor devils: a behavioural analysis of attorneys contingent fees* <[http://works.bepress.com/cgi/viewcontent.cgi?article=1000&context=eyal\\_zamir](http://works.bepress.com/cgi/viewcontent.cgi?article=1000&context=eyal_zamir)>; K. Underwood, *Contingency fees in industrial tribunals* (1996) 140(39) S.J. 994, p.994.

**Are DBCFs as simple as they appear? Deductions and how they are charged**

152. The evidence above is not consistent with the view that percentage fees are generally charged on an excessive basis. Whilst we would not suggest that this is conclusive, and we recommend further work is done in relation to, for example, the SETA datasets collected for BERR, we find no evidence of overcharging based on the level of percentage set.

153. There are, nevertheless, other areas of consumer protection on which we think the evidence is less comforting. In particular, we have concerns around the claim that DBCFs are simple and easily understood. A client knows that they will be charged a fixed percentage of what they win and nothing if they lose. This is the essential model, as portrayed by proponents of DBCFs, but is it an accurate model? We turn to these issues next.

**Calculating the percentage fee: a percentage of what?**

154. Our first issue is the sum against which the percentage is calculated. Deductions can be made from claims awarded or received. In particular, damages received may be reduced because of jobseekers allowance and income support payments (where cases are dealt with by the Tribunal).<sup>54</sup> Of particular importance in such cases is the extent to which lawyers calculate their fee as a percentage of compensation agreed or awarded (the pre-deduction figure) or as a percentage of the compensation actually paid to the client (the lower, post-deduction figure). How do DBCF lawyers manage this issue?

**Table 13: Is your normal damage-based contingency fee calculated as a percentage of compensation?**

|                  | N  | %  |
|------------------|----|----|
| Damages awarded  | 23 | 40 |
| Damages received | 29 | 51 |
| Not applicable   | 5  | 9  |
|                  | 57 |    |

<sup>54</sup> Tribunals have a range of other powers to make deductions from compensation payments and it is possible that deductions might be negotiated for other reasons, e.g. as a pragmatic response to enforcement problems.

155. Practice appears to be split roughly down the middle. It is worth considering practitioner rationales for their position before commenting further.

**If practitioner takes a percentage of the compensation before deductions, why is this the case?**

156. Roughly two-thirds of the interviewees who indicated that they based their percentage fee on the compensation awarded talked in terms of recoupment. Almost a third of these suggested that they took their fee from the compensation awarded because doing so secures a greater return for the firm. CM20 commented that:

*If the award is only nominal, recoupment applies and the claimant is a low earner, you won't recover enough if you take a percentage of what is received.*

157. Another argued that because the claimant has benefited from the money that is being recouped, it is fair that the lawyer takes a percentage of the full award.

158. Three interviewees commented that it was simply firm policy, with one emphasising the rarity of recoupment. Two interviewees pointed out that because recoupment only applies following a tribunal award, this gives the claimant an incentive to settle.

159. Four participants discussed issues other than recoupment in explaining their compensation awarded policy. Two of these responded in terms of procedure where an employer doesn't pay, indicating that where this happens they still pursue the client for a percentage of the amount awarded.

**VAT**

160. Another potentially important issue is the treatment of VAT. Practitioner responses were similarly split. Respondents were asked, does the percentage fee include VAT or is VAT added on top? Of the 46 responses:

160.1. 25 (54%) said VAT was included in the percentage figure; but,

160.2. 21 (46%) said VAT would be added on top.

161. As an example, on a 33% fee VAT 'on top' adds a further 6% to the costs deducted from a client's damages.

162. The position is in stark contrast to how the same the respondents reported dealing with hourly rates, suggesting that a significant proportion of practitioners see the desirability of

quoting fees inclusive of VAT for damage-based contingency fees.<sup>55</sup> Thus, whilst the adding on of VAT to damage-based contingency fee percentages may be confusing to consumers and run counter to their expectations, practice is better than the position for hourly rates more generally where *not including VAT* in the quoted rate is common practice.

### **Charging for disbursements**

163. Where disbursements were charged, 51 (84% of valid responses) indicated they always or sometimes charged disbursements in addition to the percentage fee. Only 10 (16%) indicated they did not charge for them separately (i.e. they would meet disbursement costs out of the adviser's percentage). Conversely, as with recoupment, our respondents tended to indicate the relative rarity of disbursements in employment tribunal cases.

164. The extra cost most commonly cited as being excluded from the damage-based contingency fee was counsels' fees: around three in five of the contingency practitioners who charged extra for disbursements charged the client for this expense over and above the percentage fee. Barristers are forbidden from taking cases on a DBCF basis (although CFAs are permitted).<sup>56</sup> Around half of the practitioners who charged extra for disbursements did so for medical and/or other expert reports; around two in five for travel expenses; roughly one in six for photocopying; around one in ten for postage and the same proportion for accommodation (which in practice appeared to be hotel costs); and only one practitioner charged extra for filing. There were other less common examples, including charging for the cost of "long" telephone calls separately.

165. These results show that the majority of contingency practitioners charge clients for extra costs in at least some of their contingency cases. Over and above the obvious economic benefit to firms, there may be other reasons for making such additional charges as the case progresses. IV77 suggested that the prospect of paying disbursements can cause the client to commit to the case and consequently it is sometimes worth charging them.

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<sup>55</sup> 47 (98%) reported that they would add VAT onto an hourly rate.

<sup>56</sup> <http://www.barcouncil.org.uk/about/instructingabarrister/fees/>

166. The qualitative data suggests that solicitors were more likely to charge for disbursements than their claims management consultant counterparts. Furthermore, the larger the firm the more likely it was that disbursements would be charged for, perhaps showing firms seeking to bring DBCF cases closer to their higher hourly rate cases in terms of profitability.

167. Practitioners doing mainly claimant work were the least likely to charge extra for disbursements (with practitioners from mixed firms being the most likely) suggesting that claimant firms have more thoroughly adapted their business practices to ensure a system that is simple and transparent for clients.

### **Extra Charges and the Consumer Interest**

168. What the above sections reveal are a range of practices in terms of charging the client a) whether or not they win and b) over and above any agreed percentage fee. There is a significant likelihood these approaches violate a lay understanding of what is meant by a no win no fee agreement. It seems to us there are two possible ways of interpreting this data.

168.1. That such terms are legitimate attempts by private practice to define the terms on which such agreements are economic and properly balance the risks between lawyer and client. It is worth emphasising that practitioners tended to point to the rarity with which damages were deducted and/or disbursements charged. The economic point is not apparently well supported by evidence that it is those firms with higher levels of DBCF that are less likely to charge these extras charges. Similarly, significant proportions of our respondents could afford not to charge VAT or percentages based on pre-deduction awards.

168.2. That these are illegitimate attempts to shift some of the risks of an apparently simple relationship onto unwitting consumers. The rarity of disbursements and deductions might support an argument that these are parts of the risk that practitioners should bear within their more general acceptance of the risk of a case. Similarly, it might be argued that there is consumer detriment in allowing simple arrangements to be more complex than they need to be, particularly where complexity shifts risks onto the unwitting.

169. The fact that practice on some areas is clearly split suggests a lack of professional consensus on the matter.

170. A crucial and unknown factor in both positions is the extent to which consumers understand and have chosen arrangements whereby the lawyer charges extras win or lose. We have no evidence from this project on what clients actually understood under their agreements. This evidence is now being collected in a subsequent study..

## 7. The pros and cons of DBCFs

171. All interviewees were asked generally about what they considered to be the pros and cons of using DBCFs. Practitioners using the arrangements were also asked whether they preferred to charge on a DBCF basis or by the hour. The results indicate general dissatisfaction with DBCFs as funding arrangements. Respondents volunteered a wider range of cons and discussion of the disadvantages was more detailed. Further, the vast majority of contingency practitioners preferred charging by the hour (Table 14).

**Table 14: Would you prefer to use damage-based contingency fees or have clients pay an hourly rate?**

|                              | Frequency |    |
|------------------------------|-----------|----|
| Damage-based contingency fee | 7         | 11 |
| Hourly rate                  | 45        | 74 |
| Mixture of both              | 8         | 13 |
| No preference                | 1         | 2  |
| Total                        | 61        |    |

172. Six of the seven practitioners who preferred to use DBCFs were claims management consultants. Further, the one solicitor worked at a drop-in centre for unemployed workers, which charges a 10% fee for all cases. As a voluntary organisation hourly fees are not charged and so the respondent's preference for damage-based contingency fees existed because it supported the continued existence of the advice organisation. No solicitors offering both types of funding chose contingency over hourly pay. Indeed, of the remaining six claims consultants, four used the arrangements in 100% of their cases with the remaining two using them in "90% plus" and 80% of claims.

### Practitioner problems with DBCFs

#### Risk

173. Roughly half of all respondents suggested risk as a disadvantage of DBCFs and over half of the DBCF practitioners who indicated a preference for hourly rates gave lack of risk as a reason for their preference, perhaps suggesting that risk is the biggest concern of those using the arrangements. Similarly, around a third of all respondents suggested lack of risk as an advantage to clients in using DBCFs.

174. Where a contingency case is lost no fee is gained, and even where a case is won the time spent may eclipse the fee. As IV188 pointed out:

*You don't ever make a loss with an hourly rate as your fees are not dependent on the outcome or the amount involved in the outcome.*

175. Some of the contingency practitioners who expressed a preference for hourly charging gave examples of cases where losses were made. IV03 once spent 7 days in a tribunal and then lost having spent 100 hours on the case. He felt he almost always lost out when using damage-based contingency fees and considered that the idea that you take on risk and get some extra profit does not work out in practice. CM20 commented that with damage-based contingency fees you can spend a month doing a case and then get nothing back. IV98 discussed cases in which his firm did several thousand pounds worth of work for nothing.

176. Often they considered that the problem materialises because of the uncertainty inherent in employment tribunal cases. Several respondents commented on the unpredictability of tribunal decisions. One practitioner suggested that all lawyers have experience of an unprecedented tribunal decision, and another referred to “bizarre results” (IV28). Tribunal decisions were described as “quirky” (CM12) and by a couple of respondents as “a lottery”, for example:

*The risk element is compounded by the fact that tribunals are often a lottery; you can have a case which loses in one tribunal which if heard in another would have won. Different tribunals often have different interpretations of facts. They are more of a lottery than the courts. (IV273)*

*Employment tribunal decisions are often so perverse that it is to the point of being negligent. (CM07)*

177. IV124 disliked using damage-based contingency fees because she does predominantly discrimination cases, which were described as very risky. IV34 considered that because the value of employment tribunal claims are normally low, taking cases on a damage-based contingency fee basis “presents an unacceptable risk for the firm”. One interviewee pointed out that contingency arrangements involve the practitioner taking on the risk which is otherwise borne by the client.

178. A couple of interviewees noted the difficulty of making an assessment of prospects of success and level of likely compensation at the outset. IV228 commented that an initial interview does not give you time to “get to the bottom of all that needs to be understood”. Several practitioners suggested that the claimant’s story could turn out to be inaccurate,

causing the case to fail. CM12 went further and suggested that the dishonesty of some clients increases the risk involved in contingency cases.

### **Profitability**

179. Many practitioners viewed DBCFs as financially disadvantageous. This issue is discussed in depth above in Chapter 6 (concerning the cost to the client in using DBCFs).

### **Cash Flow**

180. Some respondents were concerned about the cash flow issues presented by DBCFs. Roughly one in ten participants discussed cash flow as a disadvantage. Over a third of the contingency practitioners who indicated a preference for hourly rates gave ‘stability of income’ as a reason for their preference. Damage-based contingency fees provide income that is neither stable nor constant:

*With a contingency fee you either make a shed load of money and rip off the client, or you don't make much. (CM04)*

*Sometimes you have to work for a year before you get any money. (IV152)*

181. These concerns do not arise when the practitioner is charging by the hour, taking costs up front and billing on an interim basis. DBCF practitioners often discussed their preference for hourly rates on the basis that they provided regular cash intake; greater ease in meeting targets and budgeting; and the benefit to the firm of having money on account. IV146 commented that damage-based contingency fees necessitated putting in a lot of work at the start of the case, which exacerbates the problem of waiting a long time for payment.

182. Several interviewees suggested that the financial inconsistency inherent in damage-based contingency fee arrangements causes difficulty in planning and running a business. It is more difficult to stick to budgets when you cannot predict how much money will be coming through the business at any one time.

183. A few respondents commented that the cash flow issue presents more of a problem for smaller firms. As IV232 put it:

*Whilst contingency fees may work for bigger firms which can better absorb the cost of lawyers funding cases up front, they are not viable for smaller firms where managing cash flow is more of an issue. ...There is a risk of not getting paid at all for hundreds of hours of work. A small firm simply can't afford this; it could cause bankruptcy.*

184. However, our research found that the smallest firms were the most likely to use damage-based contingency fees and the most likely to use damage-based contingency fees in more than 50% of their cases. Nonetheless, the smaller the firm the more likely it was that participants gave cash flow as a disadvantage. Arguably, it could be that it is *because* these firms have no alternative that they use DBCFs to maintain some level of income and that this means cash flow becomes more of a problem for them; there are fewer hourly paying cases to cushion the blow of lost contingency cases.

### **Reputational impacts**

185. Half of the interviewees who considered reputation a disadvantage commented that contingency practitioners are perceived as “ambulance chasers”. IV20 expressly suggested that contingency practitioners are associated with “the adverts on TV”. Often there was a perceived association between damage-based contingency fees and greedy lawyers. As IV194 put it:

*There is the perception with contingency fees of greedy lawyers taking forty percent of the compensation when they have done little work.*

186. IV244 gave an example of a recent case where she had done 47 hours of work and gained £500,000 in compensation. She noted that using a 40% damage-based contingency fee agreement would have resulted in a £200,000 fee, which would not have been particularly well received by the client. She suggested that such charging cannot impact well on your reputation as a lawyer. IV228 suggested that lawyers who do take a lot of the compensation leave clients dissatisfied, which has a negative “knock-on effect” on the general reputation of lawyers. IV97 noted the existence of “the perception that a lawyer will settle the case just to get money from it”. She suggested that this is often inaccurate, but noted that the existence of this preconception means contingency lawyers may obtain a bad reputation.

187. A few interviewees suggested that using damage-based contingency fees could be bad for respondent business, for example IV194:

*There is a perception amongst company clients that if you do contingency fees you are an ambulance chasing firm, and so using contingency fees is not a wise move for firms wanting to act for companies.*

**Other practitioner problems with DBCFs**

188. The other main disadvantages of DBCFs suggested by practitioners were the creation of a conflict of interests; spurious claims; a negative impact on case management; and the attitude of clients. These issues are discussed in more depth in later Chapters.

**Practitioner advantages in using DBCFs**

189. Despite the extensive range of DBCF problems suggested by participants, advantages were also put forward.

**Generation of business**

190. The most commonly recognised advantage of DBCFs was that a whole new market becomes potentially accessible. Around three fifths of participants suggested that damage-based contingency fees are beneficial to practitioners because they generate business from clients who would not otherwise be able to pay. Two of the seven practitioners who preferred to use damage-based contingency fees did so because of the business that they generate.

191. The above observations suggest that whilst generation of DBCF business is widely recognised as a theoretical advantage in offering the arrangements, it is not in itself enough to ensure that practitioners favour the contingency structure, nor indeed enough to ensure that practitioners opt to use DBCFs in the first place. The disadvantages discussed above (and throughout this report), combined with the fact that most legal practitioners do not need to increase their workloads, mean that business generation is not a particularly strong influence promoting DBCF use.

192. However, the ability of the arrangements to attract a different client base may appeal to claims consultants. CM10 stated that he would not be able to practice without using contingency arrangements because if he charged an hourly rate then clients would probably just go to a solicitor. CM06 considered that:

*If I couldn't offer contingency fees I would struggle to get fee paying work because I'm not legally qualified. Contingency fees create a niche marketplace for non-legally qualified people such as myself.*

193. In a similar vein, a couple of interviewees suggested that damage-based contingency fees could be useful in starting up a practice; they would allow sufficient work to be done whilst a client base was being developed.
194. Practitioners discussing business generation as a pro framed their explanations in two subtly different ways: for some it opened up their services to those who could not afford them to others it rendered the process of bringing employment claims riskless to the claimants (because DBCFs relieved them of the responsibility for their own lawyer's costs and Employment Tribunal rules largely removed the complainants risk of paying their opponents costs).
195. A few practitioners commented that damage-based contingency fees allow them to take on interesting cases which they otherwise could not. Another interviewee commented that offering damage-based contingency fees results in more non-contingency clients because often individuals seeking no win no fee arrangements will have LEI and not realise it.

### **Profitability**

196. Around a third of respondents suggested profit as an advantage of DBCFs. This issue is discussed in depth in Chapter 6 (concerning the cost to the client in using DBCFs).

### **Reputation**

197. Five practitioners considered damage-based contingency fees potentially advantageous in improving a firm's reputation. Three of the interviewees commented that using damage-based contingency fees may allow a practitioner to take on a case capable of raising the firm's profile where it would otherwise have to be turned away. Presumably they have in mind, for example, cases involving novel legal arguments, or cases against well-known employers. Two interviewees suggested that offering damage-based contingency fees presents a favourable image because such lawyers are perceived as less greedy than those charging high hourly fees.

### **Other Advantages of DBCFs for Practitioners**

198. The other main advantages discussed included access to justice (mentioned by around one in eight practitioners) and efficiency (less than one in twenty). These issues are discussed in later chapters. Suggestions for other benefits included their being more straightforward; providing good experience for junior solicitors; that using a damage-based contingency fee leads practitioners to assess prospects of success early on and only take on cases with merit (contrary to the perception of defendants that they lead to more spurious cases); early

assessment of success might also mean that damage-based contingency fees do actually provide a relatively risk-free method of obtaining fees.

199. A few practitioners liked damage-based contingency fees because they allow them to control which claims they would pursue. One interviewee noted that if he didn't "like the look of someone" then he could (and would) refuse contingency funding under the guise of low prospects of success. A further few interviewees commented that damage-based contingency fees allowed for clarity of fee structure that claimants find easy to understand.
200. A few interviewees stated that using a contingency agreement makes it easier to recover fees from claimant clients because in such a situation the practitioner receives the compensation cheque and then pays the claimant what is left after the percentage is taken. Hourly paying clients may simply not pay.
201. CM06 considered it "demoralising" to work on a case you know will fail, even if you are sure to get paid by the hour for it. He implicitly suggests that hourly rate practitioners take on cases with no prospects of success. This is a rare practitioner recognition that conflicts of interest may also arise in hourly rate cases.

### **Practitioners who prefer to do both hourly and damage-based contingency fee cases**

202. Around one in eight of the practitioners who expressed a preference regarding fees indicated that they preferred to employ a mixture of hourly and damage-based contingency fees. These were all solicitors.
203. The majority of these recognised that there are advantages to both methods of payment, and therefore considered that it is preferable to use both, allowing for the potential of greater profit with damage-based contingency fees but with the back-up of hourly rate certainty. They therefore blended profitability and risk. As one interviewee put it:

*If you are hit by two to three bad contingency fee cases, there are still the opportunities provided by hourly rate cases. (IV60)*

204. A quarter of respondents who preferred mixed systems offered damage-based contingency fees in addition to an hourly rate for clients who could not afford to pay themselves or where hourly fees would lead to too great a deduction from compensation. Others favoured a mixture of contingency and hourly fees because it "makes life more

interesting” (IV242) or because the fee structure is clear, but they feared becoming “tied up” in a contingency arrangement and using up a lot of time (IV177).

## 8. Client attitude towards damage-based contingency fees

205. This study does not directly address the attitude of clients to DBCFs or other fee arrangements, although we are now addressing this in a subsequent study. Here we report on practitioner views on how clients perceive and use DBCFs.

206. Roughly one in seven practitioners complained about DBCF clients' attitudes towards their cases. Just over half of these respondents explicitly related the problem to the fact that such clients are not incurring costs; unlike hourly paying clients they do not have to worry about how much time is being spent on the case. As one interviewee put it:

*If a client is investing his own money in a case then he is more likely to act reasonably and cooperatively etc. Clients tend to be less reasonable when using a contingency fee. (IV257)*

207. IV188 suggested that clients are more committed when paying by the hour because they are "sharing the risk". It is debatable whether the risk is shared with hourly rates; the client bears all or most of the risk of losing.

208. Almost half of respondents citing client attitude as a drawback of DBCFs suggested that contingency claimants are less inclined to agree to settlement and more inclined to want to go on to tribunal. Because they are not incurring costs and know that they will only ever lose a percentage of any compensation, the decision to go to tribunal does not carry the same financial implications as for a client paying by the hour. One interviewee suggested that clients often simply won't consider the prospect of settlement; although we should note it was much more common for respondents to point to very few clients not accepting settlement advice. We discuss this problem in looking at clauses imposing termination of the agreement and/or a financial penalty where clients reject reasonable settlement advice (see Chapter 11).

209. Another suggested problem was contingency clients creating more work; as they are not paying by the hour, they are unconcerned with taking up the practitioner's time. CM12 noted:

*Contingency fee clients are often demanding as to what they want. You end up doing more work because they continuously phone you. It results in you putting in more time than you would on a standard case.*

210. A couple of participants noted that when it comes down to it clients are unhappy at losing a percentage of their compensation, despite being perfectly happy to agree to the arrangement initially. This, they said, creates bad feeling between client and practitioner.

211. Two respondents considered that contingency claimants have unrealistic ideas of claim value. One of these noted, “headlines of people getting one million pound settlements” (IV199). The other suggested that the reason contingency claimants push for more is because they know that some compensation will be lost to legal fees. This clouds their judgement as to the amount they expect to receive.
212. Three contingency practitioners based their preference for hourly fees on the consequent improvement in clients’ attitudes towards their cases. IV213 noted that he had experienced problems with clients misinterpreting the contingency arrangement and consequently disputing the fee.
213. A small number of practitioners commented that the client has more confidence in his case as a result of the DBCF, as practitioners would not take on poor cases on this basis.
214. Conversely, a handful of interviewees considered that DBCFs promote improved client attitude. Two favoured the increased financial certainty which DBCFs give to claimants. CM14 commented that clients are more at ease when visiting a practice offering more than one funding option. IV278 thought it beneficial that the practitioner could get on with the case without the client worrying about the fees. IV40 suggested that with contingency arrangements there are no arguments with the client about how long has been spent on the case. Finally, IV60 suggested that in contingency cases the practitioner shares a “common interest” with his client; both parties seek a fair deal with minimal risk. He qualified this by noting that this convergence only occurs if the client understands that the point to the claim is monetary and not one of principle, i.e. he simply wants to gain compensation, not to prove a point.

## 9. DBCFs access to justice and the ‘explosion’ in claims

215. For those without legal expenses insurance, and who are not members of a Trade Union,<sup>57</sup> DBCFs provide an alternative method of funding employment litigation. For those unable to afford to pay privately for legal representation and unable to gain access to free assistance and/or representation, DBCFs present the only practicable alternative to self-representation.<sup>58</sup> Prima facie, then, proponents suggest DBCFs offer an important means of increasing access to justice, whilst opponents suggest they have led to an ‘explosion’ of dubious claims. Both interpretations assume the same underlying phenomenon: that DBCFs have increased the number of employment tribunal claims brought. We look below at any plausible relationships between DBCFs and claim numbers. It should further be noted that a positive or negative interpretation of this increase essentially turns on the quality (in terms of the merits) of the claims brought. If DBCFs increase the number of claims brought, and the proportion of claims with good merits that are brought, then any increase would signal an improvement in access to justice. If DBCFs increased the number cases but also the proportion of dubious or meritless cases that were brought, then a negative interpretation would be more appropriate. This chapter looks at these issues in more depth.

### DBCFs and Trends in Employment Tribunal Cases

216. If the explosion criticism is well-founded, one would expect to see rising numbers of employment claims corresponding with increasing use of DBCFs. Commentators have pointed to a surge of claims in the 1990s.<sup>59</sup> One report suggests that in the late 1980s there were only around 40,000 claims per year;<sup>60</sup> in 2006/2007 there were over 200,000.<sup>61</sup> If such a rise were to be blamed on DBCFs, we would expect them to be highly prevalent. However,

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<sup>57</sup> A current source of controversy for Trade Unions is that some of their members are taking cases on DBCFs even though, for cases with merits, they would be entitled to free assistance from their Union.

<sup>58</sup> The Legal Services Commission funds limited advice and assistance but not generally representation in employment cases. Local authorities may also fund some assistance and/or representation but levels of funding around the country are generally assumed to be patchy.

<sup>59</sup> Hammersley *et al* (2007) cited note 6 page 1; Johnson and Hammersley (2005) cited 5, pp.25, 28

<sup>60</sup> Latreille *et al* (2005) cited note 6, p.308

<sup>61</sup> [http://www.employmenttribunals.gov.uk/publications/documents/annual\\_reports/ETSAS06-07.pdf](http://www.employmenttribunals.gov.uk/publications/documents/annual_reports/ETSAS06-07.pdf)

the best available evidence of their prevalence is that an estimated 11% of Employment Tribunal claims were being handled under DBCFs in 2003.<sup>62</sup> Such a low figure suggests that they cannot be held responsible for such sharp increases in claims, at least up to 2003.

217. Further, it is likely (but unknown) that DBCFs have only become established in the market in any numbers relatively recently. Our survey data suggests that about half of the employment specialists began to use them in the last five years and half over a longer period than that. Beyond this, there is no hard data on the extent to which use of DBCFs may have increased in recent years,<sup>63</sup> but let us assume for the moment that use of DBCFs in employment cases has been increasing. We can examine existing data on advice seeking and claiming in order to evaluate the extent to which trends in advice seeking or claiming have also increased. In this regard, it is interesting to note that recent tribunal statistics (between the periods of 1998/1999 and 2006/2007) (Table 15)

**Table 15: Tribunal Claims 1998-2007<sup>64</sup>**

|                      | 98/99   | 99/00   | 00/01   | 01/02   | 02/03   | 03/04   | 04/05   | 05/06   | 06/07   |
|----------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Individuals Claiming | -       | -       | -       | -       | 98,617  | 115,042 | 86,181  | 115,039 | 132,577 |
| Number of Claims     | 148,771 | 176,749 | 218,101 | 194,120 | 173,322 | 197,365 | 156,081 | 201,514 | 238,546 |

218. The results for total claim numbers are represented graphically in Figure 4.

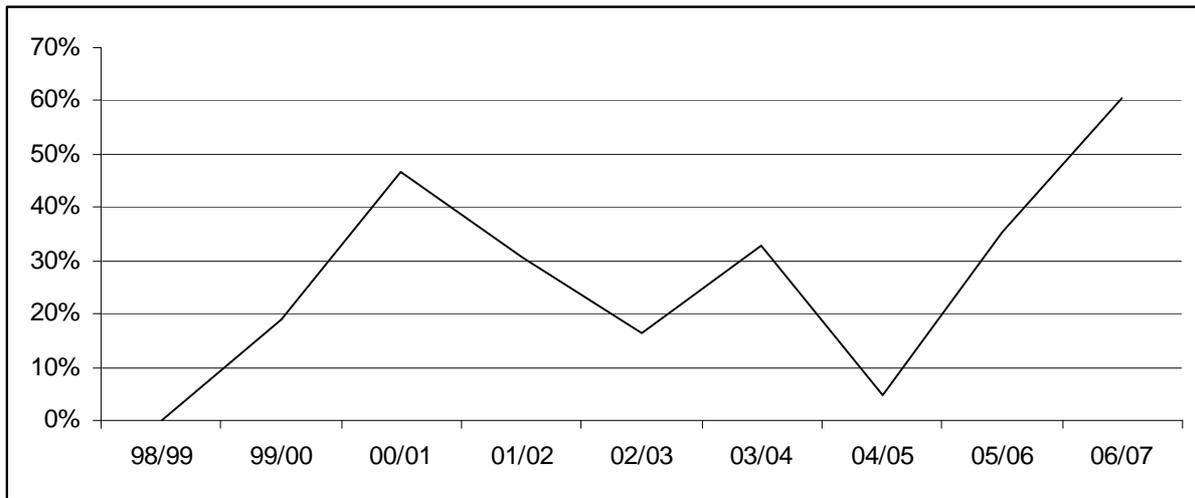
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<sup>62</sup> Hayward et al (2004) cited note 17, p.41.

<sup>63</sup> Forthcoming SETA data from BERR/BMRB should begin to address this issue.

<sup>64</sup> <http://www.employmenttribunals.gov.uk/publications/publications.htm>

Figure 4: Cumulative increase in claim numbers



219. Broadly the trend is up, although there is clearly considerable volatility in the figures.

Indeed, between 2000/01 and 04/05, the trend was broadly downwards, when a substantial proportion of our interviewees appear to have taken up contingency fees for the first time, and a substantial increase since 2004/05. This rise is chiefly attributable to increased equal pay and sex discrimination cases (Table 16):

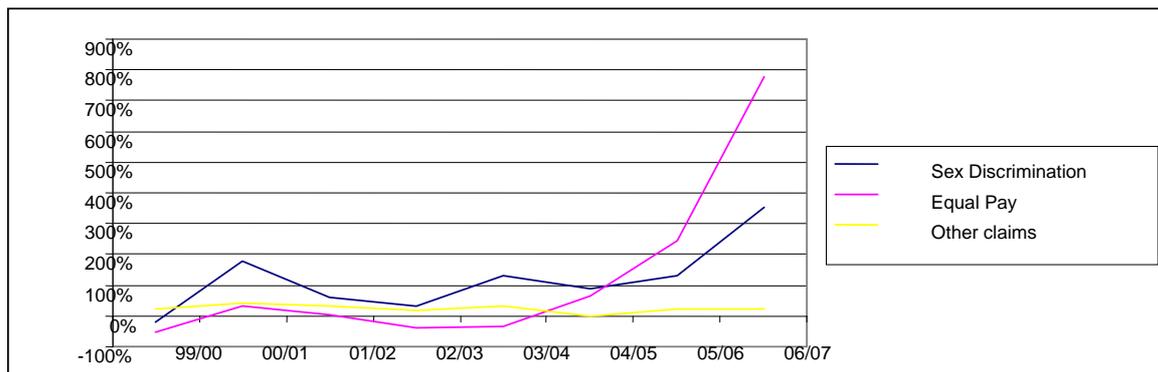
Table 16: Sex discrimination and equal pay claims 1998-2007<sup>65</sup>

|                    | 98/99   | 99/00   | 00/01   | 01/02   | 02/03   | 03/04   | 04/05   | 05/06   | 06/07   |
|--------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Sex Discrimination | 6,203   | 4,926   | 17,200  | 10,092  | 8,128   | 14,284  | 11,726  | 14,250  | 28,153  |
| Equal Pay          | 5,018   | 2,391   | 6,586   | 5,314   | 3,077   | 3,217   | 8,229   | 17,268  | 44,103  |
| Other claims       | 137,550 | 169,432 | 194,315 | 178,714 | 162,117 | 179,864 | 136,126 | 169,996 | 166,290 |

220. The results can be best seen in graphical form.

<sup>65</sup> Ibid

Figure 5: Sex discrimination and equal pay claims 1998-2007



221. Thus if DBCFs had had a *general* impact on claim numbers we would expect to see a significant increase in non-discrimination/equal pay claims over this period and in latter years in particular. Any increases have been significant but relatively modest over the 7 year period (between 0 and 20%) and importantly there is no upward trend. This is not consistent with DBCFs being responsible for the increase in claims or with DBCFs fuelling an upward trend in underlying claims.

222. There is, however, potential for DBCFs to have fuelled the dramatic increase in claims in sex discrimination and equal pay cases. That argument would depend on DBCFs being particularly attractive in those cases, relative to employment tribunals generally. There are two reasons for thinking they might be. Firstly, discrimination cases are not subject to the normal limits on compensation and so may give rise to more profitable DBCFs (although the cases may also be more complex which would inhibit profitability). Secondly, the multi-party nature of some of these claims may make them more profitable for firms.<sup>66</sup> There are, however, a couple of reasons for being somewhat cautious about that claim. One is that large numbers of these cases (anecdotally the majority by some margin) are brought by Trade Unions not by firms operating under NWNF agreements, although it is alleged this has been prompted by the activities of DBCF firms. Secondly, practitioners are generally wary of bringing equal pay claims because of their complexity, although discrimination claims were

<sup>66</sup> Because of economies of scale from having multiple, similar claims against a common employer.

generally seen as more suitable (See Table 19 below at page 81). There are, however, some firms who specialise in equal pay claims and plainly bring such claims in large numbers.<sup>67</sup>

### **Alternative explanations for growth in claims numbers**

223. Whilst it is likely, therefore, that DBCFs have contributed to a significant growth in the number of equal pay and discrimination claims, and plausible that they may have contributed to modest growth in other claims, it is important to emphasise that there is, as yet, no hard evidence of the underlying trends in the use of DBCF funding. It is also important to emphasise that we should not deduce from growth in claims alone that this is due to DBCFs. There are other plausible explanations for the growth in such claims. The large scale problems in relation to public sector pay are a structural problem not caused by DBCFs. Further, commentators have suggested a number of alternative reasons to explain rises in tribunal claims over time. Firstly, there is the obvious point that as new employment legislation is introduced new rights emerge and as a result employees have greater scope to bring tribunal applications. As Hammersley and Johnson have pointed out,<sup>68</sup> the 1990s and early 2000s saw much new employment legislation, including the Employment Rights Act 1996, the Employment Relations Act 1999 and the Employment Act 2002. Further, the introduction of the Human Rights Act 1998 has led to increased awareness of rights.<sup>69</sup> Equal pay disputes have grown against major public sector job evaluation initiatives. Importantly, Burgess et al demonstrated the importance of underlying socio-economic drivers of employment tribunal cases with factors such as the rise in numbers of women in the workforce; increases in the numbers of people employed in small enterprises; a decline in manufacturing and trade union membership accounting for significant levels of growth in employment tribunal applications.<sup>70</sup>

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<sup>67</sup> In particular, Stefan Cross Solicitors handle large numbers. One report suggests upward of 7,000 equal pay cases on no win no fee, though this figure is likely to be out of date: see, for example, *Lawyer of the week: Stefan Cross* Times, April 3, 2007

<sup>68</sup> Hammersley and Johnson (2004) cited note 6, p.2

<sup>69</sup> Hammersley *et al* (2007) cited note 6, p.1

<sup>70</sup> Burgess, Simon, Carol Propper and Deborah Wilson (2001) *Explaining the Growth in the Number of Applications to Industrial Tribunals 1972-1997* (DTI: London)

224. It must also be borne in mind that tribunal statistics only account for claims involving an application to tribunal and do not account for claims which settle before proceedings are issued. However, data from Genn's 1999 'Paths to Justice' survey, combined with LSRC surveys in 2001, 2004 and 2006, all of which reviewed justiciable problems in England and Wales, shows no significant change in reported incidence of employment problems.<sup>71</sup> If DBCFs had substantially increased the public's propensity to claim, we might expect to see an underlying increase in their identification of employment problems and we do not.

225. As already noted, the increase in tribunal applications may be interpreted as giving rise to more, and more dubious claims, or positively as increasing access to justice. Let us turn now to the issue of quality, which may help us resolve the dilemma of whether any increase is positive or negative.

### **Access to Justice? The Quality Arguments and Evidence**

226. Unlike in ordinary civil litigation, in employment cases the winning party does not usually recover its costs from the losing one, and under a DBCF a claimant does not have to pay his own lawyer's fees if the case is lost.<sup>72</sup> Consequently, a contingency claimant has minimal financial risk from losing a case; a situation which is sometimes criticised as encouraging nuisance claims. The idea is that individuals can 'have a go' without the fear of incurring a debt. Employers faced with such a claimant may simply settle for financial reasons rather than defend meritorious cases, which means that potentially unscrupulous representatives could bring unmeritorious claims in the hope of obtaining a 'nuisance settlement'.

227. Whilst the academic evidence supports the proposition that costs shifting acts as a partial brake on unmeritorious claim, it has other drawbacks: in particular leading higher costs and

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<sup>71</sup> H. Genn, *Paths to Justice: What People Do and Think About Going to Law* (Hart Publishing, Oxford 1999) p.24; P. Pleasance, *Causes of Action: Civil Law and Social Justice* (2<sup>nd</sup> Edn, The Stationary Office, Norwich 2006) p.27; P. Pleasance, N. Balmer and T. Tam, *Civil Justice in England and Wales: Report of the 2006 English and Welsh Civil and Social Justice Survey* (LSRC London 2007) <<http://www.lsrc.org.uk/publications/csjs2006.pdf>> accessed 29<sup>th</sup> August 2008, p.11.

<sup>72</sup> See, for example, J. Robins, 'Fighting for equality' (2007) L.F. 50(Aug) 8, in which some solicitors are quoted as supporting a change in the costs regime in employment tribunals. Anecdotally we heard evidence of a stiffening of the approach to costs in some tribunals.

the major disincentives to risk averse defendants.<sup>73</sup> Theoretical economics and empirical evidence also tends to support the view that, because a NWNF practitioner has to invest their own time, and possibly other costs, in a case, they are going to be careful about the cases they take on. Thus DBCFs may improve the quality of cases (quality in the sense of the underlying merits of the case) that are brought, because practitioners carefully select cases with good prospects of success.<sup>74</sup> Alternatively, it is possible that these incentives operate to restrict access to justice: practitioners are overly cautious, cherry-picking only the very best cases, or are confined by the economics of the situation to reject meritorious but low value cases which would not be profitable. The latter has already been identified as a potential problem in relation to employment cases.<sup>75</sup>

### Quality and success rates

228. There is data available on the outcome of DBCF and non-DBCF cases from which it is possible to construct a picture of success rates.<sup>76</sup> SETA data on employment tribunal applications contains data on fee types, advice/representation and outcomes. We have conducted some analysis of the available dataset and these results are set out in Table 17. It should be emphasised that these results are confined to cases where an employment tribunal application was issued. Because it is possible for an applicant in the SETA survey to have had some (albeit insubstantial help) from a range of advisers, results are also confined to those cases where an employment tribunal applicant gained most help from either a solicitor or a claims consultant. The SETA dataset identifies DBCFs but with some error<sup>77</sup> as a result

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<sup>73</sup> Rickman, Neil (1994) The economics of contingency fees in personal injury litigation. 10 *Oxford Review of Economic Policy*. 34 – 50; Hause, John C. (1989) Indemnity, settlement and litigation or I'll be suing you. 18 *Journal of Legal Studies*. 157 – 180; Katz, Avery (1987) Measuring the demand for litigation: Is the English rule really cheaper? 3 *Journal of Law, Economics and Organization*. 143 – 176; Snyder, Edward A. and James W. Hughes (1990) *The English Rule for Allocating Legal Costs: Evidence Confronts Theory* 6 *Journal of Law, Economics and Organization* 345-380 and Snyder Edward A. and James W. Hughes. (1995) *Litigation and settlement under the English and American rules: Theory and Evidence*. 38 *Journal of Law and Economics* 225.

<sup>74</sup> Helland, Eric and Alexander Tabarrok (2003), *Contingency Fees, Settlement Delay and Low-Quality Litigation: Empirical Evidence from Two Datasets*, 19 *Journal of Law, Economics, and Organization* 517 -521.; Clermont Kevin M. & John D. Currihan (1978), *Improving on the Contingency Fee*, 63 *Cornell Law Review* 529; Dana, J. & K. Spier (1993), *Expertise and Contingent Fees: the role of asymmetric information in attorney compensation*, 9 *J Law Econ Org* 349; Kritzer cited note 46.

<sup>75</sup> Hammersley *et al* (2007) cited note 6, p.21 ; Johnson and Hammersley (2005) cited note 5, p.28

<sup>76</sup> We had some data from our survey too but this was not very reliable.

<sup>77</sup> See, Hammersley *et al* (2007) cited note 6, page 11 onwards.

two definitions of DBCF used.<sup>78</sup> Cases where a person has their main support from a lawyer or an employment consultant which may have been conducted under legal expenses; trade union or other funding are labelled ‘Not DBCF’ below. The outcome data is that collected from the SETA survey which has the advantage of distinguishing more accurately between cases withdrawn and cases settled privately than Employment Tribunal statistics.<sup>79</sup> Success for the claimant is defined in the final row of the table as being success at hearing or a settlement.<sup>80</sup>

**Table 17: Success Rates in Employment Tribunals using DBCF**

|                                   | Narrowly Defined DBCF |          | Broadly Defined DBCF |          | Total |
|-----------------------------------|-----------------------|----------|----------------------|----------|-------|
|                                   | DBCF                  | Not DBCF | DBCF                 | Not DBCF |       |
| Applicant unsuccessful at hearing | 11%                   | 8%       | 9%                   | 9%       | 52    |
| Applicant successful at hearing   | 7%                    | 11%      | 9%                   | 11%      | 59    |
| ACAS settled                      | 57%                   | 54%      | 55%                  | 54%      | 320   |
| Privately settled                 | 12%                   | 14%      | 16%                  | 12%      | 81    |
| Withdrawn                         | 12%                   | 12%      | 9%                   | 13%      | 68    |
| Dismissed                         | 2%                    | 1%       | 2%                   | 1%       | 9     |
| Total                             | 112                   | 477      | 243                  | 346      | 589   |
| Success Rate                      | 76%                   | 79%      | 80%                  | 77%      | 78%   |

Source: SETA 2003

229. The differences in distribution for DBCF and non-DBCF cases are neither marked nor statistically significant:<sup>81</sup> for both kinds of case a success rate was between 76% and 80%.

More sophisticated analysis which takes into account the underlying characteristics of these

<sup>78</sup> The broader definition treats all claimants who said they had to pay their adviser “if they won the case” as being under contingency fees. The narrower definition treats only those who said they had to pay “if they won the case” and that they paid only if they won. Because it is possible for someone to pay some costs win or lose under DBCFs, it is possible that either definition is more accurate; hence the need to look at both. See Hammersley et al (2007) page 11 onwards cited at note 6, who discuss this in more detail and tend to concentrate on the broad definition in their analysis.

<sup>79</sup> Hayward et al cited note 30.

<sup>80</sup> It should be recognised that a claimant may not regard the terms of a settlement as a success, but taking this into account would overcomplicate the analysis.

<sup>81</sup> Basic inferential testing suggest they were not significantly different. Chi-square,  $p = .293$  on the narrow definition and  $p = .498$  on the broad definition

cases may reveal deeper patterns,<sup>82</sup> but Table 17 suggests that in terms of overall outcomes impact may be negligible. If outcome is taken as an indicator of quality, contingency fees neither improve nor weaken the quality of cases brought. It may also suggest that practitioners are not unnecessarily risk averse in bringing contingency fee cases (i.e. they do not appear to be generally only cherry-picking ‘easier’ cases to run under DBCFs).

### Interview evidence

230. We collected evidence on these issues in a number of ways. Firstly, we asked practitioners: what proportion of cases do you consider for damage-based contingency fees but decline? (Table 18)

**Table 18: What proportion of cases do you consider for damage-based contingency fees but decline?**

|                 | Frequency | %  |
|-----------------|-----------|----|
| 0-10%           | 13        | 25 |
| 11-40%          | 11        | 21 |
| 50-65%          | 13        | 25 |
| 66-80%          | 8         | 15 |
| 81-99%          | 8         | 15 |
| Valid responses | 53        |    |

231. It is evident from these results that practitioners screen out large proportions of cases in determining the availability of DBCF funding. The mean figure for the proportion of cases considered for DBCFs but then declined was 44% and half of respondents reported turning away 50% or more of potential DBCF cases. The solicitors we surveyed rejected a higher level of cases on average (48%) than claims consultants (37%), but the difference were not significant.<sup>83</sup> Similarly those who used damage-based contingency fees between 50 and 100% of their work were less likely to decline cases (39%) than those who used it for up to 25% of

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<sup>82</sup> Hammersley et al began this task with cluster analysis although more sophisticated multivariate analysis would be appropriate. They have suggested that levels of dismissal are higher for contingency fee cases, but withdrawals are lower and settlements more frequent. Hammersley et al cited note 6

<sup>83</sup> Two tailed T-test, p = .27

their work (48%), but again the differences did not reach significance thresholds.<sup>84</sup> The distributions did not differ significantly by firm size, team size, emphasis of the practice or between those who did more than 50% of their cases on damage-based contingency fee and those who did less than 25% or their cases on a damage-based contingency fee.<sup>85</sup>

232. Even for those practitioners heavily dependent on DBCFs, these results are not consistent with the view that DBCFs generally give rise to a willingness on the part of employment advisers to ‘have a go’ come what may.

### **Factors determining whether a DBCF is offered**

233. We asked practitioners to identify which case types were regarded as more or less suitable for DBCFs and then we asked them about the other factors underlying such decisions.

### **Case type**

234. Respondents offering DBCFs were asked how suitable they felt damage-based contingency fees to be for particular case types. Suitability in this context generally meant (as we shall see) the economic viability of advancing claims by this method. The results are represented graphically in Figure 6 and the data is in Table 19. It should be emphasised that we only generally have responses from just over 50 respondents to each of these questions; they do however indicate some relatively clear patterns of difference between case types. Those cases regarded as most suitable for DBCFs gravitate towards the bottom of the chart.

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<sup>84</sup> Two tailed T-test,  $p = .28$

<sup>85</sup> Anova and t-tests used,  $p > .05$  on all occasions.

Figure 6: How suitable are damage-based contingency fees for particular case types?

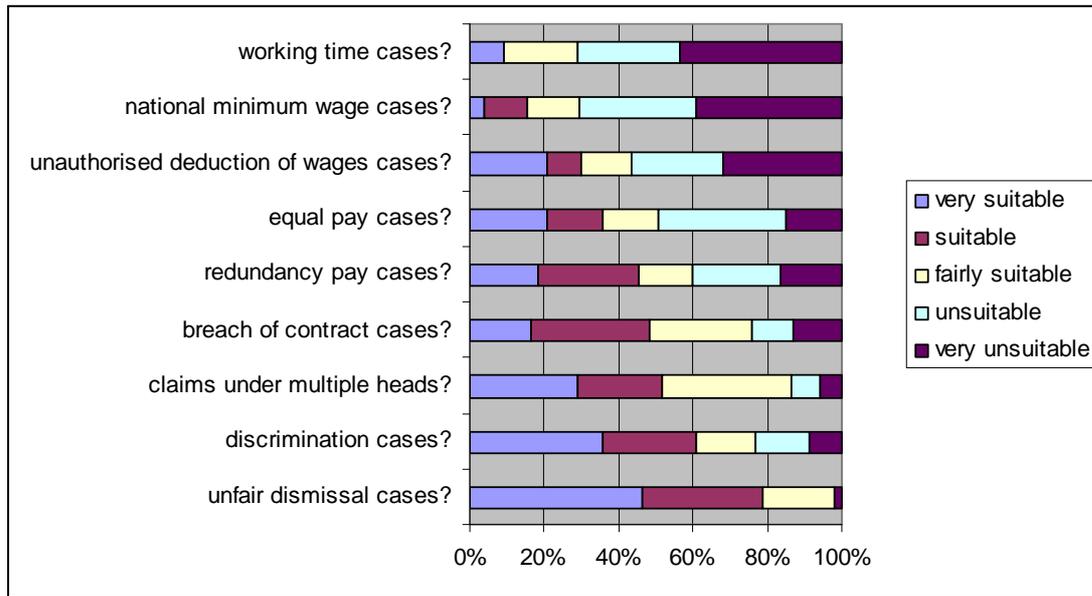


Table 19: How suitable are damage-based contingency fees for particular case types?

| How suitable are damage-based contingency fees for | Very suitable | Suitable | Fairly suitable | Unsuitable | Very unsuitable | N  |
|--|---------------|----------|-----------------|------------|-----------------|----|
| Unfair dismissal cases?                            | 46            | 32       | 20              | 0          | 2               | 56 |
| Discrimination cases?                              | 36            | 25       | 16              | 14         | 9               | 56 |
| Claims under multiple heads?                       | 29            | 23       | 35              | 8          | 6               | 52 |
| Breach of contract cases?                          | 17            | 31       | 28              | 11         | 13              | 54 |
| Redundancy pay cases?                              | 18            | 27       | 15              | 24         | 16              | 55 |
| Equal pay cases?                                   | 21            | 15       | 15              | 34         | 15              | 53 |
| Unauthorised deduction of wages cases?             | 21            | 9        | 13              | 25         | 32              | 53 |
| National minimum wage cases?                       | 4             | 12       | 14              | 31         | 39              | 51 |
| Working time cases?                                | 9             | 0        | 20              | 27         | 44              | 55 |

235. The position of equal pay cases is interesting, with only a minority thinking they were suitable or fairly suitable. It could be that that in such cases it is the existence of multiple claims, as opposed to case type, which makes the case suitable for contingency funding. Indeed, several respondents suggested that group actions are more suitable because of increased profitability. IV228 discussed damage-based contingency fee use in the recent equal pay claims:

*[such claims]...typically have a well-understood background and so all you need to know is whether your client falls within the scope of the background facts. Also, you can have a very large group of claimants with features common to the class, meaning that the risk can be spread.*

236. Beyond asking about particular case-types, we explored practitioner decision-making processes through asking the 64 practitioners who used DBCFs: what makes cases suitable for DBCF funding? And why are cases declined for DBCF funding?

### **Prospects of success**

237. Roughly three-quarters of the practitioners who used DBCFs suggested that prospects of success influence case suitability for damage-based contingency fees. Around four out of five of the DBCF practitioners giving reasons for refusal of contingency funding cited low success prospects as a reason. These figures mean that a claim's chances of success are the main influence on the likelihood that a claimant is offered a DBCF.

238. Clients with meritorious but borderline cases may be unable to access legal representation. This was explicitly recognised by a dozen or so participants, including IV62:

*Clients may find it difficult to find firms who would take on 50/50 cases, or cases with lower prospects of success. Most practitioners would want at least a 60% chance of winning for contingency fee cases. It may be that a case starts off at 50/50 or less, but then gets stronger. You only realise this when you litigate the case. In those cases members of the public with such claims can't find representation.*

239. An interesting possible implication of comments such as these is that if the client was paying an hourly rate then the prospects of success might be less relevant.
240. Another problem with making the decision to offer a DBCF dependent on prospects of success is that they are not easily determined 'up front'. As some interviewees noted in discussion of the risk element in damage-based contingency fees, tribunal decisions are difficult to predict. Assessment of prospects of success is likely to be somewhat arbitrary. Indeed, CM20 thought it inappropriate to base suitability assessment on prospects of success because it cannot be gauged with any accuracy. Practitioners will most likely know a hopeless case when they see one, but most are not as clear cut.
241. Despite this, some participants volunteered prospects of success thresholds, which cases have to meet before they will be considered. During general discussion of factors influencing case suitability for DBCFs, thresholds ranged from 50-80%, with 60% or 70% being most

common. A couple of interviewees were less specific but did suggest that prospects of success should be very high, referring to a “cast iron” (CM04) or “black and white” (CM12) case.

### **Likely Level of Compensation**

242. Around three-quarters of contingency practitioners commented that the value of a claim would influence its suitability for contingency funding. Over two-thirds of the practitioners who indicated reasons for refusal of DBCF funding stated that claim value had an impact. Thus this factor is obviously highly influential, predictable when one remembers that the level of compensation determines the lawyer’s fee.

*[I]f you use a contingency fee, either you will not recover your costs or the proportion of damages you take will be so high that a contingency fee would not be suitable for the claimant. (IV28)*

243. Clearly, lawyers are unlikely to accept cases where they look set to make a loss. As a number of interviewees pointed out, there is something of a double-bind: employees on low salaries who are likely to be most in need for DBCFs are less suitable as damage-based contingency fee clients because the cases are not economic.

*It is not a good system as the poorest people are denied access. Either they do not have enough money to pay the hourly rate or their cases are not worth enough for solicitors to justify taking them on on a contingency fee basis.*

*I’ve turned down clients with good cases but cases which won’t recover enough money. Mostly these people are very poorly paid and have no savings. Their jobs were not well paid and so you won’t recover enough. (IV128)*

244. Occasionally interviewees took this further to suggest that it is only clients who can afford to pay privately who would have cases that merited DBCFs. This seems likely to be overstressing the point: it is conceivable, particularly for those who have just lost their job, that sizeable claims may be made for some clients who do not have sufficient money to pay up front on an hourly basis. There is also experimental evidence that claimants *offered the choice* would prefer DBCFs over hourly rates and would be willing to pay significantly more than under hourly fees because of the assumption of risk by the lawyer.<sup>86</sup>

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<sup>86</sup> Zamir and Ritov cited note 53.

### **Minimum case values**

245. To try and get some data on the size of claims which were brought under damage-based contingency fees, we asked those who had experience of taking contingency claims to indicate the amount the last case they handled on a damage-based contingency fee settled for. Payments ranged between £500 and £95,000. Half the claims were settled for £10,000 or less but the average (mean) settlement was £17,500. The mean figure is somewhat skewed by large claims at the upper end of the distribution; only about 30% of claims were of this order or larger. Nevertheless it is reasonably clear from this evidence that, in so far as these example cases were representative generally of claims brought by DBCF practitioners,<sup>87</sup> DBCF cases were likely to be used in claims of higher value than the population of employment claims generally.
246. The Employment Tribunal Service figures for 2006/07 awards shows that the median amount awarded in Employment Tribunals was £3,800 and the mean amount £7,974 (the latter being much higher because of a limited number of high value awards).<sup>88</sup> The figures above are for tribunal awards, the figures for settlement are even lower. Figures for settlements of cases issued in Employment Tribunals suggest a mean level of settlement of £4,000 and a median settlement of £1,000.<sup>89</sup> That is, settlements (as a group of cases) are likely to produce significantly lower levels of award than cases proceeding to a final hearing.
247. We can compare the distribution of tribunal awards with the distribution of values for the last case settled as given by our respondents (Figure 7).

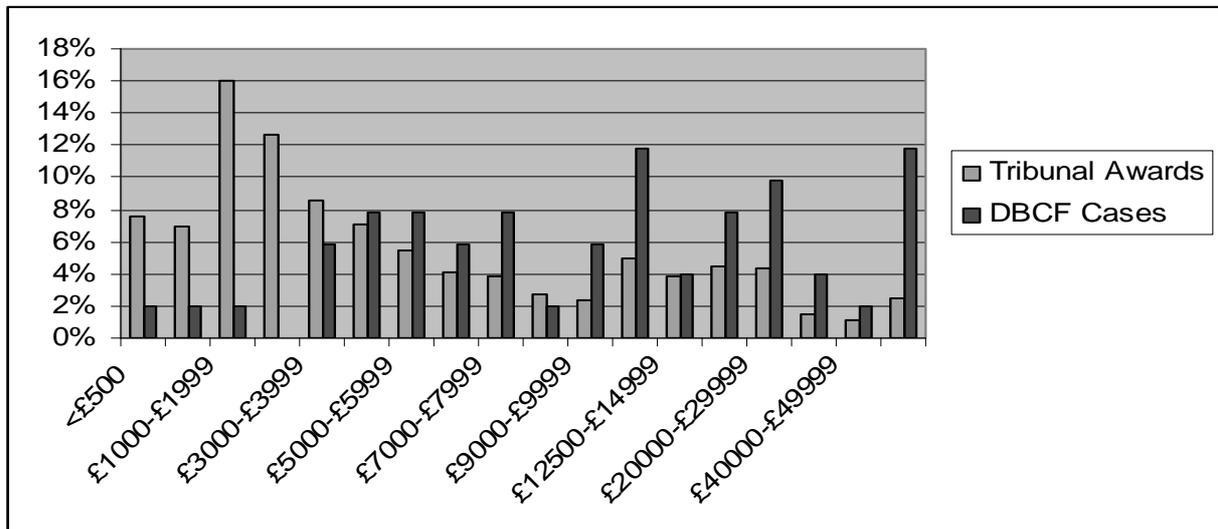
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<sup>87</sup> There is a risk that practitioners would be more likely to recall bigger cases so we may expect the figures to be inflated somewhat.

<sup>88</sup> Employment Tribunal and EAT Statistics (GB) 1 April 2006 to 31 March 2007. There are separate figures for, inter alia, discrimination claims which cover far fewer cases.

<sup>89</sup> Hayward et al (2004) cited note 30, Table 8.12

Figure 7: Distribution of DBCF settlements compared with the distribution of Employment Tribunal Awards



248. Whilst we should bear in mind that the figures for the DBCF cases may be inflated somewhat by practitioner recall biasing towards higher value cases, the profile of DBCF cases is clearly at the higher end of the compensation spectrum.

249. We also asked practitioners whether they had minimum values in mind when they took on cases. 23 respondents (38% of those using damage-based contingency fees) reported having a minimum case value that had to be reached before a case would be taken on (although many indicated that they would look at cases on their merits and that minima were more of an informal guide than a hard and fast rule). Responses ranged between £500 and £30,000. Half the respondents had a minimum level of £5,000 or less. Discrimination claims were frequently mentioned as suitable for damage-based contingency fees given the possibility of unlimited damages.

Table 20: Minimum Claim Value

|                | Frequency | %  |
|----------------|-----------|----|
| £1,000 or less | 3         | 13 |
| £2-3,000       | 5         | 22 |
| £3,500-£5,000  | 7         | 30 |
| £8-10,000      | 4         | 17 |
| £15-30,000     | 4         | 17 |
| Total          | 23        |    |

250. These limits are lower than that found in a previous study – £12,000-£15,000 before a case would be accepted<sup>90</sup> – but nevertheless suggest that large numbers of employment cases would not be perceived as viable propositions to practitioners operating DBCFs. A threshold of £3,000 would exclude an estimated 43% of cases based on the figures for tribunal awards.
251. On the other hand, a few interviewees disagreed that claim value is important in assessing case suitability. CM08 considered that if a claim has high prospects of success then its value is unimportant. CM10 stated that he takes low value cases based on a belief that the claimant is entitled to the small amount, even where this is not remunerative to him. Two interviewees stated that they would only take on lower value claims if they considered that early settlement could be obtained.
252. Our analysis of the qualitative data suggests that solicitors seemed more likely than claims consultants to indicate that claim value affects suitability and were also more likely to suggest a low likely level of compensation as a reason for refusing a damage-based contingency fee. This may be because solicitors' hourly fees are generally higher than those of claims consultants, and/or because (some) claims consultants are more dependent on damage-based contingency fees, making them more likely to need to take on cases of marginal profitability. Similarly, it appeared that the larger the firm the more likely it was that the practitioner would refuse a damage-based contingency fee based on a low claim value.
253. Level of concern with claim value was also affected by frequency of damage-based contingency fee use. Practitioners from firms using damage-based contingency fees less frequently were more likely to indicate that they would decline to use such an arrangement in a low value case. It may be that frequent damage-based contingency fee users take on a variety of claim values and these balance each other out or that they need to take on low value cases to ensure they get sufficient high value cases.

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<sup>90</sup> Hammersley and Johnson (2004) cited note 6, p.13; Johnson and Hammersley (2005) cited note 5, pp.23, 25, 28.

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**Case duration, likelihood of settlement and predicted hearing length**

254. Around a third of the respondents using DBCFs indicated that cases likely to last a long time are less suitable for contingency funding. Around one in six of the practitioners who suggested reasons for refusal of DBCF funding said that they would decline on this basis. Unlike practitioners paid by the hour, those paid on a contingency basis have an interest in spending less time on a case because doing so increases profitability. One interviewee was particularly blunt:

*To make a profit you need to do the least amount of work possible. (IV40)*

255. We discuss concerns that DBCFs lead to reduced quality service below (para. 366 onwards).

256. About a third of the interviewees who considered case duration a factor mentioned the likelihood of settlement and/or prospects of early settlement as increasing suitability.

257. A similar number of interviewees suggested the likely duration of a *hearing* as a factor influencing their decision on contingency funding. Practitioners approached this in different ways. Some practitioners presume a hearing will take place and concentrate on the length of any *potential* tribunal proceedings rather than whether that hearing was in fact likely. In other words, they decided risk on a worst case scenario. Others looked specifically at settlement prospects in deciding whether or not to pursue a contingency case. Interestingly, when contingency practitioners were discussing refusal of DBCF funding, more respondents discussed the expected length of the hearing as relevant; only a couple noted that they were more prepared to do a damage-based contingency fee where a case was likely to settle.

258. Discrimination cases were repeatedly mentioned as being likely to take up a lot of time, making them more unsuitable for damage-based contingency fees. This contrasts with comments suggesting their suitability based on the potential for unlimited compensation (see Figure 6 at page 81 above), and suggests that a claimant's chances of getting a DBCF for a discrimination case depends on the approach of the individual practitioner.

259. One claims consultant commented that, as a one-man-band, it was unfeasible for him to take on lengthy cases under damage-based contingency fees as not only was it unprofitable, it also prevented him from taking on other deserving cases.

### **Case Complexity**

260. A quarter of DBCF practitioners thought that the complexity of a case affected its suitability. Around one in seven stated that rejection occurred when a case was too complex. A few interviewees commented on the subsequent impact on access to justice. For example:

*Sex or disability discrimination, or equal pay case are not suitable for contingency fees as they are too complex. This presents a gap; claimants cannot fund these types of case unless they have LEI [or can afford the hourly rate]. (IV177)*

261. These comments imply that certain types of case may be excluded from contingency funding because of their complexity. If this were true it would create a lottery, whereby a claimant would have to suffer a certain type of grievance before he could obtain a damage-based contingency fee. Over a third of the interviewees who spoke about complexity suggested that discrimination cases were too complex for damage-based contingency fees. Thus although discrimination allows for unlimited compensation, its suitability is decreased because it is complex and likely to take up much time. Other types of case sometimes suggested to be too complex were equal pay, constructive dismissal and claims under multiple heads.

262. It is worth noting that claims consultants were more likely than solicitors to suggest that they refused contingency funding where a case was particularly complex. Whilst this might be due to lesser levels of qualification in claims consultants, almost half of claims consultant interviewees expressly mentioned some form of legal qualification, with half of these being fully qualified barristers/solicitors. These figures may be higher as we did not expressly address levels of legal qualification in the survey. Furthermore, claims consultant interviewees generally specialised in employment law. An alternative view is that concern with case complexity could stem from the fact that they were more likely to work within tiny businesses, often as one-man-bands. Complex cases are probably more time-consuming and more risky. Spending much time on one risky case is highly undesirable when it constitutes a majority of the business's income.

### **Client Characteristics**

263. Around a fifth of interviewees who used damage-based contingency fees stated that certain client characteristics affected how suitable a case was for such funding although less than one in ten indicated they refused a DBCF on this basis.

264. Several participants would not offer a damage-based contingency fee if they considered that the client's story would not stand up in court. Some suggested that the problem is with dishonest claimants; others simply talked in terms of clients making bad witnesses. CM06 went further and suggested that he would not offer a DBCF if he did not "like the look of the client". Access to DBCF representation is thus sometimes dependent on a practitioner's assessment of his client's credibility.

265. Other participants considered that clients with unrealistic expectations about case outcomes and/or clients only wanting a day in court were unsuitable for damage-based contingency fees. Suitable clients focus solely on obtaining compensation and have a responsible approach towards their case. IV98 considered that the less likely a client is to gain future employment, the more suitable his case is for a damage-based contingency fee because of increased potential compensation. She gave the example of persons approaching retirement. IV306 would not offer such funding where "the client is well off and just being cheeky".

266. A few practitioners suggested that cases are suitable for contingency funding if the client cannot afford the hourly rate. Poorer claimants are likely to have lower value cases, and thus this factor would be in tension with factors geared towards profitability.

### **Other factors potentially influencing the offering of DBCF funding**

267. Contingency practitioners offered some alternative factors as influencing case suitability for damage-based contingency fees, including: respondent solvency; how high-profile a case is; sympathy for the client; group actions; and the location of any tribunal hearing.

268. Other situations in which a DBCF would be declined were: where the client has LEI or where using a damage-based contingency fee would lead to conflict with an arrangement the firm has with a Trade Union.

### **Practitioner opinions on spurious claims**

269. The above data is consistent with practitioners assessing cases on their merits and economic return before taking a claim on a DBCF basis. Nevertheless our survey did provide opportunities for the issue of spurious claims to be discussed. In particular, this was raised when interviewees were asked about issues relating to opponents using damage-based contingency fees. Around one in ten suggested spurious claims as an issue.

*The main abuse in contingency fees is where representatives take on cases on the basis that the company will pay just to avoid the hassle of the case. They take on low merit cases just to get a settlement. This is essentially blackmail of employers; they payout to avoid the costs of defending the claim. (IV152)*

*Contingency fees are propping up a system of claimants being able to have a go without fearing any consequences of paying. (IV117)*

270. Some interviewees accused the DBCF practitioners of creating the problem. IV66 considered that they tend to conduct litigation “en masse” without assessing claim merits. Several respondents suggested that such practitioners will take on claims with little merit with the sole aim of obtaining a settlement:

*The opposition takes on cases where there is a reasonable prospect of settlement and not where there is a reasonable prospect of success. (IV141)*

271. A few accused contingency practitioners of advising claimants to bring unmeritorious claims. IV159 suggested that spurious claims are leading to respondent clients becoming “disenchanted” with the system.

272. The level of complaints is modest and generally made by those who did not have experience of bringing contingency fee cases themselves. Sometimes, their reasoning showed a lack of understanding of how DBCFs fees work. For instance, IV57 suggested that only claimants with weak cases would agree to lose a proportion of compensation. The likelihood of course is that claimants will lose some of their money win or lose when paying hourly. Occasionally concerns were raised by those with some experience: CM09 commented that, as a contingency practitioner, he tends to attract “perhaps less worthy cases” whilst also noting that many cases have “perfectly reasonable prospects of success”.

### **Quality of claims and equal pay**

273. This report does not purport to speak definitively about equal pay cases, particularly given the fluidity of the situation and the fact that many cases are unresolved. Nevertheless, given the furore over equal pay cases, we do discuss equal pay cases, partly to recognise that this is an area which gives rise to unusual and difficult problems, but also to suggest that in terms of DBCFs impact on *individual* claims, available evidence remains consistent with the view that DBCFs promote access to justice, albeit problematically.

274. It is important to preface these remarks by emphasising that for all the organisations involved in equal pay cases, the stakes are high. The issues are complex and continue to unfold.

275. The points above about the economics of contingency fees apply also to equal pay cases. There are some differences, notably the mass nature of these claims, but it is clear by the way that equal pay cases are being litigated that the costs of bringing even mass claims is likely to be high (although that is not to say that proportionately the profits from such cases may not be higher than other employment claims) and one would expect that the practitioners bringing the cases would need to be confident, in general, of the merits of the cases that they brought.
276. Criticism of no win no fee lawyers in this arena have principally come from two constituencies: local government and the trade unions. In the simplest of terms, they indicate that the presence of DBCF lawyers in equal pay cases has had a detrimental impact on the collective resolution of equal pay cases. DBCF lawyers counter with an allegation that trade union members have had their individual interests compromised in ways which are discriminatory, of significant detriment to them and without their free and informed consent. The nature of the dispute is set out in the opening three paragraphs of the Court of Appeal judgment in a leading case on the problem *Allen v GMB*:<sup>91</sup>

*1. Prior to 1997, the terms and conditions of employment applicable to local authority employees were set out in different documents which were referable to different categories of employees. Manual workers were governed by the White Book whilst administrative, professional, technical and clerical (APT&C) workers were governed by the Purple Book. A third category of craft workers came under the Red Book but this case does not concern that category. As regards the White Book and Purple Book employees, it was recognised that some gender-based pay inequalities had been allowed to develop. In 1997 a national collective agreement – the Green Book – was negotiated between the relevant trade unions and the local authority employers. The intention was to bring the White Book and the Purple Book employees under a new system with a common pay and grading structure. It was to be known as "single status". Although the overarching structure of single status was the result of a national agreement, it was envisaged that actual pay scales and pay rates would be devolved to local level and that, in order to eradicate historical inequalities, local agreements would be preceded by local job evaluation studies. Each job would be assessed and placed on the appropriate Green Book scale. This proved to be a complex exercise. In Middlesborough, a job evaluation study was carried out and, in due course, new terms and conditions reflecting it came into effect on 1 April 2005. GMB (the Union) was one of the unions which negotiated the new terms and conditions with Middlesborough Borough Council (the Council).*

*2. The complexity of these circumstances is plain to see. From the Council's point of view, the funding of any pay deal is heavily dependant upon the flow of money from central government and takes place against the backdrop of "capping". On the other side, the Union has to represent*

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<sup>91</sup> *Allen and others v GMB* [2008] EWCA Civ 810; [2008] WLR (D) 243

*members in different categories whose interests can and do conflict. Put very simply, the Council sought an outcome that was affordable. The Union wanted one that somehow compensated the victims of past inequality but at the same time provided a measure of pay protection for those who were disadvantaged by the job evaluation study and maximised the amount available for future pay across the board. In addition, the Union was constrained by the natural perception that, if it pushed too hard, the consequences might include job losses and contracting out, neither of which would be in the interests of its members.*

*3. It is beyond dispute that, faced with these conflicting pressures, the Union decided to give priority to those who needed pay protection and to achieving equality and better pay for the future rather than to maximising claims for past unequal pay. The deal done between the Union and the Council provided the White Book women with some compensation for the historical inequalities (in the region of 25% of the full value of successful equal pay claims) but did not provide the Purple Book women with any such compensation, the Council having apparently taken the view that their equal pay claims were without merit.<sup>92</sup>*

277. Allegations that the Union had indirectly discriminated against some of its members were advanced on the following basis:

*First, the Union had failed to protect the interests of the claimants by not pursuing proceedings at an early stage so as to establish an early date for the calculation of back pay. Even if the Union had preferred not to litigate, it should have protected the claimants in this way. Secondly, the Union had deliberately omitted to give advice about back pay and had refused to support litigation in order not to antagonise the Council or to delay or impede the progression to single status. Thirdly, the Union had "rushed headlong" into an ill-considered back pay deal. It had accepted too readily the Council's plea of poverty. Finally, and, it seems, crucially, the Union had failed to give the claimants a fully informed choice about the options available to them. They had not been informed that what they were being offered was substantially less than they might receive following successful litigation and there was no assessment of the litigation risk which the ET considered to be relatively small, at least for some of the claimants. The ET considered that, if the Union was going to require the claimants to make some sacrifice in the interests of other members, then that should have been made plain to them. There had been not only a failure to provide full information but also positive manipulation of "relatively unsophisticated claimants" by suggesting that the offer from the Council was acceptable and placing them in a position where they were in fear that, if they pressed for more, it might lead to job losses and to their being seen as traitors by their colleagues. The ET considered this to be "the worst aspect of the case".*

278. The Court of Appeal supported the Employment Tribunal's finding of indirect discrimination placing considerable emphasis on the Unions's dealing with "some of its members with marked economy of truth in what it says and writes to them."<sup>93</sup>

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<sup>92</sup> Cited note 91 Para. 10

<sup>93</sup> Cited note 91 Para. 24.

279. We neither know, nor offer opinion on, whether these problems are manifest more generally in the equal pay arena. What *Allen* illustrates is the tension between collective bargaining and individual employee rights and the potential for significant injustice to arise. Beyond the facts of *Allen*, we specifically do wish to draw attention to is a point about the quality of equal pay cases. As far as we are aware, the Local Government Employers organisation's main criticism is not the merits of the individual claims, but the impact of such claims on local government finance, collective negotiation and interests beyond those of the individual. For them, equal pay cases involve a bargain being struck which protects the interest of local authority residents, employees who benefit from (and are threatened by) the processes of job evaluation associated with equal pay, and the impact of settlements on job security. NWNF lawyers' significance, beyond any increase in the number of cases they are directly responsible for, LGE states, has been to stiffen the approach of trade unions to these cases, particularly in light of the *Allen v GMB* decision: forcing them to bargain harder for the rights of their members *full* entitlement to backpay.<sup>94</sup>

280. Trade union criticisms of DBCF lawyers do concentrate in part on the quality of the cases brought, but not to suggest that they generally bring cases with poorer merits.<sup>95</sup> In fact they claim the opposite: that DBCF lawyers cherry-pick the better cases, leaving trade unions deal with a wider range of cases including those that are not so straight-forward. This emphasises the potential narrowness of any access to justice contribution made by DBCFs but it is not consistent with a view that DBCFs have led to an increase in unmeritorious cases. They also make significant complaints about the costs advice given to clients under DBCFs; the ways in which clients are bound into ('handcuffed') to lawyer settlement decisions; the fact that trade union members who bring cases under DBCFs would have deductions made from damages under DBCFs which would not be made by union funded solicitors; and the advertising material used to persuade union members to take cases under DBCFs rather than through trade unions.<sup>96</sup>

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<sup>94</sup> Local Government Employers (2006) *Unblocking the route to equal pay in local government* (London: LGE)

<sup>95</sup> They also allege that claims are not well-handled, partly because of the high volumes involved.

<sup>96</sup> This research was not designed to concentrate on equal pay cases although most of these complaints are addressed more generally in our analysis of the consumer interest issues posed by employment DBCF cases.

281. There continues to be significant criticism in the press in relation to equal pay claims against public sector employers being brought under DBCF agreements.<sup>97</sup> Employers and Trade Unions continue to argue that these claims undermine collective negotiations to secure sustainable equal pay packages for all workers and that budgets are being stretched by compensation awards, which could lead to job losses and/or reductions in male workers' salaries.<sup>98</sup> Councils have suffered severe financial difficulties as a result of the level of claims and have had to borrow from the government to meet compensation awards.<sup>99</sup> BERR has also expressed concern over the operations of damage-based contingency fee lawyers in equal pay claims, suggesting that they make negotiation agreements "difficult" and "further complicate the situation and are sometimes contrary to the best interests of the claimant".<sup>100</sup> Conversely, *Allen* shows how it can be successfully argued in some cases that the Trade Unions have at least in some cases failed to properly represent their members at an individual or collective level.<sup>101</sup>

282. Importantly, at root, equal pay claims, whether funded by the unions or DBCF lawyers, arise from major structural problems in public sector pay and a fundamental problem in balancing individual and collective rights, not from any problem with the legal merits of DBCF cases. It is not alleged that they are 'bad' cases, rather that individual cases should not take precedence over collective agreements; and that the local authorities can better compromise those agreements collectively with unions. Put another way, any growth in

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<sup>97</sup> See, for example, D. Prentis & P. Kenny 'The way to achieve equal pay is through unions, not these lawyers' *The Guardian* (London 8th January 2008); D. Brindle & P. Curtis 'Fight for equality that could put jobs at risk' *Guardian* (London 2<sup>nd</sup> January 2008); J. Robins, 'Who's best at getting equal pay for women?' *The Observer* (London 12<sup>th</sup> August 2007); J. Sherman, 'Council tax to rise as 'parasitic lawyers' chase equal pay claims' *The Times* (London 6<sup>th</sup> March 2007).

<sup>98</sup> J. Sherman, 'Men are to pay a high price for sexual equality' *The Times* (London 12<sup>th</sup> March 2007); D. Rowbottom, 'Re-inventing the collective approach to equal pay' (2005) 155 N.L.J. 1701; D. Brindle and P. Curtis, 'Fight for equality that could put jobs at risk' *The Guardian* (London 2<sup>nd</sup> January 2008).

<sup>99</sup> H. Siddique, 'Council boost for equal pay claims' *The Guardian* (London 28<sup>th</sup> September 2007); P. Curtis, 'Council's face £2.8bn bill for equal pay' *The Guardian* (London 2<sup>nd</sup> January 2008).

<sup>100</sup> Business and Enterprise Committee, 'Jobs for the Girls: Two Years On: Government Response to the Committee's Second Report of Session 2007-08' HC (2007-08) 634 [51] & [53]; 'All-party MPs' call for equal pay reform' (2008) 46 IDS D.W. 2, p.3

<sup>101</sup> See, for example, J. Robins, 'Cash: Home Loans: Unions under renewed attack for failing low-paid women members: Female workers angry at the GMB for selling them short in a compensation deal have triumphed at court' *The Observer* (London 24<sup>th</sup> August 2008); J. Robins, 'Who's best at getting equal pay for women?' *The Observer* (London 12<sup>th</sup> August 2007).

DBCFs in equal pay cases appears to be consistent with increases in individuals access to justice (on current evidence and subject to some of the broader concerns discussed at para. 280). The problem is that local authorities are unable or unwilling to afford the liabilities associated with individual rights to equal pay. The Unions have recognised the dilemma and put the economic and employment interests of the collective above it's members individual legal rights, striking a bargain that is better for some (more often, but not always, men) and worse for others (more often women). Some of the losers, assisted or led by DBCF practitioners, have exposed the problems. Law and public finance have collided.

### **Practitioner views on DBCFs and access to justice**

283. Our survey also collected opinions on the access to justice issue. Generally, practitioners appeared to subscribe to the view that DBCFs widen access to justice because they enable claimants who could not otherwise afford to claim to be able to do so; almost three-quarters of respondents spoke in such terms when asked to consider the advantages of DBCFs. As IV141 put it:

*[T]he good thing about contingency fees is that the claimant gets proper legal advice; he at least has an informed legal advisor.*

284. Several discussed the alternatives, particularly self-representation. For example, IV77 thought that:

*You can't have employment law getting more and more complex and have no funding assistance available. To ensure access to justice for all we need contingency fees; they provide access to good lawyers.*

285. Three solicitors commented on what they saw as the lower quality of representation provided by CABx and Law Centres.<sup>102</sup> One of these suggested that this is due to the huge workload of these organisations.

286. Other interviewees suggested that the most likely alternative to a contingency fee was not self-representation, but not bringing a case in the first place. Around one in ten of the

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<sup>102</sup> In fact, the evidence tends to contradict the view amongst practitioners that solicitors provide better quality services than non-lawyers where the non-lawyers are specialist advisers (See, Moorhead R, Sherr A and Paterson A, (2003) *Contesting Professionalism: Legal Aid and Non lawyers in England and Wales*, 37 (4) *Law and Society Review* 765-808)

respondents discussing access to justice commented on the lack of alternative funding available to the claimant, in particular the absence of legal aid for employment proceedings:

*Contingency fees are useful as legal aid is in other areas of law; they allow members of the public to bring cases they otherwise could not. (IV306)*

287. A couple of interviewees clearly disliked contingency arrangements but considered them necessary given the lack of legal aid.

*As there is no legal aid in employment, contingency fees are important for access to justice ... They are a necessary evil given the system that we have. (IV217)*

288. These practitioners view damage-based contingency fees as the mechanism by which poorer individuals afford access to the legal system. However, it is important to emphasise their availability depends on factors completely unrelated to the claimant's financial circumstances and, as we shall see, often case selection focuses on the practitioner's, as opposed to the client's, interests. Further, IV204 suggested that clients may be vulnerable and willing to agree to any offered contingency agreement terms because of the lack of alternative funding options.

289. There may be a somewhat arbitrary relationship between damage-based contingency fees and access to justice, with access depending on whether consumers stumble across someone willing to act on a DBCF:

*Employees don't know what to do and people like me are hard to find. Solicitors are unlikely to offer contingency fees and there is no legal aid available. There is no incentive for solicitors to offer contingency fees. Big firms especially would never offer them; they would become overloaded with work. (CM15)*

290. Interestingly, practitioners did not always approach the access to justice issue purely from clients' perspectives; sometimes DBCFs permitted professional vindication. Two interviewees suggested that damage-based contingency fees provide personal satisfaction for the lawyer in assisting poorer claimants. IV85 described the "moral sense of justice" in helping an otherwise unfunded client. CM23 considered it unfair that claimants should appear unrepresented at tribunal. IV254, whose firm does not offer damage-based contingency fees, commented that when she meets clients who cannot afford to pay her she often wants to help but can't.

## Summary

291. There is inadequate evidence to draw firm conclusions about the impact of DBCFs on the number of claims. What is clear is that increases in employment tribunal business are unlikely to be wholly or mainly explained by the impact of DBCFs. Underlying changes in substantive law and particular problems around equal pay are significant factors.
292. That said, it may be that DBCFs have increased the number of claims somewhat (and in equal pay cases there appear to have had a stronger effect). As we discuss above: access to justice debates must focus not only on the number of claims but also their quality. On the latter, our data is consistent with DBCFs increasing access to justice. In particular, the weight of evidence points towards practitioners using DBCFs exercising significant controls over the quality of cases they bring on DBCFs. In particular, the evidence generally points towards a case needing to be of a reasonably high value and/or sufficiently likely to succeed before the claimant will be offered a DBCF. Other factors, including case duration and complexity, come into play but these are generally of less importance.
293. The situation is much more complex in equal pay cases but even here, the situation does not appear to be one in which DBCFs have led to a decrease in the quality (legal merits) of claims brought. Rather, DBCFs have exposed a critical tension between individual and collective resolution of employment rights and emphasised the existence of legal rights which local authorities are struggling to meet.
294. It is important to emphasise, however, that DBCFs are not unproblematic in access to justice terms, even from claimants' perspectives. Clearly lower value claims are less likely to be brought under DBCFs and it is this group in particular which is likely to struggle to afford representation (and may be most likely to struggle also with self-representation). There is also considerable variability in the risk assessment practices of advisers: this depends not only on the characteristics of the case but also the context within which practitioners work. This may mean that access to justice through this mechanism is something of a lottery, particularly if (as the evidence generally suggests) clients do not generally shop around.<sup>103</sup> For

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<sup>103</sup> Yarrow and P. Abrams cited note 11; See, also Pleasence et al (2006) *Causes of Action: Civil Law and Social Justice* (2nd edition), Norwich: TSO.

practitioners desperate for the work incentives to take on weaker cases (even spurious cases) may remain, albeit at some risk, but our evidence does not suggest this is a prevalent problem.

295. On balance then, and in spite of these problems, it should be recognised that particularly for claimants without LEI or trade union membership, and in the absence of legal aid, DBCFs represent an additional means of providing access to justice which may be their only hope of securing representation.

## 10. Conflict of Interests

296. A major criticism directed at DBCFs is that they pit the lawyer's interests against those of his client. In particular, there is a perceived danger that DBCF representatives will give settlement advice solely with their own financial interests in mind, i.e. taking into account hours worked in relation to reward to be gained, as opposed to seeking to champion the client's best interests.

297. Early theoretical models<sup>104</sup> suggest that DBCF lawyers will settle for lower sums than hourly counterparts because of diminishing their efforts on a given case,<sup>105</sup> although Rickman questions the assumption of diminishing returns to lawyer effort: an adviser's willingness to incur cost and pursue the claim may signal case strength and achieve a better outcome for the client.<sup>106</sup> Another interpretation is that hourly fees provide an incentive to over-service clients relative to contingency fees. Empirical testing of both propositions is rare and inconclusive.<sup>107</sup>

298. Contingency fees have also been accused of both slowing down and speeding up the time to settlement.<sup>108</sup> Helland and Tabarrok's empirical work points to the latter being true in medical negligence cases.<sup>109</sup> This could lead to under settlement of cases as representatives seek to recover quickly and avoid going to tribunal.

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<sup>104</sup> For example, Schwartz, Murray .K. and Daniel J.B. Mitchell (1970), *An Economic Analysis of the Contingent Fee in Personal Injury Litigation*, 22 Stanford Law Review 1125 and Clermont and Currihan cited note 74

<sup>105</sup> See also Emons, Winand (2000) *Expertise, contingent fees, and insufficient attorney effort*, 20 International Review of Law and Economics. 21 – 33.

<sup>106</sup> Rickman, Neil. (1999) *Contingent fees and settlement in litigation*, 19 International Review of Law and Economics. 295 – 317.

<sup>107</sup> See, Thomason, Terry (1991), *Are Attorneys Paid What They're Worth? Contingent Fees and the Settlement Process*, 20 Journal of Legal Studies 187 and Helland and Tabarrok cited note 74. See also Kritzer, H. M. (1990) *The Justice Broker: Lawyers and Ordinary Litigation* (OUP).

<sup>108</sup> Olson, Walter K. (1991) *Sue City: The case against the contingency fee*. Policy Review and Miller, Geoffrey P (1987) *Some agency problems with settlement*. 16 Journal of Legal Studies 189 – 215.

<sup>109</sup> Helland Eric and Tabarrok Alexander. (2003) cited in note 74

299. Hammersley et al found that damage-based contingency fee cases were more likely to be settled than cases involving hourly payment;<sup>110</sup> that contingency cases were more likely to be privately settled and less likely to be settled through ACAS;<sup>111</sup> and that contingency claimants who do go to hearing do less well than claimants not using the arrangements.<sup>112</sup>
300. As noted above (para. 77 onwards), some non-DBCF practitioners suggested conflicts of interest as a reason for not offering the arrangements. Our study examined in more detail practitioner perceptions of the settlement process as well as collecting data on the consequences contingency claimants face should they reject their representative's settlement advice.
301. Figure 8 shows the results for practitioner assessment of whether DBCFs impact on decision to go to a hearing. Practitioners using DBCFs were asked whether their own use impacted on the likelihood of going to a hearing (results shown under the 'Me' column). Because practitioners may be wary of saying their case tactics were altered by DBCFs, practitioners were also asked what happened when their opponent was on a DBCF (results shown under the 'Opponent' column).
302. Before we look at the data, it should be noted that funding arrangements do not have to be disclosed in employment proceedings and so a judgment as to whether an opponent is using a damage-based contingency fee is likely to be based on instinct or 'common-knowledge' about an opponent adviser's business model. Indeed, many of the interviewees who indicated that they do not have experience of opposition damage-based contingency fees cited the lack of required disclosure as the reason for their answer. This lack of definite knowledge of opponent arrangements is a problem. There is a danger that preconceptions of DBCFs will reinforce themselves. For example, if a solicitor considers – independently of actual experience – that DBCF practitioners seek to settle, then whenever an opponent does seek to settle that solicitor may assume (rightly or wrongly) that a DBCF is being used.

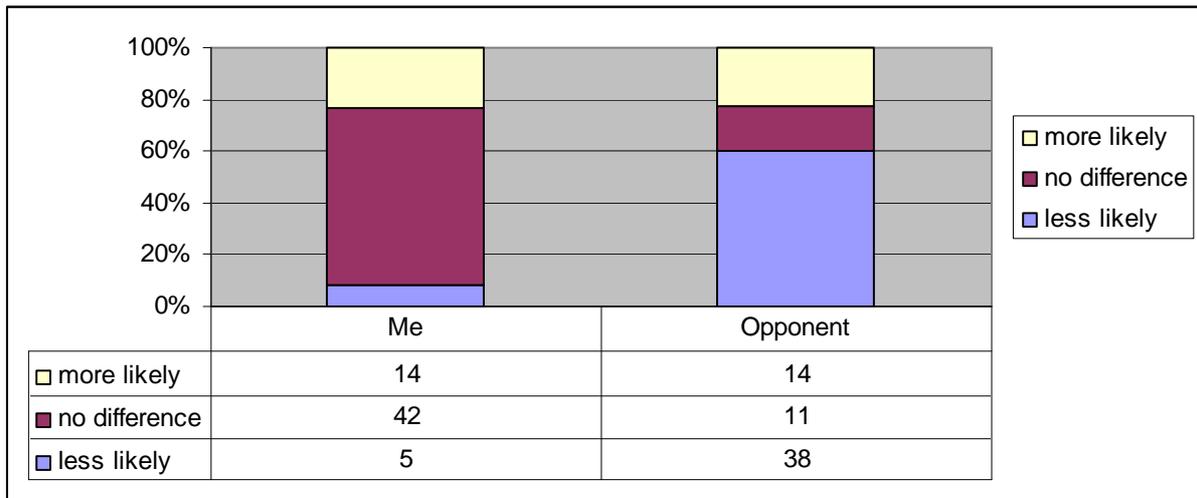
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<sup>110</sup> Hammersley *et al* (2007) cited note 6, p.15. In a much smaller study with a less robust sample, Hammersley and Johnson found that many claimants using contingency fees felt pressured into accepting settlements (Hammersley and Johnson (2004) cited note 6, pp.12-13; Johnson and Hammersley (2005) cited note 5, 26, p.27.

<sup>111</sup> Hammersley *et al* (2007) cited note 6, p.15

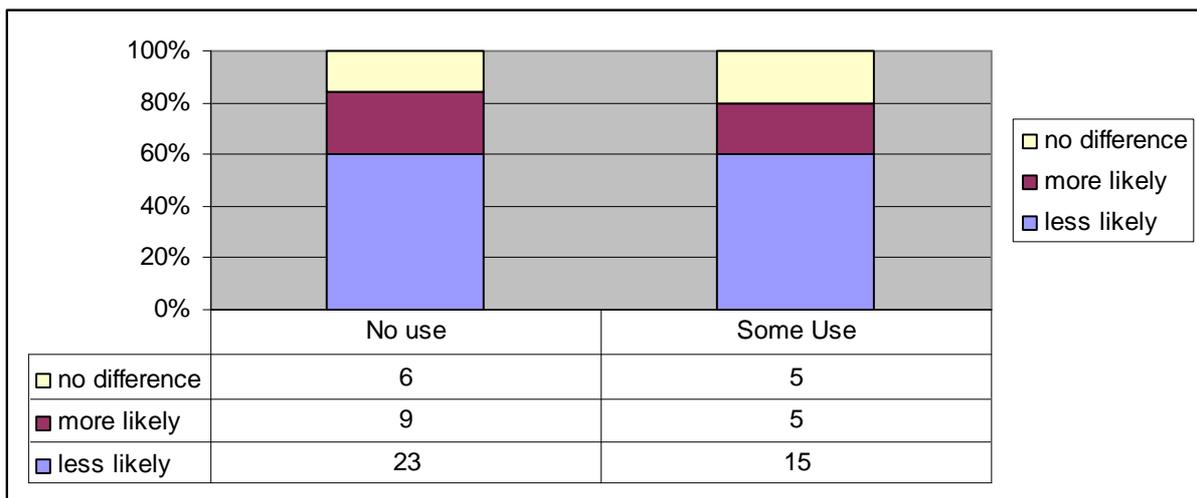
<sup>112</sup> *Ibid* p.18

Figure 8: Does using a contingency fee impact on the likelihood that a case goes to full hearing?



303. Whilst those using DBCFs tended to say it made no difference to the likelihood of a hearing, when those who had experience of their opponents were asked to consider their opponent they tended to take the view that DBCFs made tribunal hearings less likely. Importantly, given the possibility that those without experience are simply expressing a prejudice, this view was offered by both practitioners who did and did not use DBCFs themselves, in very similar proportions (see Figure 9).

Figure 9: Does using a contingency fee impact on the likelihood that an opponent's case goes to full hearing (by use and non use of DBCF)?



304. Similar questions were asked about the timing of settlement and impact on the level of settlement (Figure 10).

Figure 10: Does using a contingency fee cause settlement to be earlier or later?

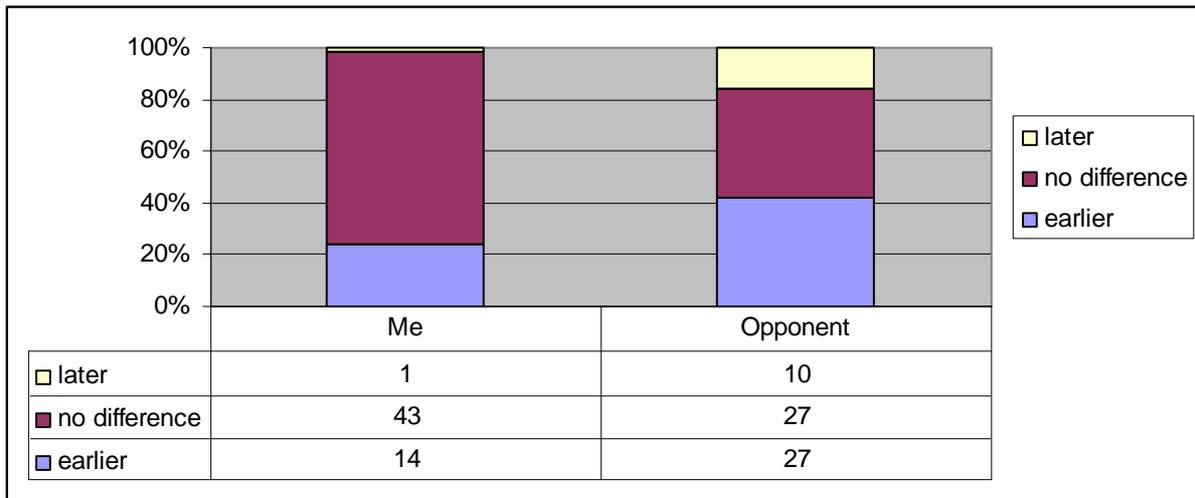
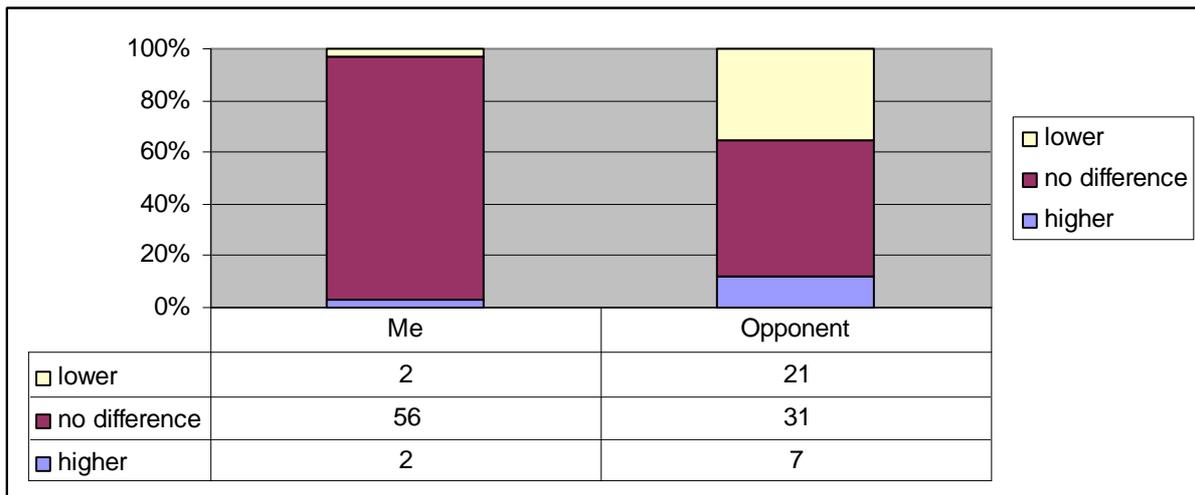
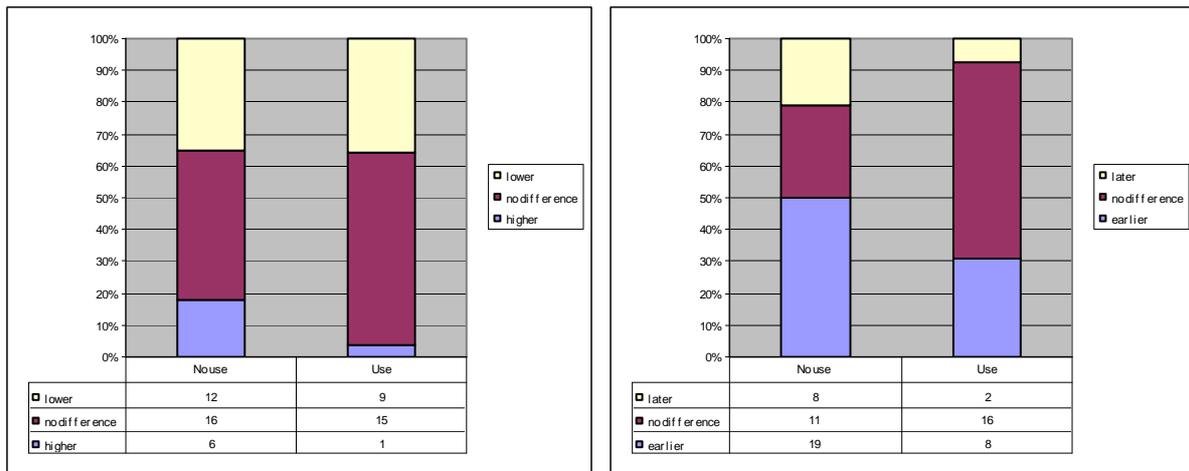


Figure 11: Does using a contingency fee make the level of compensation accepted under settlement higher or lower?



Variations by practitioner use of DBCFs (for answers discussing opponent practice) are show in Figure 12.

**Figure 12: Variations in settlement timing and value (discussing opponents' practices only)**



305. Similar proportions of practitioners thought that DBCFs would lead to lower settlements although the most common response was that it made no difference for both groups. In terms of timing of settlement, those who used DBCFs thought their opponents were unlikely to alter the time at which they settled; those who did not use DBCFs thought settlement was likely to occur earlier.

306. It follows that there is reasonably consistent evidence from these interviews that DBCF cases are more likely settle without a tribunal hearing (with the exception that DBCF practitioners do not think they themselves are more likely settle DBCF cases before hearings). There is also some evidence that practitioners think that cases may settle for less and sooner than non-DBCF cases but this is more equivocal.

### **What percentage of cases go to a full hearing?**

307. We also tackled this issue less directly by asking in another part of the interview what proportion of the interviewees cases generally went to a hearing. We would expect that, if DBCFs did impact on settlement behaviour, this might show up in their estimates of cases that went to a hearing. On average respondents said that about 20% of their cases went to a full hearing (mean, 189 responses). Variations in relation to firm size, etc., are shown in Table 21 but do not appear to be statistically significant.<sup>113</sup>

<sup>113</sup> Analysis of variance (Anova) p . > .05

**Table 21: Proportion of cases going to a full hearing**

| Firm Size | Mean (%) | N   | Team Size   | Mean (%) | N   | Emphasis of employment practice   | Mean (%) | N   |
|-----------|----------|-----|-------------|----------|-----|-----------------------------------|----------|-----|
| Tiny      | 20       | 27  | Sole Team   | 15       | 28  | Mainly Respondent Work            | 20       | 110 |
| Small     | 24       | 25  | Small Team  | 22       | 39  | Mixed Claimant and Defendant Work | 21       | 48  |
| Medium    | 20       | 53  | Medium Team | 20       | 39  | Mainly Claimant Work              | 22       | 31  |
| Large     | 18       | 75  | Large Team  | 19       | 42  |                                   |          |     |
| Total     | 20       | 180 | Total       | 20       | 148 | Total                             | 20       | 189 |

308. The difference between claims consultants and solicitors however is more marked and significantly different. On average, solicitors reported that 19% of their cases go to tribunals, whereas the figure was 30% for claims consultants: a significant difference.<sup>114</sup>

309. Those who make considerable use of damage-based contingency fees also indicated a higher level of cases going to a full hearing, contrary to what would be expected from the other interview data, but again this did not reach conventional levels of statistical significant difference (See Table 22).<sup>115</sup>

**Table 22: Proportions of Full Hearings and use of damage-based contingency fees**

|  | Mean | N   |
|--|------|-----|
| No use   | 20   | 125 |
| Up to 25% use of damage-based contingency fees     | 17   | 43  |
| More than 50% use of damage-based contingency fees | 28   | 21  |
| Total  | 20   | 189 |

<sup>114</sup> Two-tailed T-test, p = .023

<sup>115</sup> Anova, p=.131

### **Participant discussion of the conflict of interests issue**

310. A significant proportion of participants commented on the conflict issue, predominantly when talking about the disadvantages to clients in using DBCFs: over a quarter of respondents suggested it as a client drawback.

311. Solicitors appeared more likely to suggest conflicts of interest as a negative aspect of DBCFs than CMCs. This may be because the centrality of their professional obligation to act in the client's best interests makes them more aware of any potential for conflict. Interestingly, practitioners making frequent use of damage-based contingency fees were much less likely than infrequent/non users to suggest conflicts of interest as disadvantageous.

### **Settlement Issues**

312. The overwhelming majority of discussion of conflict of interests centred around its impact on settlement. Many interviewees pointed out that conflict arises because the lawyer's fee depends on the compensation received in relation to hours worked:

*With a contingency fee, the lawyer is always assessing settlement in relation to costs incurred. If the respondent offers an appropriate settlement which covers their costs then they may be tempted to take the money and run. This may not be the best for the client. (IV244)*

*Once an offer comes in at a certain level the solicitor may encourage the client to settle, as he knows that at this level he will get a return on his fees ... The solicitor is inhibited from giving a truly objective opinion because he is mindful of the need to recover costs. (IV199)*

313. Some practitioners went into detail about the actions which DBCF practitioners are likely to take in relation to settlement. Many simply suggested that they seek to settle as opposed to going to tribunal:

*[The lawyer's] principal aim is to settle rather than to go to a full hearing, because of the costs involved and the chance of losing. (IV101)*

*The solicitor may be tempted by a sum of money offered as a settlement just because he will then get paid. He may persuade the client to accept the settlement just so that he can get his fees and avoid the litigation risk. (IV221)*

314. IV197 suggested that there is a conflict because the client loses control over the decision to go to tribunal:

*With settlement negotiations, the solicitor may want to avoid the risk of litigation and settle but the client may want to go ahead with a full hearing. This could lead to conflict. Normally you would do what the client wants but there is a conflict with contingency fees.*

315. IV124 commented that individuals have come to her and reported incidences where DBCF practitioners have refused to represent the client if he insisted on proceeding to full hearing, and suggested that often these claimants could have got more at tribunal.

316. Other participants suggested that contingency practitioners will seek to settle earlier in order to “maximise billing” (IV275). If a case settles quickly then the solicitor has worked fewer hours and consequently any settlement will be worth more to him.

*The interests of the client are usually to take litigation as far as possible, whereas the solicitor wants to settle as early as possible when he is using a contingency fee. (IV175)*

317. IV117 considered that the situation is the same where the client has insurance or is supported by a Trade Union; the representatives involved “wants a quick deal at the lowest possible expense”. If this is the case then it may be that contingency clients are no more disadvantaged as regards settlement than those using LEI or their Trade Union.

318. In a similar vein, a handful of interviewees stated that contingency practitioners may settle for lower amounts to cover costs. IV244 commented that a previous client had come to her asking for a damage-based contingency fee but she refused. The client consequently went to another firm to seek the funding. According to IV244, he later told her that:

*[T]he solicitors bullied him into accepting a settlement of half of what his claim was worth, and then took a percentage of that amount.*

319. Comments relating to the conflict of interests in relation to settlement generally imply that the client’s interest is in taking the case as far as possible, suggesting an assumption that doing so leads to greater recovery. If this is the case, then clearly the best course of action for the contingency client is indeed to continue as opposed to settling; he will get more money and the fee payable to his representative remains an agreed percentage of this award. However, the hourly paying client must weigh the likelihood of increased compensation against future costs, and it may not always be in that client’s financial interests to continue. It could be argued that if an hourly paid client would settle because of the cost disadvantage in continuing, then a contingency client is not really disadvantaged if he is pressured into settling for a similar amount. With damage-based contingency fees, it is simply that the cost-benefit analysis is done by the practitioner (who better understand the risks and costs involved) and not the client.

320. A few practitioners appeared to go against the general consensus that for the contingency practitioner settlement is best and earlier is better. For example, IV217 thought that

contingency solicitors may fight a risky case where otherwise they would settle. IV86 thought that the representative may push for a higher figure where this may not be in the client's best interests.

321. Several participants did not speak in terms of settlement of an individual case; seeing pressure to settle as being more pervasive. IV121 made the point that:

*Looking at it as a business model, it is better to submit ten tribunal claims and get ten low settlements rather than fight for one higher settlement.*

322. This argument is worrying because it emphasises how pressure to settle might impact across a cohort of cases, not on an individual or idiosyncratic basis.

### **Other issues around conflicts**

323. IV306 expressed a desire to avoid *accusations* of an “ulterior motive” in advising clients, whilst being quick to point out that he would not cave in to such temptation. Thus not only are practitioners concerned to avoid damage-based contingency fees because of the temptation to act in a self-interest manner, they are concerned to avoid them because of association with the negative *perception* that they will act with self-interest. IV69 suggested that the lack of Law Society safeguards in relation to the situation makes it, “likely...that the client will suffer at the hands of the solicitor”. Four interviewees suggested that practitioners may try and do less work or cut corners in order to maximise fees, which is clearly not in the client's best interests. The temptation to do less work conflicts with the claimant's desire for a comprehensive service.

324. IV55 commented that some clients, such as bankers, understand the damage-based contingency fee environment and so “are in a position of equality”, which reduces the significance of the conflict of interests issue. However, those who have been unfairly dismissed and are unemployed are not in a position of equality; rather, “the lawyer has the bargaining power”.

### **The comparison with hourly rate fee structures**

325. Proponents of hourly charging often argue that they avoid the conflict of interest inherent in damage-based contingency fees. For example:

*The beauty of an hourly rate is that you are not interested in the financial outcome of the case; you just go for the best and most just result. (IV217)*

326. However, with an hourly rate the lawyer's interest is in taking time with the work, which may also not be in the client's interest. Only a very small proportion of interviewees acknowledged that a comparable conflict can exist when the solicitor is being paid by the hour. A difference, admittedly, is that hourly paid lawyers do not usually risk getting nothing if they lose and so there may be less pressure to vindicate a personal interest. IV59 suggested that "it is easier to distance the conflict when you are on an hourly rate". Nonetheless the potential conflict still exists and it is unrealistic to confine conflict of interests only to the damage-based contingency fee realm.

327. Interestingly, eight interviewees explicitly rejected the idea that DBCFs involve a conflict of interest and instead suggested that they align practitioner and client interests. In their opinion, basing a fee on compensation means that the solicitor will work to obtain the highest amount of compensation possible, which is clearly in the client's interests. Two respondents considered the position of the contingency client as favourable to the position of the hourly paid client.

*The client feels that the solicitor is more on his side with contingency fees. The solicitor has an interest in getting more money, and with hourly paid work people often think that the solicitor is wasting time in order to get paid more. (IV202)*

### **Settle or Drop Strategies**

328. Anecdotally, DBCFs are blamed for 'settle or drop' strategies. Practitioners taking cases on DBCFs, trying to settle them quickly and cheaply but then dropping them when the costs of proceeding outweigh the benefits. In the United States, it is reported that lawyers take such cases on this basis, making it explicit to the client that they are taking the case on a settlement only basis.<sup>116</sup>

329. Only two interviewees suggested that opponents using damage-based contingency fees employ settle or drop strategies, i.e. dropping the case if settlement cannot be achieved. These practitioners commented that the case will be dropped immediately prior to hearing

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<sup>116</sup> We are grateful to Bert Krtizer for this point. See also, Moorhead R and P. Hurst (2008) *"Improving Access to Justice" Contingency Fees: A Study of their Operation in the United States* (London: Civil Justice Council)

(i.e. when the solicitor is sure settlement will not occur) and that the client will then be left to represent himself. IV139 suggested that this occurs “quite often”.

### **Respondent exploitation of conflicts**

330. During discussion of practitioner advantages, ten participants (around one in twenty interviewees), all respondent practitioners not using damage-based contingency fees, stated that knowing the claimant opponent is using a damage-based contingency fee allows them to employ advantageous tactics for *respondents*. The majority of these would offer a lower figure based on the assumption that the opposition solicitor would want to settle quickly to avoid costs and/or the litigation risk.

331. One of these interviewees was particularly specific. He assesses how much the claimant is likely to get at full hearing, and bearing this in mind, makes his offers according to how cost-effective it is for the opposition solicitor to fight on. These practitioners are using the potential conflict of interest between contingency client and solicitor to their advantage.

332. Another interviewee stated that when he is aware that the opposition is using a damage-based contingency fee he will make it clear that the respondent will not settle. In his experience the opponent will then drop the claim, although he admitted that this only happens when the respondent has a good case.

333. Three interviewees admitted to creating work for the opposition solicitor in the knowledge that he may not get paid for it. IV77 stated that:

*I'll suggest using the tactic of stringing out the case to try and make [the opposition] settle for less.*

### **What happens when the claimant rejects the DBCF practitioner's advice to settle?**

334. As we have noted, in a DBCF situation the representative's fees are inextricably linked to the financial outcome of a case, and because of this, many practitioners view the arrangements as impacting on settlement practices. The existence of such an impact points to a substantial shift in control over settlement decisions away from the client to the lawyer.

335. Settlement decisions crystallise the economic interests of claimants and their advisers. The client's interest is relatively straightforward. A settlement offer should be rejected if it is likely that they would gain more from a later settlement or, failing that, the Tribunal would be

likely to award them more. The biggest risk to the client is losing the case, in which case they would get nothing. For the DBCF lawyer the situation is more complicated. Not only do they have to gauge the impact of holding out for more on the likelihood they will ultimately be successful, they also have to consider the effort that would be required to increase a settlement offer. If the cost of that effort (which is borne by the lawyer) outweighs the likely return to the lawyer, they will want to settle when the client may want to proceed.

Conversely, where a client is more risk averse than a lawyer, they may want to settle (get a lower guaranteed payment of compensation rather than risking that by going further and risking getting nothing) when a lawyer feels that their return can be increased significantly by holding out for more.

336. As is evident from the discussion on conflicts of interest and the quantitative settlement data, some of our interviewees were plainly sensitive to the potential alignment problems of damage-based contingency fees. Six interviewees went further and explicitly suggested that DBCF clients lose control over their cases. Four of these explained their argument by reference to the use of clauses dictating procedure for client rejection of settlement advice.

*[I]f the firm advises the client that ... a good settlement offer is made and the client refuses [to accept] the firm can end the agreement. If the client was paying an hourly rate then the firm would advise the client in the same way but ultimately they would do what the client wants as he is paying. (IV98)*

337. Another interviewee pointed out that some clients may want a day in tribunal because they feel hurt by their employer, but that in DBCF cases such clauses effectively prohibit them from making such a decision.

338. Evidently, such clauses raise interesting issues of principle and ethics. Because both parties have an interest in the outcome of a settlement, both have an interest in taking the decision. Practitioners have the added claim of having the relevant expertise to be able to judge the quality of the offer; whereas claimants have the legitimacy (and property) arguments that it is 'their case' first and foremost.

339. A solicitor is of course bound by their core duty to the client and, in formal terms, one would anticipate the client's interest trumping the lawyer's. Similarly, even where the interests are properly balanced *in fact* there is also the need to ensure that the client perceives these interests as being properly balanced.

340. There are a number relevant ethical rules but in particular Solicitors Conduct Rule

3.01(2)(b)) states there is a conflict of interests if:

*your duty to act in the best interests of any client in relation to a matter conflicts, or there is a significant risk that it may conflict, with your own interests in relation to that or a related matter.*

341. Guidance on the Rule states:

*You must always be careful to ensure that any settlement achieved for a client, or any advice given in a non-contentious matter conducted on a contingency fee basis, is in the client's best interests and not made with a view to your obtaining your fee.<sup>117</sup>*

342. Because of these issues, all contingency practitioners were asked to explain their procedure upon client rejection of settlement advice.

343. It is important to preface this discussion with the observation that, when we asked contingency practitioners if clients had ever rejected settlement advice, around three-quarters of those who answered indicated that it had never happened, suggesting that in practice clients simply agree to settle. Whilst some indicated this was due to the financial penalties of not-settling provided for under the contingency agreement (one practitioner indicated that the clauses which we discuss below are, “really just there to frighten the clients”: CM21), other explanations for the situation never having arisen included: a practice of warning clients that they may get nothing if the settlement is rejected (CM13); a good relationship with all clients (CM19); clients accepting because they acknowledge that the practitioner is experienced (IV306); or a practice of only selecting clients who are known to the firm (IV65).

### **Settlement clauses in damage-based contingency fee agreements**

344. Upon a client rejecting settlement advice, around three in five contingency practitioners indicated they would automatically terminate the contingency agreement (although we would expect, as about a fifth of these respondents suggested, that a decision to terminate would be based on some assessment of the reasonableness of the rejection by the client). Less than one in ten said they would agree to continue on a contingency basis.

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<sup>117</sup> Para 54, *Solicitors' Code of Conduct 2007* Dated 10 March 2007 and commencing on 1 July 2007 <http://www.sra.org.uk/documents/code/solicitors-code-of-conduct-full.pdf>, last downloaded 7<sup>th</sup> October 2008

345. This suggests that the rejection of settlement advice by the client would usually be fatal to a contingency arrangement. Further, less than one in ten practitioners would agree to continue on an hourly rate basis, suggesting that a majority of practitioners would discontinue representing the client altogether.
346. Clearly then, there is a strong incentive for the client to accept settlement advice; a client is unlikely to want to lose his representative in the midst of a claim. Thus clients of these practitioners have a choice between accepting settlement advice and losing their representation.
347. It was also a reasonably common practice, where an agreement was terminated, that the client incurred a debt for work done to date (often on an hourly basis), which again is likely to deter the client from rejecting advice.
348. Termination clauses were not confined to settlement advice. IV98 was entitled to terminate the contingency agreement where the client was “unlikely to win” indicating that this clause would be used, for example, where initial assessment gives a case high prospects of success but where documents are later disclosed reducing success prospects dramatically.
349. Just four contingency practitioners give their clients the option to continue with the contingency arrangement where the client rejects settlement advice. Three of the four respondents qualified the client’s right to continue. CM14 will only continue “if the business [i.e. the Claims Management Company] accepts the costs implications”; if it does not then the agreement is terminated. IV202 indicated they would generally continue the case “with gritted teeth”. He does have a clause allowing him to withdraw but he is reluctant to use it and would only do so where the case is “very weak”.
350. IV40 gives the client a choice: he can either terminate the agreement or carry on. However, if he does carry on then unless the award is 20% more than the offer the client is billed £800/day for the tribunal appearance. Our understanding was that IV40 also takes the originally agreed percentage fee on top.
351. CM15 was the only interviewee to provide the client with an unqualified right to decline settlement advice. He had never had a client do so. He recognised that many other businesses use a withdrawal clause. In his opinion:

*...they don't care about the best settlement they only care about the quickest. If they can't get the quickest settlement possible they dump the client.*

### Shifting Clients from Damage-based contingency fees to Hourly Rates

352. Six practitioners indicated they would continue representing the client but on an hourly paid basis. They differed on how to deal with the work done prior to this shift from damage-based contingency fee to hourly fee: half would charge by the hour for all the work done to date; one was unclear on the issue; and two indicated that they would not seek to recoup costs already incurred. The latter interviewees would simply charge an hourly rate from the point that settlement was rejected onwards. IV01 explained that this policy stemmed from a desire to “reach an agreement with the client to keep the work”, although IV21 suggested that there may be circumstances in which his firm would seek to recoup retrospective costs.
353. Clearly a threat of retrospective and/or prospective hourly payment is likely to act as a strong incentive on a client to accept settlement advice; particularly where, as practitioners often acknowledged, those clients had only been able to afford to claim on the basis of a damage-based contingency fee. We do not know the extent to which this incentive explains the very low rate of rejection of settlement advice by clients but some interviewees suggested that because of termination and payment clauses, clients normally just accepted their advice.

### Other approaches

354. It should be noted that there are many options as to what can be done when settlement advice is rejected. Some organisations are believed to offer second opinions. Another approach is to increase the percentage fee charged on any subsequent settlement. CM06 had built protection against clients rejecting settlement advice into his sliding scale of charges. He charged 15% for cases settled before the ET1; 20% for those settled after the ET1; and 35% for cases going to a full hearing. Where a client rejects his settlement advice and then goes on to lose or get a lower amount, he will charge a percentage of the original settlement figure but he will use the point of case completion as the indicator of the level of percentage to charge. In his words:

*For example if a settlement offer of £5,000 was made and at that point the fee was 20%, if the client went to tribunal and did not get as much or lost he would be charged at 35% of £5,000.*

355. He stated that he had started doing this recently because people had rejected his advice and then gone on to get less at tribunal. If, however, the client gained more at tribunal then he would still charge 35% of the higher amount. Perhaps importantly, a losing client under this version of ‘no win no fee’ agreement also faces a large bill; although the adviser will presumably struggle to enforce it against impecunious former clients.

356. CM23's approach echoes this latter part of CM06's approach: he terminates his contingency agreement and simply charges 20% of the offered settlement figure, irrespective of what then happens. IV60 indicated he worked on the same basis:

*[T]he agreement...allow[s] me to charge a percentage of what the client could have got if my advice was followed.*

357. Another approach was to charge the client after rejection of settlement advice where the client failed to later obtain a particular amount (often 20%) over the advised settlement figure. In such circumstances the charge incurred was generally by the hour, although one firm would take a percentage of the amount the claimant eventually received (presumably meaning that nil recovery would yield nil fees). It appeared (although some of the data is unclear) that the majority of firms would withdraw from the agreement, meaning that in order to avoid incurring costs clients would have to achieve the required increase whilst representing themselves (or instruct another representative at cost). This also provides a strong incentive for claimants to accept settlement advice.

358. Further, whilst the majority of respondents indicated that the client would not become liable for any charge until the case result was determined, one interviewee would charge the client at the point where advice was rejected and then reimburse him should he obtain the required increase.

359. The 'increase-dependent' approach to contingency case charging has the benefit of there being some post facto assessment of the reasonableness of the client's rejection of the settlement offer; although this will depend heavily on the extent to which the client is able to, or their adviser is motivated and able to, get a higher settlement. One further approach was to continue on a damage-based contingency fee but to add in extra fixed charges for, for example, tribunal hearings (one respondent quoted £800 a day for the tribunal appearance: IV40).

### **Variations by firm type in charging/termination practice**

360. Our analysis of this qualitative data suggests some differences in the approaches of claims consultants and solicitors to this problem. Solicitors were somewhat more likely to terminate the agreement; to continue but on an hourly rate basis; and to charge the client by the hour for work to date. Claims consultants were more likely to continue on a damage-based contingency fee basis or to charge the client nothing and terminate the agreement. Larger firms were also more likely to terminate their contingency agreement upon client rejection of

settlement advice. It was generally small firm practitioners who were prepared to continue on a damage-based contingency fee basis or continue on an hourly paid basis. Similarly, practitioners from tiny firms were far more likely to indicate that they do not charge contingency clients when settlement advice is rejected.

361. Contingency practitioners using the arrangements in less than 25% of their cases were more likely than those using them in over 50% of their cases to terminate the agreement where a client rejects settlement advice. Regular users of damage-based contingency fees were much more likely to continue with the damage-based contingency fee; whereas no infrequent users would do this. Perhaps where a business largely relies on contingency income it becomes more important in such situations to keep the work and attempt to recover from it or they are more likely to see the risk that a client rejects their advice as part of the risk they manage and charge for in the original percentage fee. Similarly, they may see reputational benefits in being seen as unequivocally on their client's side and not acting in their own interests.

## Summary

362. Evidence from theoretical economics and empirical work on contingency fees in other contexts suggests that damage-based contingency fees may lead to undersettlement when compared with hourly fee cases. Other evidence on employment cases and the findings from our practitioner survey tend to suggest that this may indeed be a risk posed by DBCFs. Practitioners tend to agree that whilst DBCFs would not impinge on their own approach to settlement where they are operating under a DBCF, other practitioners would be tempted to settle rather than go to a hearing. Evidence from practitioners on the time taken to reach settlement and the likely levels of compensation are more equivocal. It is an area which needs to be scrutinised further.<sup>118</sup>

363. It always needs to be acknowledged in this context that some pressure towards settle has healthy impacts: reducing the time taken to resolve cases; reducing the costs of those cases;

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<sup>118</sup> This is something which may be addressed as part of ongoing work being recommended to the Ministry of Justice in the light of merging SETA data from BERR.

and perhaps leading to more proportionate settlement. In other words, there is potential for some balanced pressure to settle to be in the broader public interest.

364. Interestingly, given the structural incentives towards settlement, and the potential for practitioners' interests to conflict, most practitioners indicated very robust contractual approaches to clients who rejected their settlement advice. Such settlement clauses raise some difficult issues. Whilst the need to use such clauses rare in practice, the potential impact of these clauses on clients' decision-making processes is likely to be dramatic. One might have hoped that professional expertise would be sufficient protection for practitioners wishing to persuade clients of the wisdom of settlement. DBCFs raise interesting problems partly because clients do not bear the additional cost of rejecting settlement; although they do bear the risk of losing everything. Practitioners have a legitimate interest in ensuring the settlement decision is properly structured; but there must be a question-mark over the lengths to which these clauses go to 'persuade' clients of the need to settle. This must be particularly so given professional conduct rules for solicitors which indicate clearly that settlement advice should not be shaped by their own interest in getting paid.

365. Prima facie, these contractual clauses raise conflict of interest issues as well as issues around essential fairness. A proper and informed debate needs to be had on the correct balance to be struck around settlement clauses. To that end we are conducting a further research project looking at client experiences of operating under different funding arrangements which we would expect to report on in early 2009.

## 11. DBCF impact on the quality of case management

366. Aside from concerns about conflicts of interest, we collected a range of responses from participants suggesting that DBCFs impacted on case management, the overwhelming majority of which considered the impact to be negative. The most common suggestion was that DBCFs lead to provision of a lesser quality service. This was predominantly suggested by respondent practitioners.

### A negative impact?

#### Lower Quality Service

367. Roughly one in six interviewees suggested that DBCF clients are disadvantaged by service of a lower standard. CM16, a user of damage-based contingency fees, commented that:

*Clients get a lower standard of service with contingency fees. This is because they are seen as second class citizens; fee paying work takes priority and the practitioner fits in contingency work around that.*

368. Another contingency practitioner stated that clients using the arrangements must be told that less time will be spent on their files than on those of hourly paying clients. These respondents explicitly acknowledged that if you paid by the hour you got a better service.

369. CM17 stated that the representative would try and save time in order to achieve target recovery and suggested that this could result in, for example, “making a quick phone call instead of writing the detailed letter that is required”.

370. Two participants suggested that lower quality service results from contingency practitioners taking on large numbers of cases. IV07 commented that:

*No win no fee gives the impression of a churning factory as opposed to a tailored service to the client's requirements.*

371. IV116 suggested that, in extreme cases, contingency practitioners may, “abuse the system and try and not disclose documents”.

372. Respondents commenting on the oppositions' lower quality of service tended to indicate that their opponents were less well prepared or left preparation to the last minute. More specific problems included:

- 372.1. “witness statements, pleadings and evidence will not be completed as thoroughly” (IV90);
- 372.2. the opponent making inappropriate use of standard form documents or conducting disclosure “on a shoestring” (IV111);
- 372.3. taking longer to respond;
- 372.4. not complying with case management directions; or,
- 372.5. more generally betraying a “stack it high sell it cheap” approach (IV272).

373. The latter type of comments, in particular, alluded to a relationship between damage-based contingency fees and high volume practises, resulting in poorer quality service. Similarly, some interviewees linked the alleged reduction in service quality to a desire to minimise the costs taken out of the contingency percentage.

### **More aggressive and unethical opponents**

374. Six respondents suggested that opponents using DBCFs were more aggressive. IV60 accused such representatives of causing “as much trouble as possible” and CM21 commented that:

*Unscrupulous representatives can take advantage of contingency fees. They may over-egg the case and cook the evidence; they will dishonestly advise the claimant as to what evidence to give.*

375. IV271 commented that contingency opponents are often “ridiculously aggressive” at the commencement of a claim in an attempt to scare the respondent into settlement.

376. Two interviewees suggested that contingency representatives attempt to inflate claim value in order to increase their fee, which makes settlement negotiations more difficult. One of these participants commented that the opposition will use the threat of continuing with the case to try and secure a higher amount (contrary to the weight of evidence which tends to suggest the opposite).

### **Non-financial remedies**

377. Two interviewees suggested that damage-based contingency fees obstruct the possibility of the claimant gaining a non-financial remedy. IV292 commented that:

*Firms do not give any thought to the possibility of non-financial settlement when drafting contingency fee agreements. What is a percentage of re-deployment or re-engagement? Nothing. These options may be better but the solicitor will not want to accept them.*

378. IV96 gave a case example where a non-financial settlement was clearly the best result for all:

*For example, one case with an ex-police officer bringing a claim for disability discrimination after he failed medicals for depression. The potential outcome of an employment tribunal hearing was a maximum financial reward; the potential financial reward was £15,000. However, a compromise was struck which included the possibility of re-applying to the police force. This was the claimant's ambition, and so this outcome plus a reduced financial package was better for him than going to an employment tribunal and getting a purely financial result. These compromises are obstructed when a money outcome is the be all and end all of a case.*

379. It does appear that damage-based contingency fees may not encourage such outcomes. However, IV77 (in a different context) noted that their agreement did cover non-financial remedies:

*If the tribunal orders a re-engagement then the firm will take a percentage of 3 months salary.*

380. Clearly then, in some circumstances at least, it is possible to employ damage-based contingency fees in respect of non-financial benefits.<sup>119</sup>

### **A positive impact?**

381. Some interviewees considered DBCFs as beneficial to case management, although they were in the minority.

### **Efficiency**

382. Around one in twenty interviewees considered that damage-based contingency fees increase practitioner efficiency. Some of these suggested that when working on an hourly rate there was an incentive for the lawyer to take longer because doing so results in higher fees, whereas damage-based contingency fees encourage working as quickly as possible. IV202 countered criticism of damage-based contingency fees with the idea that corner cutting

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<sup>119</sup> See, also, K. Underwood (2001) *The real no win, no fee case*, *Litigation Funding*, 12 (Mar) 6,8, 6

is inhibited by DBCFs because it makes a lawyer more likely to lose or get a poor settlement and so a lower payment.

383. Related to this, some noted that damage-based contingency fees forced the practitioner to assess case merits at a very early stage to avoid proceeding with risky cases. Arguably, the same incentive does not exist in hourly paid arrangements; practitioners may take time looking into merits, all the while charging for their time.<sup>120</sup> Some respondents discussing efficiency thought that without damage-based contingency fees far more claimants would end up representing themselves. If they are right, damage-based contingency fees may actually have some advantages to respondents and the Tribunal Service; if they did not exist then the resulting longer cases would mean higher fees. However, there is also the likelihood that many claimants simply would not bring cases.

### **Higher Quality Service**

384. In comparison with the numerous practitioners who suggested that DBCFs lead to reduced quality service, a few interviewees suggested the inverse. The majority of these related the increase in service quality to the representative's interest in the compensation; the practitioner works harder because it is in his interests to do everything possible to increase compensation. IV188 suggested that without DBCFs clients would have to rely on publicly funded organisations which would not give the same level of service as a lawyer.

### **Summary**

385. There appears to be a reasonable number of practitioners who consider that representatives using DBCFs provide reduced quality service. However, without further investigation it is not possible to determine if these allegations are opinion or fact. The fact that concerns have been raised, however, points to a need for further research.

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<sup>120</sup> See Helland and Tabarrok cited note 74.

## 12. Marketing

386. Another issue which is sometimes raised in relation to ‘no win no fee’ arrangements is an alleged link with aggressive advertising techniques. Conditional fees for personal injury cases are widely advertised on the television and have led to accusations of ‘ambulance chasing’. This criticism is sometimes applied to damage-based contingency fees.

387. Historically, there has been a problem with mail-shooting of employment tribunal applicants<sup>121</sup> which prompted the Government to stop publishing the Public Register.<sup>122</sup> Some recent evidence, however, suggests that cold-calling is not a problem particularly associated with damage-based contingency fees.<sup>123</sup>

388. Our study asks practitioners about how they advertise and aims to draw conclusions on whether damage-based contingency fee representatives engage in more aggressive techniques. As well as exploring general patterns of marketing/advertising undertaken by employment lawyers and adviser, we are able to analyse the figures to establish whether there were particular patterns of advertising attributable to particular firm sizes, team sizes, and client mix. We are also able to look at it by use of damage-based contingency fees. The results are interesting and largely contrary to the popular picture.

### **How do firms advertise?**

389. We looked at how firms advertise and sought to analyse this by firm size, type and their propensity to use damage-based contingency fees. Table 23 shows the results by mix of work as this was the factor that appeared most likely to affect marketing approach. Those that show significantly different differences in distribution between respondent, claimant and

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<sup>121</sup> Hammersley and Johnson (2004) cited note 6, p.14

<sup>122</sup> IDS, ‘*Say goodbye to the Register of tribunal applications*’ IDS Brief 763

<sup>123</sup> Hammersley *et al* (2007) cited note 6, p.15

‘mixed’ firms are in bold although it is worth noting that for each type of marketing the differences were near significant.<sup>124</sup>

**Table 23: Marketing by mix of work**

|   | Mainly<br>Respondent<br>Work | Mainly<br>mixed | Claimant  | All       |
|---|------------------------------|-----------------|-----------|-----------|
|   | %                            | %               | %         | %         |
| Do you get clients through referrals from clients?                          | 86                           | 98              | 100       | 92        |
| <b>Do you have a website?</b>   | <b>84</b>                    | <b>90</b>       | <b>81</b> | <b>85</b> |
| Do you get clients through referrals from lawyers/advice agencies?          | 81                           | 92              | 84        | 84        |
| <b>Do you advertise via leaflets?</b>                                       | <b>65</b>                    | <b>62</b>       | <b>39</b> | <b>60</b> |
| Do you get clients in any other way?  | 58                           | 60              | 52        | 58        |
| <b>Do you directly mail named individuals with information on services?</b> | <b>56</b>                    | <b>42</b>       | <b>29</b> | <b>48</b> |
| Do you advertise in any other printed media?                                | 45                           | 58              | 42        | 48        |
| <b>Do you advertise in telephone directories?</b>                           | <b>36</b>                    | <b>60</b>       | <b>68</b> | <b>48</b> |
| <b>Do you get walk-ins?</b>   | <b>25</b>                    | <b>56</b>       | <b>58</b> | <b>39</b> |
| <b>Do you use any other types of online advertising?</b>                    | <b>15</b>                    | <b>26</b>       | <b>32</b> | <b>21</b> |
| Do you advertise on radio?  | 4                            | 8               | 3         | 5         |
| Do you advertise on TV?   | 2                            |                 | 3         | 2         |
|   | 110                          | 50              | 31        | 191       |

390. The main differences appear to be between mainly claimant firms and those that are mixed or do more respondent work. Leafleting and direct mailing, the *bête noire* of critics of claimant lawyers, is more prevalent in respondent firms who appear to use it to contact former and existing clients. The only approach of claimant lawyers which might conceivably

<sup>124</sup> That is the Chi-square result  $p < .1$  for each variable suggesting that there was a less than 1 in 10 chance that the differences in distribution were caused by chance. Referrals from clients,  $p = .090$ ; referrals from lawyers/advice agencies,  $p = .056$ ; walk-ins,  $p = .002$ ; advertise in printed media,  $p = .053$ ; have a website,  $p = .012$ ; use of other online advertising,  $p = .027$ ; direct mail,  $p = .000$ ; leaflets,  $p = .000$ ; other,  $p = .052$

fit with an aggressive, advertising model of claimant lawyering is the greater use of online advertising by claimant only firms.

391. The same analysis is shown for looking at significant patterns apparently related to damage-based contingency fee use (Table 24). These results show that firms using damage-based contingency fees are:

391.1. More likely to take clients from ‘walk-ins’;

391.2. More likely to advertise in telephone directories (particularly where they do less than 25% damage-based contingency fee work);

391.3. Less likely to have a website where they do more than 50% damage-based contingency fees; and,

391.4. More likely to use other forms of internet advertising to advertise their services.

392. Because it is possible that damage-based contingency fee providers wary of a reputation for sharp marketing practice may have given self-serving answers, the results need to be treated with some caution. Nevertheless, this is not evidence of damage-based contingency fee providers having advertising/marketing practices which aggressively seek to target individuals, or of such practices engaging in mass marketing through leafleting or other forms of advertising, save through the traditional route of telephone directories.

**Table 24: Marketing analysed by use of damage-based contingency fees**

|  | No use | Up to 25% use of damage-based contingency fees | More than 50% use of damage-based contingency fees | All |
|--|--------|--|--|-----|
| Do you get walk-ins?   | 31     | 56   | 52   | 39  |
| Do you advertise in telephone directories?                           | 38     | 74   | 52   | 48  |
| Do you have a website?   | 83     | 93   | 76   | 85  |
| Do you use any other types of online advertising?                    | 15     | 37   | 24   | 21  |
| Do you directly mail named individuals with information on services? | 56     | 42   | 14   | 48  |
| Do you advertise via leaflets?                                       | 65     | 58   | 38   | 60  |
| N  | 127    | 43   | 21   | 191 |

393. What is interesting is to take a closer look at those that do engage in more direct forms of advertising. Table 25 looks at significant patterns based on firm size.

**Table 25: Marketing conducted by firm size**

|  | Tiny | Small | Medium | Large | All |
|--|------|-------|--------|-------|-----|
|  | %    | %     | %      | %     | %   |
| Do you have a website?   | 52   | 77    | 93     | 95    | 85  |
| Do you advertise via leaflets?                                       | 4    | 50    | 69     | 79    | 60  |
| Do you directly mail named individuals with information on services? | 15   | 19    | 48     | 69    | 48  |
| Do you get walk-ins?   | 11   | 35    | 67     | 31    | 39  |
| N  | 27   | 26    | 54     | 75    | 191 |

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394. The only areas where the distributions for different size firms were significantly different were the extent to which they got clients through walk-ins;<sup>125</sup> those that had websites;<sup>126</sup> those who direct mail named individuals;<sup>127</sup> and those who use leaflets.<sup>128</sup> Whilst walk-ins seemed to be more important to the medium-sized firms, it is the larger firms that appear to place more reliance on direct mailing and leaflets.

395. A similar analysis was conducted for team size. The distributions were significantly different only for walk-ins;<sup>129</sup> whether they advertised on radio;<sup>130</sup> whether they had a website;<sup>131</sup> whether they use any other form of online advertising;<sup>132</sup> mailing named individuals;<sup>133</sup> and using leaflets.<sup>134</sup> Larger and/or medium firms seem more likely to use these methods. These results are shown in Table 26.

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<sup>125</sup> Chi-square, p = .000

<sup>126</sup> Chi-square, p = .000

<sup>127</sup> Chi-square, p = .000

<sup>128</sup> Chi-square, p = .000

<sup>129</sup> Chi-square p = .007

<sup>130</sup> Chi-square p = .017

<sup>131</sup> Chi-square p = .029

<sup>132</sup> Chi-square p = .012

<sup>133</sup> Chi-square p = .012

<sup>134</sup> Chi-square p = .040

Table 26: Marketing by Team Size

|  | Sole Team | Small Team | Medium Team | Large Team |
|--|-----------|------------|-------------|------------|
| Do you get walk-ins?   | 57        | 53         | 35          | 21         |
| Do you advertise on radio?   | 0         | 3          | 15          | 0          |
| Do you have a website?   | 79        | 85         | 93          | 100        |
| Do you use any other types of online advertising?                    | 14        | 18         | 25          | 17         |
| Do you directly mail named individuals with information on services? | 36        | 43         | 58          | 81         |
| Do you advertise via leaflets?                                       | 57        | 58         | 78          | 81         |
|  | 28        | 40         | 40          | 42         |

### Summary on marketing

396. The picture is, thus, an interesting one. Far from the techniques of aggressive advertising being concentrated in the smaller firms with damage-based contingency fee practices to feed, it is the larger firms, those with medium and/or large employment teams and/or those with a greater emphasis on respondent work that use the techniques most commonly associated with aggressive marketing but to contact their and former existing clients.

397. That is not to imply that these respondents are engaged in improper marketing of their practices but it does suggest something of a double standard in the criticisms that are made against small, claimant firms operating under damage-based contingency fees. Firstly, such firms do not seem to be engaging in proactive marketing practices to the same extent as their respectable cousins; secondly, even if they were it might be asked why the practice is acceptable in the context of business clients but not acceptable in a claimant context. One answer might be that respondent solicitors are merely competing for market share and that if claimant solicitors engaged in such practices it, alongside the self-interest in the result engendered by damage-based contingency fees, might encourage them to put forward weak, or even fraudulent, claims. This answer is rather called into question by the relatively low levels of such marketing techniques. It is also debatable as to whether respondent solicitors are simply engaged in a battle for market share: they are also engaged in persuading employers of the merits of defending cases with external representation rather than doing it themselves.

## 13. Unqualified Representation

398. A legal qualification is not required for advisers to represent clients in employment tribunals. This enables claims management consultancies to offer such representation in competition with solicitors firms in a way that cannot be done for litigation. Little is known about the true impact of consultancies on employment representation.

### **Participant opinion on non-qualified representatives**

399. Where respondents did discuss unqualified representatives they were painted in a negative light.

### **Unqualified representation and quality of service**

400. Several respondents suggested that unqualified employment practitioners provide a lower quality service. CM15 suggested that many employment law consultants “don’t even have a degree”, and IV124 considered that clients in need of contingency funding have to accept unqualified practice because “beggars can’t be choosers”. IV60 described unqualified representatives as “maniacs” and accused them of making serious, untrue allegations in order to force companies into settlement. IV272, a respondent practitioner, suggested that the quality of work that comes in to him is often “appalling” and blamed this on de-regulation of service provision and the consequent claims management consultants bringing employment claims.

401. Four further participants did not suggest that contingency practice is always unqualified, but did suggest that the lawyers using damage-based contingency fees are, as IV93 put it, “second rate”. These respondents commented that contingency work is usually done by lower calibre (IV128), less experienced (IV81), or less specialised (owing to the prevalence of damage-based contingency fees in High Street firms) (IV75) representatives.

402. Conversely, CM04 commented that solicitors who do not specialise in employment law “have started to dabble in it” and suggested that these practitioners do not have adequate understanding of its complexity. His implication was that claims consultants such as himself, with years of experience in only employment disputes, are in fact better qualified to deal with such disputes than non-specialist solicitors.

### **The qualifications of ‘non-qualified’ representatives**

403. Although we did not specifically ask, some of the 20 claims management consultants that we interviewed provided details of legal qualification held. Two indicated completion of the LPC, one the CPE and one a law degree. Two were non-practising barristers and two were non-practising solicitors. Others indicated extensive experience in employment law, with the majority of these having a human resources background. It should also be remembered that others may have had legal qualifications and simply not disclosed them. Based on our sample, it does not appear that there are many claims consultants who enter the field completely unprepared, although of course it could be that less scrupulous businesses simply did not respond to our request for participation.

### **Summary**

404. Not enough is known about the operation of claims management consultants in employment claims. Clearly some practitioners have their reservations about their operation. Objective assessment of non-qualified practitioners in the legal aid context has suggested that specialisation is the crucial variable: non-qualified specialist practitioners have repeatedly been found to exceed the quality provided by specialist solicitors firms.<sup>135</sup>

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<sup>135</sup> Moorhead et al cited note 102; R. Moorhead et al (2001) *Quality and Cost: Final Report on the Contracting of Civil, Non-Family Advice and Assistance Pilot* (Stationery Office, Norwich); and R. Moorhead and A. Sherr (2003) *An Anatomy of Access: Evaluating Entry, Initial Advice and Signposting using model clients* (LSRC, London).

## 14. Conclusions

405. Damage-based contingency fees (DBCFs) are an important and significantly under-researched aspect of the justice system in England and Wales. They were allowed to develop in employment cases through a gap in the regulatory framework whilst regulators and government concentrated on promoting (and regulating) conditional fees in civil cases. The result is that a significant vehicle for access to justice has developed largely unscrutinised by serious research or policy attention.
406. This failure is all the more surprising given the constant, and somewhat ill-informed, criticism of damage-based contingency fees as an unwelcome Americanisation of our justice system. Similarly, the furore over equal pay cases (with no win no fee lawyers being blamed for a significant impact on local authority budgets) has inflamed the current debates about compensation culture.
407. As a result, this study takes as its focus the use of DBCFs in employment cases. It has aimed to:
- 407.1. To provide data from practitioners on the extent to which they use damage-based contingency fees in employment cases;
  - 407.2. To provide data from practitioners on the nature of the agreements they use;
  - 407.3. To understand the types of cases in which damage-based contingency fees are (or are not) used;
  - 407.4. To consider the pros- and cons- of using damage-based contingency fees from the perspective of practitioners;
  - 407.5. To consider any broader issues practitioners believe damage-based contingency fees raise in practice; and,
  - 407.6. To analyse this and pre-existing data in considering the big issues surrounding DBCFs: do they provide access to justice; do they do so in the public interest; and to what extent are consumers of DBCFs interests properly protected under such agreements.

## Methods

408. The project was based on conducting short structured telephone interviews with practitioners conducting employment cases. We interviewed solicitors and non-solicitor providers of employment advice. Sampling is discussed above (para 25 onwards). We also conducted some original analysis of data on employment tribunal applicants (SETA data) and examined existing literature.
409. The response rate for solicitors was 57%, a very respectable figure, but we are likely to have a bias towards those who *do* have some experience of damage-based contingency fees in our sample. We do not claim, therefore, that this sample is necessarily representative of all employment firms, but it does represent a wide and significant range of practice within the employment advice sector. Response rates were much lower for Claims Management Consultants (the response rate was as poor as 16%).
410. As far as we are aware, it is the first study of its kind and it contains detailed and valuable information on employment practice generally and DBCF practice in particular. It is important also to acknowledge that survey data has limitations. Whilst we had high response rates amongst solicitors and our reading of the data suggests practitioners generally discussed their approaches with candour, there are limits. Practitioners may not always be able to describe accurately what they do and may also not wish to reveal particularly aberrant behaviour. We have been mindful of this in conducting our analysis and further address this through triangulating our findings with SETA data and the broader literature on contingency fees where possible.
411. As ever, there is potential for much more to be done both in terms of gaining objective information about costs and outcomes on such cases and in understanding client, practitioner and other stakeholder viewpoints. A programme of work has been recommended to the Ministry of Justice.<sup>136</sup> Moorhead and Cumming are also engaged in a further project on employment tribunal claimant perspectives on funding arrangements funded by the Nuffield Foundation which should be complete early in 2009. Nor does our study directly address all

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<sup>136</sup> Moorhead, Richard, Paul Fenn and Neil Rickman (2008) *Scoping Project on No Win No Fee Agreements in England and Wales* (unpublished, 7<sup>th</sup> October 2008)

the issues associated with the use of DBCFs in equal pay cases. This is an area where the multi-party nature of the claims and the apparent fact that the majority of claims appear to remain unresolved mean we would be warier about applying our general findings to the specific dynamics of equal pay cases without further research.

### **Data on participants**

412. Claims Management Consultants generally worked in small organisations whereas the reverse was often true for the solicitors we interviewed. It was clear that those we interviewed were generally highly specialised: three quarters spent 90% or more of their fee earning time doing employment work.

413. Solicitors were more likely to concentrate on respondent work than Claims Management Consultants who tended to concentrate mainly on claimants, but even so they indicated they did significant volumes of work for respondents. As firm size increases, there is a noticeable trend upwards in the proportion of firms doing mainly respondent work.

### **Is access to justice for claimants a concern?**

414. Concerns about access to justice are commonly reflected in concerns about the extent to which claimants are represented in employment tribunal hearings. Other research has shown that claimants are less likely than respondents to have nominated a representative; and are considerably less likely to get the help of a solicitor or to be represented at a full tribunal hearing.<sup>137</sup>

415. We were able to look at imbalances in advice and representation in a different way by comparing specialist legal resources devoted to claimants and respondents in our samples. In our sample, the amount of resources we can estimate as being spent on representing defendants outweighs that spent on claimants by roughly three times. This suggests a larger differential in support for claimants and defendants than bare indicators of whether or not someone has assistance or is represented.

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<sup>137</sup> Hayward et al cited note 30.

### **Prevalence and use of DBCFs**

416. Most of the practitioners we surveyed did not use DBCFs (127 respondents (66%) said they did not). Only 11% of those we interviewed used them in more than 50% of their cases. Firms that are smaller and concentrate on claimant work appear more likely to do damage-based contingency fee work, although the very smallest firms and employment teams were not more likely to use DBCFs than their slightly larger counterparts.

### **How long have firms been doing damage-based contingency fee work?**

417. Damage-based contingency fees are not generally a new phenomenon. One respondent indicated that his firm had been using them for 20 years and over half of those who responded had been using them for over five years.

### **DBCFs for defendants?**

418. Although it is technically possible to devise damage-based contingency fees for respondents, those we spoke to only used them with claimants.

### **Why do firms not offer damage-based contingency fees?**

419. The predominant reason for not using damage-based contingency fees appears to be the lack of any need to do so on a commercial basis: the nature of their client base, the normal approach to funding respondent work and concerns about profitability and riskiness of damage-based contingency fee cases were the reasons most often given by interviewees. However, there was also a strong underlying sense that lawyers ought, in a normative sense, to be paid on the basis of the time they put into a case.

420. It is clear from this analysis that opportunity cost is likely to be a major driver behind firms' decisions to take on DBCFs. Where firms have a steady supply of privately paying or other funded work, there is less need for them to use DBCFs. This partly explains why DBCFs were more common in smaller firms. Interestingly, where small firms did not provide damage-based contingency fees they were more likely than bigger firms to mention cash flow, conflict of interest, insufficiency of profit, client relationship issues, and reputation/image as reasons for not doing damage-based contingency fees. This may suggest that because damage-based contingency fees are more common in smaller firms, economic pressures may render ethical dilemmas more acute.

### **How are contingency fees calculated**

421. 57 (89%) of those who did contingency fee work charged a percentage of compensation in such cases. 4 (6%) charged a conditional fee-style arrangement.
422. In terms of setting the percentage rate 42 (74%) indicated they did not have a set rate but charged within a band. Many however had a normal rate, which they varied in more or less exceptional circumstances. The rate could drop as low as 5-10% but most respondents indicated a lower band of around 25 or 30% and an upper limit of between 40 and 50%. The average (mean) fee was 31% with 33% being the most common (modal) fee.
423. Interestingly, firm size, client mix and the proportion of a firm's work done on a DBCF did not generally appear to impact on the rate charged.

### **Where the percentage fee varies, what factors cause it to vary?**

424. The most commonly cited factors influencing the percentage at which a fee was set were case duration; level of compensation; and prospects of success.

### **Are contingency fee percentages exploitative of clients?**

425. Interview data is not the ideal means of exploring this issue, although asking about specific cases is likely to be more accurate than asking about general practices. As a result, we asked DBCF practitioners for costs information from the last contingency fee case they completed and non-DBCF practitioners were asked to indicate their normal hourly rates for similar cases. From this data it is possible to calculate notional hourly rates for the DBCF cases and compare them with their normal hourly rates.
426. The data, which needs to be treated with caution, suggests that DBCF cases were not generally more profitable than equivalent hourly rate cases. In fact, levels of profitability looked very similar. The fact that these assessments take no account of the risk that cases would be lost is a further reason for thinking that DBCFs are not likely to be more profitable than hourly fees.<sup>138</sup> Furthermore, published data on costs in Employment Tribunal cases

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<sup>138</sup> There is also the risk that lawyers paid on an hourly basis will not be paid by their client.

suggests that no win no fee agreement cases cost applicants similar or less than those paying win or lose.<sup>139</sup>

427. Interestingly, for those firms that did not take cases on DBCFs, there did appear to be some potential for greater profits if they *had* used DBCFs: on average, given the compensation paid, the level of fee on a damage-based contingency fee would have been considerably higher than the actual hourly fee. However, these firms either perceived such cases as too risky; or saw reputational and/or ethical problems in taking DBCFs for ‘high-end’ clients.

428. At the very least then, this evidence does not support the view that where DBCFs are used they are generally more expensive than hourly rate cases, or that across the range of cases the charges generally exceed the effort put in. Indeed this evidence suggests that, comparatively speaking, DBCFs are less profitable than hourly fee cases. This view was supported by some but not all interviewed practitioners, but particularly those with experience of DBCFs. Whilst we would not suggest that this is conclusive, and we recommend further work is done in relation to, for example, the SETA datasets, and multi-party cases, we find no evidence of overcharging based on the level of percentage set.

### **Are DBCFs as simple as they appear? Deductions and how they are charged**

429. There are, nevertheless, other areas of consumer protection in relation to DBCFs on which we think the evidence is less comforting; in particular, the claim that DBCFs are simple and easily understood. The idea that DBCFs are simple is based on a model where a client knows that they will be charged a fixed percentage of anything they win and nothing if they lose. Is it an accurate model?

### **Calculating the percentage fee: a percentage of what?**

430. Our first issue is the basis on which any percentage is calculated. Deductions can be made from claims awarded or received. In particular, a claimant’s damages may be reduced

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<sup>139</sup> Hayward et al cited 17, Table 4.23. Further analysis would need to be conducted to establish the robustness of these findings.

because of welfare benefit deductions (where cases are dealt with by the Tribunal) so that the amount received is less than the amount awarded. This begs the question: how do such deductions impact on the fee taken? Similarly, disbursements may be incurred: is a percentage fee taken in addition to such disbursements or does the adviser meet those out of their fee? Finally, should a percentage fee include or exclude VAT?

### **Deductions**

431. In terms of the extent to which lawyers calculate their fee as a percentage of compensation agreed or awarded (the pre-deduction figure) or as a percentage of the compensation actually paid to the client (the lower post-deduction figure), practice appears to be split roughly down the middle: half of interviewees charge pre-deduction and half post-. Deductions in employment tribunal cases were said to be relatively rare.

### **VAT**

432. Treatment of VAT was similarly split. It should be noted that adding VAT on a 33% fee adds a further 6% to the costs deducted from a client's damages. About half of respondents added VAT to their percentage fee and half did not. The position is in stark contrast to how respondents reported dealing with hourly rates, suggesting that a significant proportion of practitioners see the desirability of quoting fees inclusive of VAT for damage-based contingency fees.<sup>140</sup> Thus, whilst the adding on of VAT to damage-based contingency fee percentages may be confusing to consumers and run counter to their expectations, practice is better than the position for hourly rates more generally where *not including VAT* in the quoted rate is common practice.

### **Charging for disbursements**

433. The majority of practitioners 51 (84% of valid responses) indicated they always or sometimes charged disbursements *in addition* to the percentage fee. A common practice was that when disbursements were incurred they would be charged for whether or not a client won their case. Only 10 (16%) indicated they did not charge for them separately (i.e. they would meet disbursement costs out of the adviser's percentage). Disbursements in employment tribunal cases were said to be relatively rare.

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<sup>140</sup> 47 (98%) reported that they would add VAT onto an hourly rate.

### **Hidden extras and the consumer interest**

434. What the above sections reveal are a range of practices in terms of charging the client a) whether or not they win and b) over and above any agreed percentage fee. There is a significant likelihood that these approaches violate a lay understanding of what is meant by a no win no fee agreement: to consumers they may constitute 'hidden extras'.
435. It seems to us there are two possible ways of interpreting this data.
436. Firstly, that such terms are legitimate attempts by private practice to define DBCF agreements on terms which are economic and properly balance the risks between lawyer and client. It is worth emphasising that practitioners tended to point to the rarity with which damages were deducted and/or disbursements charged. The economic point is not apparently well supported by evidence that it is those firms with higher levels of DBCF that are less likely to charge these extras charges.
437. Alternatively, these charges are dubious attempts to shift some of the risks of an apparently simple relationship onto unwitting consumers. The rarity of disbursements and deductions might support an argument that these are parts of the risk that practitioners should bear within their more general acceptance of the risk of a case.
438. The fact that practice on these areas is split suggests a lack of professional consensus on the matter. A crucial element in both positions is the extent to which consumers understand and have chosen arrangements whereby the lawyer charges extras win or lose. We have no evidence from this project on what clients actually understood under their agreements. This evidence is now being collected in a subsequent project.

### **Are all barristers always operating within Bar guidance?**

439. Bar Council guidance for barristers states that they cannot use damage-based contingency fees.<sup>141</sup> We received some interview evidence that some barristers may be accepting such fees.

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<sup>141</sup> <http://www.barcouncil.org.uk/about/instructingabarrister/fees/>

**Practitioner attitude to DBCFs**

440. All interviewees were asked what they considered to be the pros and cons in using DBCFs. Practitioners using the arrangements were also asked whether they preferred to charge on a DBCF basis or by the hour. The results indicate general dissatisfaction with DBCFs as funding arrangements. 74% preferred to use hourly rates where they could; 11% preferred DBCFs and only 13% preferred a mixture of both. Six of the seven practitioners who preferred to use DBCFs were claims management consultants.

441. The main practitioner problems with DBCFs were the risk associated with such cases; poorer profitability; cash flow problems; reputational impacts (being perceived as ambulance chasers, or being seen as 'part of the problem' where they had a respondent client base to protect). The creation of conflicts of interest; spurious claims; a negative impact on case management; and the attitude of clients were also raised by smaller numbers of interviewees.

442. Despite the extensive range of DBCF problems suggested by participants, advantages were also put forward. The main ones were the capacity of DBCFs to generate extra business; the potential for greater profitability (practitioners seemed split on this issue); and some reputational benefits through 'putting their money where their mouth was', and being able to take on some worthy cases which they might otherwise turn down.

**Practitioner opinions on client attitude in DBCF cases**

443. Roughly one in seven practitioners complained about DBCF clients' attitudes towards their cases. Just over half of these respondents explicitly related the problem to the fact that such clients are not incurring costs, unlike hourly paying clients.

**DBCFs access to justice and 'explosions' in claims**

444. It is reasonably clear that, for those without legal expenses insurance, and who are not members of a Trade Union, DBCFs provide an alternative method of funding employment litigation. For those unable to afford to pay privately for legal representation and unable to gain access to free assistance and/or representation, DBCFs may present the only practicable

alternative to self-representation.<sup>142</sup> In spite of this, an issue which excites much debate is the extent to which DBCFs increase access to justice or have led to an explosion of unwarranted claims.

445. These two views stem from the same underlying phenomenon: an alleged relationship between DBCFs and the number of employment tribunal claims brought; but they also involve a value judgement about the quality (merits) of the cases brought. In other words, for the 'access to justice case' to be made out one needs to establish an increase in claims numbers attributable to DBCFs without an associated reduction in the quality of claims. For the 'explosion' argument to be made out one needs to establish (dramatic) increases in the number of claims attributable to DBCFs and an associated reduction in the quality of cases brought.

### **DBCFs and trends in employment tribunal cases**

446. DBCFs' impact on case numbers is uncertain. If they had a general impact on claim numbers we would expect to see a significant increase in general claims over this period and in latter years in particular. Any increases have been significant but relatively modest and irregular over the 7 year period (over that period the cumulative increase varies between 0 and 20%). More importantly, existing (but somewhat out of date) evidence on the prevalence of DBCFs in employment tribunal cases does not suggest that levels of DBCF funded claims are high: in 2003 only an estimated 11% of claims were funded by DBCF.<sup>143</sup> This is not consistent with DBCFs fuelling a substantial upward trend in underlying claims.

447. There is potential for DBCFs to have contributed to the dramatic increase in claims in sex discrimination and equal pay. For this to be true, the proportion of cases brought using DBCFs would need to be dramatically higher in these areas than others. Our survey data on this is equivocal, although anecdotally the evidence is quite strong in equal pay cases (where group claims may make DBCFs more economic for claimant firms).

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<sup>142</sup> The Legal Services Commission funds limited advice and assistance but not generally representation in employment cases. Local authorities may also fund some assistance and/or representation but levels of funding around the country are generally assumed to be patchy.

<sup>143</sup> Hayward et al cited note 49

448. It is also important to emphasise that large numbers of such cases are brought by Trade Unions and not by firms operating under NWNF agreements, although there are allegations that DBCF lawyers forced Trade Unions towards this position.

449. There are also other plausible explanations for the growth in claims, in particular changes in employment legislation, large public sector initiatives in relation to job evaluation and the exposure of large scale discriminatory practices in relation to pay.

### **Access to justice? The quality arguments and evidence**

450. The evidence then is consistent with DBCFs having had a perhaps modest upward impact on general claim numbers with a more dramatic impact in equal pay (and possibly discrimination) cases. What of the quality arguments?

451. Theoretical economics and empirical evidence tends to support the view that, because a NWNF practitioner has to invest their own time, and possibly other costs, in a case, they are going to be careful about the cases they take on. Thus in theory DBCFs should improve the quality of cases that are brought, because practitioners carefully select cases with good prospects of success.<sup>144</sup> Alternatively, it is possible that these incentives operate to restrict access to justice: practitioners are overly cautious, cherry-picking only the very best cases, or are confined by the economics of the situation to reject meritorious but low value cases which would not be profitable. The latter has already been identified as a potential problem in relation to employment cases.<sup>145</sup>

452. We collected evidence on these issues in a number of ways.

453. Our analysis of SETA data on employment tribunal claims (Table 17) suggests that the proportion of cases which a claimant with legal assistance loses in employment tribunals is in the region of 20-25%. DBCFs do not appear to give rise to higher failure rates than other forms of funding (at least once cases have been issued in employment tribunals). If this is correct, and if outcome is taken as an indicator of case quality, contingency fees neither

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<sup>144</sup> Helland, Eric and Alexander Tabarrok (2003), *Contingency Fees, Settlement Delay and Low-Quality Litigation: Empirical Evidence from Two Datasets*, 19 Journal of Law, Economics, and Organization 517 -521; Clermont & Currivan cited note 74; Dana & Spier cited note 74; Kritzer HM cited note 46.

<sup>145</sup> Hammersley *et al* (2007) cited note 6, p.21 ; Johnson and Hammersley (2005) cited note 5, p.28

improve nor weaken the quality of cases brought. It also suggests that practitioners are not unnecessarily risk averse in bringing contingency fee cases.

454. This view on quality is reinforced by a number of other pieces of evidence.

455. We asked practitioners what proportion of cases they considered for damage-based contingency fees but then declined. The mean figure for the proportion of cases considered for DBCFs but then declined was 44% and half of respondents reported turning away 50% or more of potential DBCF cases. Even for those practitioners heavily dependent on DBCFs, the results were not consistent with the view that DBCFs generally give rise to them taking on cases irresponsibly.

456. Similarly, in rejecting cases, heavy reliance is placed on prospects of success and likely level of compensation. The thresholds employed plainly exclude large numbers of employment cases as uneconomic.

457. The above data is consistent with practitioners assessing cases on their merits and economic return before taking a claim on a DBCF basis. Nevertheless our survey did provide opportunities for the issue of spurious claims to be discussed. Around one in ten of those with relevant experience suggested spurious claims as an issue.

458. The situation is much more complex in equal pay cases but even here, the situation does not appear to be one in which DBCFs have led to a decrease in the quality (legal merits) of claims brought. Whilst the law affords employment claimants individual rights, it is difficult to criticise DBCFs which fund legitimate claims on access to justice grounds. This suggests, without being conclusive,<sup>146</sup> that even in equal pay cases increases in tribunal claims are consistent with improved access to justice not an unwarranted increase in claims.

459. Rather, DBCFs have exposed a critical tension between individual and collective resolution of employment rights which local authorities are struggling to meet. Other arguments against DBCFs in equal pay cases centre on consumer protection (such as

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<sup>146</sup> A particular issue which is not resolved by this argument is whether trade union members who brought cases under DBCFs would have been better off if they had relied on trade union representation.

exploitative charging, inadequate advice on alternative funding and conflicts of interest on settlement, see para. 461 onwards).

### **Imperfections in access to justice through DBCFs**

460. That said, DBCFs are not a panacea to access to justice problems. Clearly, lower value claims are less likely to be brought under DBCFs and it is claimants in this group in particular who are likely to struggle to afford representation (and may also be most likely to struggle with self-representation). There is also considerable variability in the risk assessment practices of advisers: this depends not only on the characteristics of the case but also the context within which practitioners work. This may mean that access to justice through this mechanism is something of a lottery. For practitioners desperate for the work, incentives to take on weaker cases (even spurious cases) may remain, although our evidence does not suggest that this is a prevalent problem.

### **Conflict of interests**

461. A major criticism directed at DBCFs is that the arrangements pit the lawyer's interests against those of his client. In particular, there is a perceived danger that contingency fee representatives will give settlement advice with their own financial interests in mind, as opposed to seeking to champion the client's best interests. This could lead to under-settlement of cases as representatives seek to recover quickly and avoid going to tribunal or it may lead to practitioners holding out for more when their clients wish to settle. Our study examined practitioner perceptions of the settlement process as well as collecting data on the consequences contingency claimants face should they reject their representative's settlement advice.

462. There is reasonably consistent evidence that DBCF cases are more likely settle without a tribunal hearing (with the exception that DBCF practitioners do not think they themselves are more likely settle DBCF cases before hearing). There is also some evidence that cases may settle for less and sooner than non-DBCF cases but this is more equivocal.

463. Qualitative evidence tends to support the concern that DBCFs may lead to greater under settlement. There is also some evidence of respondent practitioners adopting particular tactics with opponents when they know or suspect they are on DBCFs by stringing cases out or encouraging early, poor settlement.

## **What happens when the claimant rejects the DBCF practitioner's advice to settle?**

464. As we have noted, with a DBCF the representative's fees are inextricably linked to the financial outcome of a case, and because of this many practitioners view the arrangements as impacting on settlement practices. Such impact points to a shift in control over settlement decisions away from clients and towards their representatives. As is evident from the discussion on conflicts of interest and the quantitative settlement data, some of our interviewees were plainly sensitive to this re-alignment. Settlement clauses in DBCF agreements are an important part of the legal framework underlining an alignment that protects the lawyer's position. They largely seek to bind the client to accepting their lawyer's advice on settlement.

465. The use of such clauses is interesting and difficult. There are a number of relevant ethical rules but in particular Solicitors Conduct Rule 3.01(2)(b) states there is a conflict of interests if:

*(b) your duty to act in the best interests of any client in relation to a matter conflicts, or there is a significant risk that it may conflict, with your own interests in relation to that or a related matter.*

466. Guidance on the Rule states:

*You must always be careful to ensure that any settlement achieved for a client, or any advice given in a non-contentious matter conducted on a contingency fee basis, is in the client's best interests and not made with a view to your obtaining your fee.<sup>147</sup>*

467. Because of these issues, all contingency practitioners were asked to explain their procedure upon client rejection of settlement advice. It is important to preface this discussion with the observation that, when we asked contingency practitioners if clients had ever rejected settlement advice, around three-quarters of those who answered indicated that it had never happened, suggesting that in practice clients simply agree to settle. Some however indicated this was due to the financial penalties of not-settling provided for under the contingency agreement. One practitioner indicated that the clauses which we discuss below are, "really just there to frighten the clients" (CM21).

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<sup>147</sup> Para 54, *Solicitors' Code of Conduct 2007* Dated 10 March 2007 and commencing on 1 July 2007 <http://www.sra.org.uk/documents/code/solicitors-code-of-conduct-full.pdf>, last downloaded 7<sup>th</sup> October 2008

468. Upon a client rejecting settlement advice, around three in five contingency practitioners indicated they would automatically terminate the contingency agreement. There were a variety of practices as to what happened next: clients could be charged in full on an hourly basis for work done to date; or they might have such charges deferred to the end of the case; more complex arrangements sometimes kicked in where charges would be waived if clients 'beat' previous offers having had the agreement terminated. It is clear that the most likely impact of such clauses is to provide a very strong incentive for the client to accept settlement advice. Clients of these practitioners have a choice between accepting settlement advice and losing their representation. It was also a reasonably common practice, where an agreement was terminated, for the client to incur a significant debt for work done to date, which is likely to further deter the client from rejecting advice.

469. Firms that largely relied on contingency income appeared somewhat less likely to adopt these approaches, suggesting that they have taken an informed view that it becomes more important in such situations to keep the work and attempt to recover from it than to drop the client. They may also be more likely to see the risk that a client rejects their advice as part of the risk they manage and charge for in the original percentage fee. Similarly, they may see reputational benefits in being seen as unequivocally on their client's side and not acting in their own interests.

470. It always needs to be acknowledged in this context that pressure to settle has some healthy impacts: reducing the time taken to resolve cases; reducing the transaction costs of those cases for opponents; and perhaps leading to more proportionate settlement. In other words, there is potential for some balanced pressure to settle to be in the broader public interest. Furthermore, practitioners have a legitimate interest in ensuring that the settlement decision is properly structured; although there must be a question-mark over the lengths to which these clauses can legitimately go in 'persuading' clients of the need to settle. This must be particularly so given professional conduct rules for solicitors which indicate clearly that settlement advice should not be shaped by their own interest in getting paid. Prima facie, these contractual clauses raise conflict of interest issues as well as issues around essential fairness. A proper and informed debate needs to be had on the correct balance to be struck. To assist in that we are conducting a further research project looking at client experiences of operating under different funding arrangements which we would expect to report on in early 2009.

## **DBCF impact on quality and case management**

471. Aside from concerns about conflicts of interest, we collected a range of responses from participants suggesting that DBCFs impacted on case management, the overwhelming majority of which considered the impact to be negative. The most common suggestion was that DBCFs lead to provision of a lesser quality service, predominantly suggested by respondent practitioners. Respondents commenting on the oppositions' lower quality of service tended to indicate that their opponents were less well prepared or left all preparation to the last minute.

472. Some interviewees considered DBCFs as beneficial to case management, although they were in the minority. These suggested that when working on an hourly rate there was an incentive for the lawyer to take longer because doing so results in higher fees, whereas damage-based contingency fees encourage working as quickly as possible.

## **Marketing**

473. Another issue which is sometimes raised in relation to 'no win no fee' arrangements is the alleged propensity of representatives working on this basis to engage in aggressive advertising techniques.

474. Our study asked practitioners about how they advertise and aimed to draw conclusions on whether damage-based contingency fee representatives engage in more aggressive techniques. As well as exploring general patterns of marketing/advertising, we were able to analyse the figures to establish whether there were particular patterns of advertising attributable to particular firm sizes, team sizes, and client mix. We were also able to look at it by use of damage-based contingency fees. We were not able, however, to analyse the content of adverts. The results are interesting and largely contrary to the popular picture.

475. Far from the techniques of aggressive advertising being concentrated in the smaller firms with damage-based contingency fee practices to feed, it is the larger firms, those with medium and/or large employment teams and/or those with a greater emphasis on respondent work that use proactive techniques to secure business from the business community. That is not to imply that these respondents are engaged in improper marketing of their practices but it does suggest a double standard in the criticisms that are made against small, claimant firms operating under damage-based contingency fees. Firstly, such firms do not seem to be engaging in these marketing practices to the same extent as their respectable cousins;

secondly, even if they were, it might be asked why the practice is acceptable in the context of business clients but not acceptable in a claimant context.

476. One answer might be that respondent solicitors are merely competing for market share and that if claimant solicitors engaged in such practices it, alongside the self-interest in the result engendered by damage-based contingency fees, might encourage them to put forward weak, or even fraudulent, claims. This answer is rather called into question by broader evidence on case merit/quality in this report. It is also debatable as to whether respondent solicitors are simply engaged in a battle for market share: they are also engaged in persuading employers of the merits of defending cases with external representation rather than doing it themselves.

### **Unqualified representation**

477. CMCs that represent claimants have been subject to Part 2 of the Compensation Act 2006 and therefore required to be authorised and regulated by the Ministry of Justice since April 2007. Not enough is known about the operation of claims management consultants in employment claims. Our interviews suggest that some solicitors have reservations about their operation. Objective assessment of non-qualified practitioners in the legal aid context has suggested that specialisation is the crucial variable: there non-qualified specialist practitioners have repeatedly been found to exceed the quality provided by specialist solicitors firms.<sup>148</sup> The context here is significantly different. Claims management consultants are competing for business from lay rather than public funders and are often relying on low value work apparently at the margins of profitability.

### **Core Conclusions**

478. This Study provides in-depth data on the use of DBCFs amongst employment practitioners. Our core findings can be summarised as follows.

478.1. Access to justice in employment tribunals has long been subject to criticism. Inequalities in representation are well established. This study further deepens our

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<sup>148</sup> Moorhead et al cited note 102; R. Moorhead et al (2001) *Quality and Cost: Final Report on the Contracting of Civil, Non-Family Advice and Assistance Pilot* (Stationery Office, Norwich); and R. Moorhead and A. Sherr (2003) *An Anatomy of Access: Evaluating Entry, Initial Advice and Signposting using model clients* (LSRC, London).

understanding estimating that within our sample the level of specialist resources devoted to assisting and representing employers is roughly three times of that devoted to employees.

- 478.2. The impact of DBCFs on the overall number of employment claims pursued is uncertain. Increases in employment tribunal applications appear to be more significantly related to other underlying factors such as changes in substantive law.
- 478.3. DBCFs have probably made a modest contribution to access to justice in employment tribunals ensuring that some applicants have access to advice and representation when they would otherwise not.
- 478.4. The situation in equal pay cases is more complex, but the evidence is not consistent with DBCFs giving rise to more, poorer quality claims. DBCFs have, however, exposed significant tensions between individual and collective resolution of complex pay situations and contributed to the considerable financial strain on local authorities posed in correcting pay inequalities.
- 478.5. Any contribution to access to justice is not uniform: lower value claims and claims with high levels of risk or cost associated with them are less likely to be brought.
- 478.6. The claim that DBCFs lead to an increase in spurious or weak claims is not borne out by the weight of evidence currently available.
- 478.7. There is no evidence to support the view that the percentage charged under DBCFs is generally excessive.
- 478.8. There is evidence, however, that approaches to charging DBCFs are not consistent and may be likely to lead to consumer confusion and detriment, particularly as regards VAT, disbursements and recoupment.
- 478.9. DBCFs appear to encourage earlier settlement of cases and, in particular, greater settlement without the need for tribunal hearings. Whilst there are often benefits in earlier settlement, which may ensure settlement is proportionate, it is debatable whether the 'pressure to settle' inherent in DBCFs leads to cases being compromised inappropriately. There is some evidence that it may do so.

- 478.10. The survey did not provide evidence that the marketing practices by DBCF practitioners was generally more aggressive than other practitioners.
- 478.11. Solicitors raised issues about the competence and practices of claims consultants. This would benefit from proper scrutiny.
- 478.12. Firms' contractual arrangements around settlement, and sometimes other, decisions in DBCF cases generally effectively 'handcuff' the client to their lawyer's advice. The consequences of rejecting such advice can be serious both in terms of the impact on their representation and in respect of debts that fall due. Conversely, firms have a legitimate interest in protecting their financial position.
- 478.13. Whether the protections taken are appropriate is open to debate and should in particular be debated by the professions, regulators and consumer groups. Given a solicitors' duty not to place themselves in a conflict situation with their client, the apparent risk that DBCFs *may* give rise to such conflicts and the tendency of such 'handcuff' clauses to reinforce the power of advisers (in situations of potential conflict) requires the scrutiny of such rules to be searching.

-end-

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## Appendix A: Interview Schedule

### Research Into Contingency Fees

NAME of INTERVIEWEE:

Name of Firm:

Date:

Hello, my name is [Rebecca Cumming]. I am ringing up to follow up Richard Moorhead's letter inviting you to participate in some research on employment cases and contingency fees.

Can I check you've read the letter and are happy to participate?

yes – Is now convenient or should I ring at another time, it should take 30 minutes. Great. THANK YOU As stated in the letter your answers will remain anonymous in any future publication

no, You do not have to give any reasons, but it would be useful to us to know why you are reluctant:

## Section One: Introductory Issues

I just need to ask a few basic questions about you and your firm:

*\*\*NB – ensure you have looked at website and established whether it is definitely a solicitors firm*

*\*\*If this is not clear...*

Just to clarify, this is a solicitors firm?

Yes     No

How big is the firm:

partners (*if solicitors firm*) / owners (*if not solicitors firm*)

solicitors

other fee earners

Are you a partner (or owner)?  yes     no

*\*\*NB – partners are always solicitors – tick 5 yes and go to 7*

Are you a solicitor?  yes     no

If not a solicitor, are you:

a trainee solicitor

a qualified member of ILEX

other (specify)

How much of your time do you spend doing employment work? [      ]%

How much of this is contentious work (disputes that might go to a tribunal)?  
[      ]%

How many other colleagues conduct employment work? [      ]

I'm going to ask you about how you get your clients. Do you get any by?

- Referrals from former clients
- Referrals from lawyers/advice agencies
- Walk ins
- TV
- Radio
- Telephone Directories
- Adverts in other printed media
- Online
- Website     Other (please specify)
  
- Direct mailing to named people
- Leaflets
- Other

If Other, please specify:

What percentage of your employment cases proceed to a full hearing?

- %

## Section Two: Funding Arrangements

OK, thanks. Now I'd like to ask some questions about your firm's funding arrangements in employment cases.

Do you do any work funded by

Trade Unions

Legal aid

Does your firm represent claimants, defendants or both?

Claimants

Defendants

Both

If Both – roughly what percentage of your workload is for claimants?

*\*\*NB – answer relevant to questions asked in section 3*

Does your firm offer contingency fee funding in employment cases?

Yes

for claimants, defendants or both?

claimants

defendants

both

No

If No, could you give reasons for this?

*\*\* Go to question 0 page 165*

If it was not possible to use contingency fees, do you think that your firm's employment workload would decrease?

Yes, dramatically

Yes, slightly

No, not really

No, not at all

### Section Three: Use of Contingency Fees

OK thanks. I now want to ask you in more detail about how you use contingency fees.

[If the firm uses contingency fees for defendant and claimant work]

Do you have more experience of using contingency fees in either claimant or defendant work?

[     ] claimant    [     ] defendant    [     ] similar

If similar, choose claimant or defendant alternately

To keep the interview shorter, I would like to concentrate solely on [claimant/defendant] cases.

For how many years has your firm been offering contingency fee funding in employment cases?

[     ] years

In what percentage of your [claimant/defendant] cases would you charge clients on a contingency fee basis? [     ]%

I am going to go through a list of types of employment cases and ask you how suitable you find them for contingency fee agreements

on a scale of 1 to 5, 1 being very suitable and 5 being very unsuitable

[2 = suitable, 3 = fairly suitable, 4 = unsuitable]

| 1                        | 2                        | 3                        | 4                        | 5                        |   |
|--------------------------|--------------------------|--------------------------|--------------------------|--------------------------|---|
| <input type="checkbox"/> | unfair dismissal  |
| <input type="checkbox"/> | unauthorised deduction of wages   |
| <input type="checkbox"/> | breach of contract  |
| <input type="checkbox"/> | redundancy pay  |
| <input type="checkbox"/> | discrimination (sex; race; disability;<br>religious; sexual orientation; age) |
| <input type="checkbox"/> | working time  |
| <input type="checkbox"/> | equal pay   |
| <input type="checkbox"/> | national minimum wage   |
| <input type="checkbox"/> | claims under multiple heads   |

What makes cases particularly suitable or unsuitable?

#### Section Four: Fee calculation

I now want to ask you how you calculate your contingency fees

Is your normal contingency fee for employment cases calculated as a percentage of compensation [received {claimant} or protected {defendant}]

[  ] yes

[  ] no

If no, please explain how the charges work

[Consider carefully whether the next questions can be answered]

Where contingency fee funding is offered, what percentage of compensation normally constitutes the 'fee'?

[  ]%

Is the fee always that percentage, or does it vary?

[     ] Always     [     ] Varies

If it varies, through what range of percentages does it vary?

[     ]% and [     ] %

If it varies, why does it vary

[prompts]

level of likely compensation? [check for details]

likely prospects of success?

likely duration of the case?

nature of the client affect?

Do you charge your client any costs in addition to the percentage fee, for example disbursement costs?

Always    Sometimes    No

If Yes – Could you give details?

On the last contingency fee case you completed, could you tell me:

what level of compensation was paid?  

what the fee paid out of that compensation was?

%

how many chargeable hours did you spend on the case?

hours

what is your normal hourly charge out rate for similar cases?

/hour

Generally, do you prefer to use contingency fees or have clients pay a set hourly rate?

Contingency fee       Hourly rate

Why?

What proportion of cases do you consider for contingency fees but decline?

%

Why do you decline to take those cases on a contingency fee?

Do you have a minimum value a claim must reach before it will be taken on under a contingency fee agreement?

£

No

Do contingency fee agreements make it more or less likely that your firm will go on to represent the client at a final hearing?

More likely     Less likely     No difference

If contingency fees have an effect – Why does it make that difference?

Do contingency fee agreements make you settle any earlier or later?

Earlier     Later     No difference

If contingency fees have an effect – Why does it make that difference?

What happens if a client rejects your advice to settle?

[get example of actual experience?]

Do contingency fee agreements influence the level of compensation you are prepared to accept under settlement?

Yes, I am prepared to accept lower compensation

Yes, I would be more inclined to push for higher compensation

No, it makes no difference

[If settlement behaviour is affected by contingency fees] **Could you explain why you settle [earlier/later] and are inclined to settle for [lower/higher] compensation?**

**Section Five: Opponents**

I now want to ask you if you have experience of your opponents using contingency fees in cases you are taking?

yes       no

Are they acting as claimants, defendants or have you experience of both?

claimant     defendant     both

[If both]

Do you have more experience of opponents as claimants or as defendants?

claimant     defendant     similar

If similar, choose claimant or defendant alternately  
keep list to hand]

To keep the interview shorter, I would like to concentrate solely on  
[claimant/defendant] opponents.

In what percentage of cases is the opposition [claimant/defendant] funded on a contingency fee basis?

%       Don't Know

Do you think that, this impacts on:

a) the likelihood that a case goes to a full hearing

more likely     less likely     not different

b) where cases settle, is settlement likely to take place

earlier     later     no difference

c) is the level of compensation settled for likely to be

higher     lower     no difference

Does it give rise to any other issues?

## Section Six: Pros and Cons of Contingency Fee Agreements

Thanks. I'd like to move on to your opinions on the pros and cons of contingency fees.

In your opinion, what pros and cons do contingency fees offer for practitioners?

From the client's perspective, what are the pros and cons of using a contingency fee agreement?

We welcome any further comments that you may have on this issue:

Thank you very much for your participation. Please do not hesitate to contact us if you require further information. Thank you. Goodbye.

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