Department of Justice

An Roinn Dlí agus Cirt
Männystrie O tha Laa

Parameters for the 2024 review of the personal injury discount rate for Northern Ireland

Responses to consultation

April 2024

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ABI

ABI Response to Northern Ireland Department of Justice – Discount Rate Review

Confidentiality statement

The data and other external information provided in this response is confidential to the ABI and to its members and is not to be circulated outside the Northern Ireland Department of Justice without the prior written consent of the ABI. In particular it should not be released if within the scope of a request for information under the Freedom of Information Act.

Irrespective of the points made above, our position is also that the information contained in this response is provided to the Northern Ireland Department of Justice for the purpose of, and during the course of, formulating policy, such as would fall within the exemptions under the Freedom of Information Act for at least as long as it takes for policy to be implemented, not simply formulated.

Executive summary

- The Personal Injury Discount Rate (PIDR) in Northern Ireland should aim to reflect as best as possible the principle of Full Compensation (not over or under-compensation). The discount rate of minus 1.5% in Northern Ireland is the lowest in the world, which is leading to a significant additional cost to motor and liability insurance customers and the NHS. In addition, Northern Ireland already has higher motor insurance costs than other parts of the UK, due to a combination of factors including higher accident rates and the legal costs involved in a compensation claim. This environment underlines the importance of ensuring the PIDR in Northern Ireland reflects as best as possible the principle of Full Compensation as to over-compensate simply adds to an already high, cost burden.

- The further margin applied in setting the current rate in Northern Ireland skews the PIDR away from the aim of Full Compensation. It is therefore an unnecessary and additional cost to both premium paying business and customers in respect of motor, employers' liability and public liability premiums, and the NHS in respect of clinical negligence claims.

- It is vital that due regard to actual, low risk investment behaviour is taken and such evidence is obtained as part of reviewing the notional portfolio in Northern Ireland. The notional portfolio in Northern Ireland should be revisited and the reliance on equities increased to reflect a moderately cautious, low risk portfolio.

- The requirement that the impact of inflation is to be allowed for by reference to the retail prices index (RPI) should be revisited. The PIDR should be set by reference to the consumer prices index (CPI) instead of RPI and the appropriate amendments to legislation will be required via secondary legislation. Officially, RPI is no longer deemed to be an appropriate index, because of its failure to meet international standards and tendency to overstate inflation. With CPI as the appropriate starting reference point, the Northern Ireland Department of Justice will need to consider whether the rate should be set at CPI itself or CPI plus a percentage. The ABI's considered view is that any percentage uplift on CPI should be smaller than that used by GAD when setting the discount rate for England and Wales in 2019: 0.5% at most. Should the Northern Ireland Department of Justice decide that the correct reference is still RPI, then the reference point should be RPI minus 2% so that equates to a similar outcome to use of CPI.

- When considering economic factors including inflation there should only be a focus on long-term trends, not short-term or temporary changes, given the long-term investment period for the vast majority of claimants.

- Higher taxes and management expenses are associated with more active investment approaches which should

generate higher net returns; however, recipients of personal injury compensation, as low risk investors, should not require active investment approaches. Our view is therefore that the current method of calculation for the PIDR in Northern Ireland already accounts too much for tax and management expenses. The ABI would propose that a rate of 0.5% should be applied, instead of the 0.75% currently in place.

- It is difficult to determine a preference between a single rate or dual rate model in the abstract. We think that either a single rate or a switched dual rate are the only options that should be considered. The stepped dual rate model, a multiple rate model, a different heads of loss approach and the blended model (as defined in the MoJ's recent Call for Evidence on dual/multiple discount rates) should all be dismissed for various reasons.

- An outcome where insurers are having to apply single and dual rates in different jurisdictions within the UK would only serve to build delay and significant cost into the process of settling claims. The Expert Panel in England and Wales will consider in detail the prospects of a dual rate model, and it would be preferable to await this detailed consideration before any decisions on single / dual rates are made. In any event a collective approach should be adopted across all jurisdictions of the UK to considering the complex issue of single / dual rates. Whilst it is accepted that the different legislative processes create difficulty in achieving that outcome, the very significant detrimental impact that different outcomes in different jurisdictions would have on all parties including compensators should be taken into account.

- The Northern Ireland Department of Justice should also refrain from implementing PIDR models that are overly complex, open to interpretation or could lead to opportunities for gaming. For example, in the event of a dual rate model it must not be possible to defeat the purpose of a dual rate by claiming a lump sum settlement for short-term losses up to the switching point, and a PPO for the years after.

- If a dual rate is to be considered in the future in Northern Ireland, this should further remove the need for the application of the further margin, which is already an artificial application of additional prudence that skews the PIDR away from the aim of Full Compensation.

Whether any adjustments to the factors to be taken into account when calculating the discount rate in Northern Ireland would be merited

The make up of the notional portfolios in Northern Ireland

1. It is important to recognise that lump sum settlements for catastrophic injury claims by their very nature require a degree of supposition and measured risk in assuming, amongst other things, investment returns. It is vital therefore that due regard to actual, low risk investment behaviour is taken and such evidence is obtained as part of reviewing the notional portfolio in Northern Ireland.

2. We also do not expect any change in rates to have significant impact on claimants' investment behaviours in Northern Ireland. The previous rate changes did not demonstrate any significant change to the best of our understanding, although as above, there is lack of evidence and analysis of claimant investment behaviours. We would therefore urge the Northern Ireland Department of Justice to commission this, which would ensure that an understanding of claimant investment behaviours informs future reviews of the notional portfolio.

3. The notional portfolio in Northern Ireland is currently as follows:

    - Cash or equivalents – 10%
    - Nominal gilts – 15%
    - Index-linked gilts – 10%
    - UK equities – 7.5%
    - Overseas equities – 12.5%
    - High-yield bonds – 5%
    - Investment-grade credit – 30%

- Property – 5%
- Other – 5%

4. In previous reviews, the ABI argued that the notional portfolio, since adopted by the Northern Ireland Department of Justice, was overly cautious as it placed too little reliance on equities at only 20% of the portfolio. In its 2019 report to the Lord Chancellor on the discount rate in England & Wales, GAD suggested that a moderately cautious, low risk portfolio would contain 32.5% equities, which is the percentage that the Lord Chancellor adopted for the portfolio applied in calculating the discount rate in England and Wales. The ABI still maintains that it would be appropriate and more in line with the principle of Full Compensation for the Northern Ireland Department of Justice to recognise that pursuers will likely invest in more equities over a longer period of time, and as such the notional portfolio should be revisited and the reliance on equities increased. The notional portfolio in Northern Ireland should also be revisited and the reliance on equities increased to reflect a moderately cautious, low risk portfolio.

5. If a dual rate model were to be adopted in Northern Ireland, consideration should be given to what a **representative investment profile in a mixed portfolio of assets** should be, with presumably a more cautious portfolio for the short-term rate(s) and a less risk averse portfolio for the longer term rate(s). The lack of evidence of current claimant investment profiles makes it difficult to predict what these suitable portfolios should look like for the basis of any potential short and long-term rate(s).

The assumed period of investment in Northern Ireland (43 years)

6. 43 years is the average period of loss/life expectancy for a personal injury claim to which the discount rate applies. This is evidenced by a data collection exercise which the ABI carried out to inform its response to the 2019 call for evidence on the discount rate in England and Wales. Based on the data collected and taking the claimant's age at the date of settlement, the ABI applied ONS life expectancies from 2008 (in line with those used in the Ogden tables) and showed that for **<u>all claims</u>** the average life expectancy was 43 years, with some 78% of all claimants having a life expectancy of more than 30 years. A more detailed breakdown for different claim values was as follows:

   - **Claims from £250k-500k:** average life expectancy of 42 years, with 75% of claimants having a life expectancy of more than 30 years
   - **Claims from £500k-1m:** average life expectancy of 43 years, with 80% of claimants having a life expectancy of more than 30 years
   - **Claims from £1m-3m:** average life expectancy of 47 years, with 80% of claimants having a life expectancy of more than 30 years
   - **Claims over £3m:** average life expectancy of 50 years, with 88% of claimants having a life expectancy of more than 30 years

7. Based on this data, we propose that the assumed period of investment in Northern Ireland should remain at 43 years. It is also important to note that this evidence and analysis was accepted by the 2019 report on the discount rate in England and Wales, where GAD noted as follows:

   4.5 The responses to the Call for Evidence suggest that an average duration for personal injury cases is between 40 and 45 years. As such, in my analysis I have assumed a representative claimant invests over a period of 43.

8. It is also important that proper consideration is given to the effect on investments over this time period. In its response to the call for evidence in England and Wales, the ABI noted that the following table from the 2019 GAD report on median asset class return simulations (in excess of CPI) shows the unnecessarily cautious approach taken by GAD:

Table 14: Median asset class return simulations (in excess of CPI)

Median money weighted real return % pa in excess of CPI	5 years	10 years	15 years	20 years	30 years	40 years	50 years
Nominal gilts	-2.8%	-2.2%	-1.9%	-1.5%	-0.9%	-0.4%	-0.1%
Index-linked gilts	-3.3%	-3.2%	-2.7%	-2.2%	-1.3%	-0.8%	-0.4%
Investment grade credit	-0.1%	-0.4%	-0.2%	0.0%	0.4%	0.8%	1.1%
UK equities	2.2%	2.6%	2.8%	2.9%	3.0%	3.0%	3.1%
Overseas equities	2.6%	2.9%	3.0%	3.1%	3.2%	3.3%	3.4%
Cash	-1.2%	-0.9%	-0.6%	-0.4%	0.0%	0.2%	0.4%

9. The explanation for the table is as follows: *"Making regular withdrawals from a fund can have a significant impact on the effective returns achieved – for example, making a significant withdrawal from the fund following an early fall in asset values will hinder an investment manager's ability to recover the fund in subsequent periods. In technical terms – this is essentially the difference between Time-Weighted Rates of Return (which ignore withdrawals from the fund) and Money-Weighted Rates of Return (which are affected by withdrawals and additions to the fund). We are assuming that the assumed claimant included in this analysis has to finance regular withdrawals from the fund in order to meet their needs. As a result, the risk of withdrawals following a period of low returns is a significant risk. As such, references to projected returns in this report allow for the specified assumed withdrawals from the fund and the table…shows the median annualised effective real return achieved on key asset classes that will be modelled. These returns are real (in excess of CPI) and assume that regular withdrawals are made from a fund that is solely invested in a representative broad index for each asset class. For example, if the entire fund were invested in UK equities and used to provide regular CPI-linked damages over a 30 year period then the median effective real return is CPI+3.0% pa. Or equivalently, a PI discount rate of CPI+3.0% pa with an assumed investment strategy of 100% UK equities would result in the median level of over/under-compensation of 0%. Assets with higher returns also have higher risk. As a result, although a claimant would expect to benefit from investing in an asset with a higher expected return they are also increasing the probability of experiencing poor returns and hence incurring poor outcomes".*

10. The underlined section of the above explanation already indicates a measure of prudence in the forecasting. However, if the table from the 2019 GAD report is compared with the following table from the Barclays Equity Gilt Study 2022, it can be demonstrated that, over the long-term, the economic scenario generator applied by GAD does not reflect real-world rates of return:

FIGURE 1. **Real investment returns by asset class (% pa)**

	2021	10 years	20 years	50 years	122 years*
Equities	9.8	4.7	2.9	4.9	4.9
Gilts	-12.6	1.0	2.4	3.0	1.3
Corporate Bonds	-10.0	3.1	2.3		
Index-Linked	-3.1	2.5	3.2		
Cash	-7.0	-2.5	-1.1	0.9	0.6

Note: * Entire sample.
Source: Barclays Research

11. Whilst the table from the 2019 GAD report shows an increase in equity returns of just 7% over the 20 to 50 year period, the Barclays study for the same period shows a (significantly higher) increase of 69%. The ABI has in the past, including in its comments on GAD's PIDR technical memorandum in 2019, encouraged GAD to make reference to wide ranging market studies such as the Barclays study when constructing asset allocations. This would ensure that the economic scenario generator applied by GAD is not over-prudent, as it was in its 2019 report.

The impact of inflation, currently allowed for in Northern Ireland by reference to the Retail Price Index

12. The requirement that the impact of inflation is to be allowed for by reference to the retail prices index (RPI) should be revisited. The PIDR should be set by reference to the consumer prices index (CPI) instead of RPI and the appropriate amendments to legislation will be required via secondary legislation. Officially, RPI is no longer deemed to be an appropriate index, because of its failure to meet international standards and tendency to overstate inflation.

13. With CPI as the appropriate starting reference point, the Northern Ireland Department of Justice will need to consider whether the rate should be set at CPI itself or CPI plus a percentage. The ABI's considered view is that any percentage uplift on CPI should be smaller than that used by GAD when setting the discount rate for England and Wales in 2019: 0.5% at most. The reasons for this are explained below.

14. Should the Northern Ireland Department of Justice decide that the correct reference is still RPI, then the reference point should be RPI minus 2% so that equates to a similar outcome. For the reasons set out below, the preference should in the ABI's view be CPI + 0.5% at most.

CPI instead of RPI

15. Schedule B1 of the Damages Act 1996 states that:

    9(2) The impact of inflation is to be allowed for by reference to, whether indicating an upward or downward trend—
    (a) the retail prices index within the meaning of section 833(2) of the Income and Corporation Taxes Act 1988, or
    (b) some published information relating to costs, earnings or other monetary factors as is, for use instead of the retail prices index, prescribed in regulations made by the Scottish Ministers.

16. In previous reviews of the PIDR in the UK the ABI has supported the use of RPI. This was based on evidence from economists projecting that earnings inflation was expected to come down from its historically high rates and track more closely to RPI in the future. In fact, at present the Annual Survey of Hours & Earnings (ASHE) and Services Producer Price Inflation (SPPI), which are both seen as representing earnings inflation, are tracking well below RPI and CPI, though this is not expected to last beyond 2025.

17. In the terms of reference set out for GAD in the 2019 review of the discount rate in England and Wales, the Lord Chancellor stated that he wanted returns on investments and, by extension, the discount rate expressed relative to CPI. GAD decided that, in the absence of any clear evidence, it was reasonable to make an assumption for damage inflation of CPI + 1% p.a.

18. The Office for National Statistics (ONS) has long opposed using RPI because evidence suggests it likely overstates inflation. In 2013, RPI lost its designation as a national statistic because its formulation failed to meet international standards. In 2018, the ONS published a paper[1] describing RPI as 'a very poor measure of general inflation' for several reasons:

    - The Carli formula, which is used to formulate RPI (but not CPI) increases the growth rate of RPI by around 0.7% when compared with CPI;

[1] Office for National Statistics, 'Shortcomings of the Retail Prices Index as a measure of inflation' (8 March 2018): https://www.ons.gov.uk/economy/inflationandpriceindices/articles/shortcomingsoftheretailpricesindexasameasureofinflation/2018–03-08

- RPI is heavily influenced by house prices and interest rates;
- RPI excludes the richest and poorest households;
- RPI's sample sizes for expenditure data are too small.

19. The UK Statistics Authority (UKSA) has a policy of addressing the shortcomings of RPI in full at the earliest practical time: it proposes to make changes aligning its methods and data sources in line with CPI, which will not occur before 2030. Until then, however, RPI will be considered a 'legacy measure' by professional organisations including the ONS and UKSA. This means that since 2013 the methodology for formulating RPI has not been updated, unlike CPI, so that flaws that resulted in RPI losing its position as a national statistic have become magnified as CPI formulation has improved.

20. CPI was developed much more recently, using careful, international analysis of a significant number of factors affecting modern economies. It was constructed in accordance with a European Council Regulation passed in October 1995 [Council Regulation (EC) No 2494/95 of 23 October 1995 concerning harmonised indices of consumer prices (HICP)] and a subsequent series of Regulations and Guidelines. HICPs for each EU Member State have been developed by the Statistical Offices of the Member States, under the direction of Eurostat, the Statistical Office of the European Community. CPI was launched in January 1996, and the ONS first published UK inflation on a CPI (then called HICP) basis in February 1997 to complement existing indices such as the RPI.

21. The UK Government retains responsibility for setting the objectives of economic policy, including the inflation target. In December 2003, the target measure became CPI. CPI replaced RPI from 2011 as the UK Government's preferred measure of inflation for benefit and tax uprating purposes.

Adjustment applied to CPI

22. Whilst the ABI accepts the use of CPI as the appropriate index, it believes GAD's 2019 assumption for damage inflation of CPI + 1% p.a. is wrong for three reasons.

23. Firstly, in its 2019 report on the discount rate in England and Wales GAD adopted a historic approach when considering inflation. *'In arriving at my view on annual earnings inflation, I have considered long-term empirical evidence dating back to 1970. However, it should be noted that within this long-term time frame, there are periods in which earnings have been higher and also lower, which could produce quite different assumptions – for example, real earnings growth has generally been lower in more recent periods.'* The logic behind this was hard to understand as every other aspect of the calculation was considered by reference to forecasts. Additionally, as the trend showed a lower rate of wage inflation in more recent years, the trend for wage inflation is downward, meaning it will track lower in the future.

24. Secondly, the rate as calculated by GAD placed too much emphasis on short term economic factors. If the same mistake was made at present, claimants would be heavily over-compensated, especially once the current, short-term high rate of inflation returns to a more normal lower rate.

25. Finally, GAD gave too much consideration to how to measure earnings and care costs when setting the total rate. The ABI's view is that once you break the award of damages down into constituent parts you start to run into significant difficulties around which are the appropriate indices to reflect the respective parts.

26. One of GAD's assumptions in its report to the Lord Chancellor in 2019 was that earnings will exceed CPI by 2% per annum, which was one of the factors resulting in its setting of the rate of inflation at CPI + 1%. Earnings and care costs are measured by ASHE and average weekly earnings (AWE), which are currently both below CPI (6.56% and 7.4%, respectively); predictions are that they will not track at CPI + 2% in the medium to long term.

27. A single measure of inflation over all aspects of a case will have a fluctuating correlation over time, i.e. the inflationary aspects related to earnings and other damages. On a broad-brush approach this will work to ensure the right outcome. That measure of inflation should be assessed based on predictions for the future rather than on the historic picture and on that basis CPI + 2% cannot be the correct starting point for earnings.

28. Factoring in changes to the economy since 2019, the ABI's considered view is that the use of forecasts instead of historic

analysis would have indicated the correct appropriate rate of inflation to be CPI + 0.5%, rather than CPI + 1% as adopted by GAD.

Assessment of inflationary pressures

29. In looking at the various PIDR options (single rate, dual/multiple rates and rates for different heads of loss) there are different points that need to be highlighted when addressing inflationary pressures.

30. Single rate: **all inflationary pressures need to be judged over the long-term, ideally 43 years to reflect average periods of loss**. It must be remembered that the Bank of England's goal is to return inflation to 2% annually, which it expects to do in the next few years. Additionally, over the long-term, the Bank's goal is to keep inflation at a 2% trend, even taking aberrations like the present spike into account.

31. Dual/multiple rates: though a short-term rate will be assessed over a shorter term (such as 10 to 15 years), **the Bank's 2% annual inflation rate target will apply to both short and long-term rate setting**. We do not see any basis on which it would ever be appropriate to set a period of less than 5 years for a short-term rate. For any multiple rate where a short-term rate of between 5 and 15 years is applied, the inflationary trend should follow the Bank's 2% target and short-term volatility of inflationary measures is unlikely to be a material factor (although for the reasons discussed in Annex A, we do not support a multiple rate model).

32. It is important that **short-term volatility is put to one side when setting even the short-term rate in any dual rate model**. Just as it would be unfair to defendants to set that rate by reference to higher-than-normal inflation levels at the time of the review, so it would provide an unfairly low base for claimants if one were to factor in the prediction of 2% inflation in or around the end of 2024 (as predicted by a number of economists), with the OBR predicting inflation at or near 0% from mid-2024 to mid-2026.

Issues with current inflation rates

33. It is important that the PIDR (including both short and long-term rates in a dual discount rate model) avoid taking account of temporary inflationary pressures such as those the UK is experiencing at present. The setting of discount rates, whether as a single rate or as short and long-term rates, needs to be based on the predictions of the Bank of England in the longer term, taking into account the Bank's goal of keeping CPI at 2%.

34. As GAD has stated, economic cycles tend to last five to ten years. We are currently in an economic anomaly due to a set of unpredictable events all happening in a short period of time. The current economic situation and resultant inflation numbers need to be treated as outliers if the aim of Full Compensation is to be held to.

35. As of June 2023, CPI is 8.7%. By Q1 2025, the Bank predicts that CPI will be near 1%, and it will be at 0% by Q1 2026. The OBR expects CPI to oscillate around 0% from mid-2024 to mid-2026.[2] The Bank's goal remains getting inflation back to an annual rate of 2%.[3]

36. One reason for the unusually high rate of inflation is that energy prices have spiked over the last year, largely because of the war in Ukraine. The wholesale price of natural gas rose to nearly $10.00 in August 2022, from its 2021 rate of just under $2.00. Whilst the wholesale price has now dropped back to 2021 levels, consumers are yet to see the savings passed on to them – though this is expected to happen from July. Spikes like this could happen again in the future but will be temporary and should be ignored in tracking longer term trends.

37. Wage inflation was unusually high in the second half of 2022, and after a short flattening of growth at the start of

[2] https://obr.uk/forecasts-in-depth/the-economy-forecast/inflation/#CPI
[3] https://www.bankofengland.co.uk/monetary-policy-report/2023/february-2023

2023, we are seeing consistent high wage inflation.[4] An increase in unemployment, brought on by a recession, could have a negative effect on wage growth, but the Bank of England is concerned that persistent wage growth will continue to keep inflation higher than the target.

38. The current, unusual inflation rate spike also has goods inflation outpacing services and wage inflation, recently by more than 2.0%.[5] This is anomalous when compared to long-term trends, but everyone expects rates to revert to the long-term trend. Setting discount rates that factor in current rates would result in awards that do not reflect costs for goods/services over the duration of a claimant's lifetime, especially if that lifetime is predicted to be on average 43 years.

39. The key takeaway from the above is that, like CPI, wage inflation is unusually unstable at present, and **inflationary pressures for setting discount rates (including both short and long-term discount rates in any dual discount rate model) need to focus on longer term predictions in the years to come.**

Summary

40. The PIDR in Northern Ireland will probably be set at a time when inflation rates are still in a state of recovery from their current historical highs. The contemporary numbers and the rates over the recent past at the time will be outliers when compared to long-term rates and predictions.

41. To better ensure the likelihood of meeting the aim of Full Compensation, **it is important that in setting the PIDR in Northern Ireland the focus is not on recent inflationary trends**. This is equally true whether the PIDR in Northern Ireland remains a single rate or whether dual rates are set based on duration.

The standard adjustments made in Northern Ireland for the impact of taxation and the costs of investment advice and management (0.75%)

42. Most properly advised claimants will pay very little tax over the long-term. This is because, over the long-term, investment in various tax wrappers will mitigate income and capital gains tax risks. Given the low levels of risk that are assumed for a claimant, there will also be limited management of the long-term fund and therefore management fees can be kept to a minimum. This is supported by expert evidence we previously commissioned, which shows that:

- Most of those whose personal injury claims are subject to the PIDR are either non or basic rate taxpayers;
- By investing the monies in different tax wrappers; for example, insurance company bonds/collectives and ISAs (where appropriate), income and capital gains tax is greatly mitigated; and
- In some years there is no tax to pay.[6]

43. Even in the short-term, the tax risk is also far more limited for the claimant as they are less likely to face any significant changes in tax policy in the short-term. In any event, far more of any short-term fund is likely to be held in cash assets, requiring lower/no management costs.

44. Overall, higher taxes and management expenses are associated with more active investment approaches which should generate higher net returns; however, recipients of personal injury compensation, as low risk investors, should not require active investment approaches. Our view is therefore that the current method of calculation for the PIDR in Northern Ireland already accounts too much for tax and management expenses. In a financial

[4] https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/bulletins/averageweeklyearningsingreatbritain/june2023

[5] https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/may2023#latest-movements-in-cpi-iflation

[6] MVA report dated May 2017 – Annex C to the ABI's consultation response to *'The Personal Injury Discount Rate [in England and Wales] – How it should be set in the future'*. Our understanding is that the rationale is not changed.

memorandum in 2018, the Scottish Government noted that under the minus 0.75% PIDR in Scotland, *'Awards currently average 120% to 125% even after management costs and tax'*, which indicates significant over-compensation rather than under-compensation.[7] With the minus 1.5% PIDR in Northern Ireland the over-compensation will be even more significant. For the reasons above, were a dual discount rate model to be put in place in Northern Ireland, it would be necessary to ensure that the short-term rate would account less for tax and management expenses than the current single rate models. For a single rate model, the ABI would propose that a rate of 0.5% should be applied in Northern Ireland, instead of the 0.75% currently in place.

The further margin in relation to the rate of return (0.5%)

45. The further margin applied in setting the current rate in Northern Ireland skews the discount rate away from the aim of Full Compensation. It is therefore an unnecessary and additional cost to both premium paying business and customers in respect of motor, employers' liability and public liability premiums, and the NHS in respect of clinical negligence claims.

46. Northern Ireland already has higher motor insurance costs than England and Wales, due to a combination of factors including higher accident rates and the legal costs involved in a compensation claim. This underlines the importance of the PIDR in Northern Ireland aiming to reflect as best as possible the principle of Full Compensation. Removing the further margin in Northern Ireland in relation to the rate of return would make a significant contribution to achieving that aim.

47. The further margin builds in an unnecessary layer of prudence into a calculation which (as we have noted above) already includes an over-prudent notional portfolio. If an over-prudent economic scenario generator is also applied by GAD, this will create many layers of over-prudence in addition to the further margin already factored in.

Whether single or multiple discount rates should apply in Northern Ireland

48. The Ministry of Justice has recently conducted a call for evidence into whether a single or dual rate is more appropriate. We have summarised our comments on each of the different types of dual rate proposed in the call for evidence at **Annex A** of this paper.

49. The ABI considers that a collective approach should be adopted across all jurisdictions of the UK to considering the complex issue of single / dual rates. Whilst it accepts that the different legislative processes create difficulty in achieving that outcome, the very significant detrimental impact that different outcomes in different jurisdictions would have on all parties including compensators should be taken into account.

50. The ABI and its members are concerned that separate consideration in the different jurisdictions of the UK as to whether single or dual rates are appropriate could lead to different outcomes. This would cause significant difficulties for insurers and all parties in implementing the different processes for each jurisdiction. That would undoubtedly cause significant confusion and delays to settlement and drive up the costs of processing claims for insurers – costs which would be met by premium paying customers.

Conditions that should apply to discount rate models

51. Our view is that a stepped dual rate model, a multiple rate model and a different heads of loss approach, as referred to in the MoJ's recent Call for Evidence, would each be impractical, have adverse unintended consequences and should therefore not be pursued in Northern Ireland. In addition, the blended dual rate model (briefly discussed in the MoJ Call for Evidence) would result in significant over-compensation for those in receipt of long-term awards. We therefore do not believe that the blended dual rate model should be pursued in Northern Ireland under any circumstances (we consider the various dual/multiple discount rate models at Annex A).

52. The question is therefore whether the current single rate model or a switched dual rate model, as referred to the in MoJ

[7] Financial Memorandum for the Damages (Investment Returns and Periodical Payments) (Scotland) Bill, paragraph 10

Call for Evidence, would be preferred. **We believe it is very difficult to determine a preference between a single rate or dual rate model in the abstract. Instead, we have set out some conditions that we think need to be applied for both a single or dual rate to be fair, practically implementable and able to command our support. These conditions lead us to conclude that either a single rate or a switched dual rate model are the only options that should be considered.**

53. Conditions that should apply to both single or dual rate models:

   a. The PIDR model should aim to reflect as best as possible the principle of Full Compensation (not over or under-compensation).
   b. Short-term economic factors should not be taken into account.
   c. An appropriate indexation for inflation should be applied based on forecasts rather than historic outcomes.
   d. A further margin is not applied in relation to the rate of return. Any further margin at the end of the calculation serves only to skew the rate(s) away from the aim of Full Compensation. Any further margin is therefore unnecessary and creates a significant additional cost to both premium paying businesses and customers in respect of motor, employers' liability and public liability premiums, and the NHS in respect of clinical negligence claims.

54. Conditions that should apply to a dual rate model:

   a. The model must be simple and not overly complex. Any dual rate model should not be too complex for compensators or claimants to understand (taking into account that claimants will be legally represented and receive appropriate financial advice). It should not be overly complex to allow for adaption of compensator processes, IT changes, training and familiarity with revised Ogden tables.
   b. The model provides a clear basis for settlement and is not open to interpretation. It should provide a degree of certainty on the level of damages that may be awarded.
   c. It should not lead to opportunities for gaming, particularly gaming that might take advantage of cliff-edges between short and long-term rates, which could delay settlements and lead to otherwise avoidable litigation.
   d. The two rates are set by reference to date of losses, with one rate for short-term losses and another for long-term losses.
   e. The switching point is at 10 to 15 years to best reflect economic cycles and real-world investment practice.
   f. The long-term rate properly reflects the returns on long-term investments.
   g. No account is taken of short-term volatility in setting the long-term rate.
   h. The short-term rate is not factored into the rate for losses beyond the switching point.
   i. The long-term rate is set on the basis that it is unlikely to change (accepting that the statutory mechanism requires a review every 5 years).
   j. It is not possible to defeat the purpose of a dual rate model by claiming a lump sum settlement for short-term losses up to the switching point, and a PPO for the years after.

55. The overriding aim should be for a fair and suitable PIDR in Northern Ireland that reflects as closely as possible the aim of Full Compensation. Even minor changes in the discount rate can significantly affect the level of lump sum award and therefore, the prospects of achieving the aim of Full Compensation. However, even in circumstances where a switched dual rate model would in theory best reflect the aim of Full Compensation there may be a case, on balance, for the retention of the single rate model. This would be on the grounds that, given the (i) operational implications of moving to a switched dual rate for both claimants and compensators and (ii) any potentially increased prospects of gaming, the retention of the single rate in Northern Ireland may, overall, be the fairest and most practical solution. The lower number of claims in Northern Ireland compared to England and Wales may in particular make maintaining the existing single rate model more straightforward.

56. In our response to the MoJ's recent Call for Evidence, we also set out very similar conditions that we think need to be applied for both a single or dual rate in England and Wales to be fair, practically implementable and able to command our support. These conditions led us to conclude that either a single rate or a switched dual rate model are also the only options that should be considered.

Association of British Insurers
July 2023

The UK insurance and long-term savings market and the ABI

The Association of British Insurers is the voice of the UK's world-leading insurance and long-term savings industry. A productive and inclusive sector, our industry supports towns and cities across the UK in building back a balanced and innovative economy, employing over 20,000 FTE in Scotland and 5,000 FTE in Northern Ireland in high-skilled, lifelong careers.

The UK insurance and long-term savings industry manages investments of over £1.9 trillion, contributes over £16bn in taxes to the Government and supports communities across the UK by enabling trade, risk-taking, investment and innovation. We are also a global success story, the largest in Europe and the fourth largest in the world.

The ABI represents over 200 member companies, including most household names and specialist providers, giving peace of mind to customers across the UK.

For the purposes of this response, 'insurers' refers to insurance, reinsurance and long-term savings companies.

Annex A: consideration of dual/multiple discount rate models – Summary of views provided by the ABI to the Ministry of Justice Call for Evidence on dual and multiple rates in England and Wales

Switched dual rate model

1. A switched dual rate model (a version of this model is applied in Ontario) differs from the current single rate model in Northern Ireland that it is designed to combine one component that is nearer-term economic conditions (the short-term rate), with a second element that anticipates reversion to a long-term average (the long-term rate). By a switched dual rate model, we mean as set out in the MoJ's Call for Evidence and the 2019 report of the Government Actuary's Department (GAD) regarding the previous discount rate review process in England and Wales. Under the switched dual rate model, if the switching point is 15 years then, a claimant with a 16-year period of loss would have the first 15 years of damages discounted at the short-term rate, and the cashflow in the final (16th) year discounted at the long-term rate.

2. In principle, and subject always to the overriding aim of Full Compensation, the main advantage of a dual rate would be that a lower rate is used in the short-term where expected returns are lower due to a more cautious investment strategy that manages a greater risk of short-term volatility. Then, after the switching point, a higher rate is used in the long-term where expected returns are higher. In the long-term, a less cautious investment strategy is needed to manage a lower risk of volatility which will be smoothed over the longer period. A dual rate could therefore result in fairer outcomes for compensators, and for claimants (for example, in cases of short-term life expectancy).

3. We note that in the 22 years since the dual rate system was introduced in Ontario, the short-term rate has been amended 16 times, but the long-term rate has remained unchanged. It is positive that the long-term rate has remained unchanged given the long-term average for yields on Government bonds in Canada is between 2-3%, and so a steady rate of plus 2.5% has been adopted. However, the short-term rate being amended 16 times in 22 years is not conducive to certainty. If a dual rate system was introduced in Northern Ireland, it would not be desirable for the short-term rate to be amended so frequently. **Certainty is a highly important factor for both compensators and claimants** and so, all other things being equal, we would not expect short-term rates to necessarily change following every or most five-year reviews (and we would expect long-term rates to change even less frequently).

4. While we note the view that a dual rate is more complex and harder for the public to understand than a single rate, this is only a material consideration for claimants as opposed to the public at large. Claimants will also be legally represented and receive appropriate financial advice. **In our submission to the MoJ call for Evidence in England and Wales we stated that the switched dual rate model does not add such a degree of complexity** that it would be too difficult (i) for properly advised claimants to understand or (ii) for compensators to implement and account for in their pricing and reserving strategies. However, given the relatively fewer claims Northern Ireland, there may be less of a need to move from the single rate model. ABI members have indicated that the Ontario model is relatively easy to apply, and that there tends not to be disagreement between claimants and defendants regarding how the calculations are produced. This is critical as any change in the models in Northern Ireland must avoid the PIDR becoming a contentious issue in claims. This would only serve to unnecessarily (i) increase expert costs (including on life expectancy evidence, employment experts and forensic accountancy), (ii) prolong claim lifecycles and (iii) increase judicial workloads. On a practical level, it is important that personal injury quantum assessments remain workable for compensators, without more experts than currently required at unnecessary additional cost.

5. There is a potential **risk of gaming** with a switched dual rate model where claimants might seek to concentrate losses (particularly loss of earnings) in the initial period. Countering this might therefore require increased commissioning and focus on life expectancy and working life expectancy evidence, at additional cost.

6. The notional portfolio in Northern Ireland would also need to be reviewed under a dual rate model. Our view is that a switched dual rate model could have the potential to more accurately reflect real-world investment practice. This is supported by expert evidence we previously commissioned to support the 2019 rate review in England and Wales, which shows that independent financial advisers advise clients on portfolio construction with emphasis on using a diversified portfolio suitable for the level of risk the client wishes to take.

7. In broad terms, these portfolios aim to maximise returns for a given level of risk over a set time horizon. The expert

evidence we previously commissioned shows that, with regard to the current portfolio asset allocation for a cautious/moderately cautious risk investor over the long-term, 'the long-term' is designated as 16 years plus. Clients are advised to take account of the investment time horizon, such that **investors with a longer time horizon (16 years plus) adopt a different strategy to those with a shorter time horizon**.[8] This reflects the rationale for the switched rate model, namely that a lower rate could be used in the short-term where returns are expected to be lower. After the switching point, a higher rate could then be used in the long-term where expected returns are higher.

Stepped dual rate model

8. A stepped dual rate model applies different rates to claims depending on duration. In Jersey, where a stepped rate model has been applied, the discount rate for claims not exceeding 20 years is 0.5%, and for claims exceeding 20 years the discount rate is 1.8%. This means that there are in effect two single rates in force, depending on how long the claimant's future needs are expected to last for.

9. If a stepped dual rate model was introduced in Northern Ireland, it would be more likely to extend or cause additional disputes, delays and costs. If, for example, there is a claim where one medical expert regards the life expectancy as 19 years and another regards the life expectancy as 21 years, suddenly a minor difference in expert opinion would become hugely material for the valuation of the claim. Such a **'cliff edge'** would likely delay settlements and lead to otherwise avoidable litigation. In turn, this would likely impact on the court system and, particularly given the pressures resulting from court backlogs, impact on access to justice.

Blended dual rate model

10. While the MoJ's Call for Evidence did not ask about the blended dual rate model, we think it important to set out our views on this model here as it was considered as part of GAD's 2019 assessment of a potential dual rate for England and Wales.[9] Whilst it is another example of a dual rate model, it **does not reflect actual investment practice** and for that reason is not used elsewhere and, in our view, **should not be given further consideration in Northern Ireland**. Under this model, all damages falling prior to the switching point would be discounted at the short-term discount rate. Any damages beyond the switching point would be discounted at the short-term discount rate for the period up to the switching point, and at the long-term rate thereafter. A claimant with a 16-year period of loss, for example, would have the first 15 years of damages discounted at the short-term rate. Damages in respect of the final (16th) year only would be discounted for 15 years at the short-term rate, and one year at the long-term rate.

11. The model is therefore on the face of it similar to the switched model, in that there is a defined period where the short-term discount rate is applied and a switching point. It does not however then apply the long-term rate in the same way. In a switched rate model, the long-term rate is applied to all damages beyond the switching point. However, the blended model never allows for the long-term rate to apply in full in any year of future loss as it only ever applies after the switching point. Even at, say, year 43 the short-term rate would apply for the first 15 parts (allowing for a switching point at 15 years) and the long-term rate for the 28 parts that fall after the switching point. This does not reflect actual investment practice. When looking to achieve a suitable return for use in the long-term, investors do not invest in a way which is subject to short-term volatility or need to realise assets in the short-term. The effect of the short-term rate should be restricted to meeting the losses for that short-term period, and not applied in the way it is in the blended rate.

12. The only application of a blended rate that we are aware of is when shortly after Ontario adopted a dual rate system, the Ontario Superior Court interpreted the rules setting out the discount rate in a way that resulted in a blended rate. In response to the judgments, the Ontario government redrafted the rules to make it clear that the rates were not to be blended as the courts were doing.

[8] Panells report dated May 2017 – Annex B to the ABI's consultation response to *'The Personal Injury Discount Rate [in England and Wales] – How it should be set in the future'*. Our understanding is that the rationale is not changed.

[9] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/817236/Setting_the_Personal_Injury_Discount_Rate__web_.pdf

13. As with the other dual rate methods, we have analysed the potential impacts on lump sum settlements under the blended model. Our analysis indicates that **the blended model would not be conducive to the overriding aim of Full Compensation and would in fact result in significant over-compensation for those in receipt of long-term awards.** This would run contrary to a reasonable expectation that the rates are exhausted at the end of the period for which they are awarded. For example, with a long-term period of loss (43 years) and a large lump sum award of £10 million, applying a -2% short-term rate and a 1.5% long-term rate, a switching point at 15 years for a switched dual rate results in a lump sum of approximately £7.9 million, whereas a blended rate results in a lump sum of approximately £10.7 million. Similarly, a switching point at 20 years for the switched dual rate results in a lump sum of approximately £8.6 million, whereas the blended rate results in a lump sum of approximately £11.9 million. **This reinforces our view that the blended dual rate model results in significant over-compensation for those in receipt of long-term awards and should not be pursued under any circumstances in Northern Ireland.**

14. Our view is also that the blended model would be (i) unnecessarily and overly complex for compensators or claimants to understand (even taking into account that claimants will be legally represented and receive appropriate financial advice), (ii) too difficult to implement, (iii) provide less clarity on the level of damages that may be awarded and (iv) undermine the basis for negotiations between parties to reach settlements in cases. ABI members have indicated that practical application of the calculation methodology would be very complex, likely require bespoke and costly software investment and/or the involvement of forensic accountants, which would add in a layer of unnecessary expense. As above, on a practical level it is important that personal injury quantum assessments remain workable for ordinary practitioners, without more experts than currently required.

Multiple rate model

15. Hong Kong has a threefold (multiple rate) approach whereby different rates apply to losses for (i) up to a five-year period, (ii) up to a ten-year period and (iii) for a period in excess of ten years. This means that there are in effect three single rates in force, depending on how long the claimant's future needs are expected to last for.

16. It would appear unnecessary to have different rates for such short periods given periods of loss rarely tend to fall into these categories. If a similar multiple rate system was introduced in Northern Ireland, our view is that it would be more likely to extend or cause additional disputes, delays and costs. If, for example, there is a claim where one medical expert regards the life expectancy as 9.8 years and another regards the life expectancy as 10.2 years, suddenly a minor difference in expert opinion would become hugely material for the valuation of the claim. Such 'cliff edges' would likely delay settlements and lead to otherwise avoidable litigation. In turn, this would likely impact on the court system and, particularly given the pressures resulting from court backlogs, impact on access to justice. In this respect, the key disadvantage of a multiple rate model is the same as that for the stepped dual rate model. **A multiple rate model would therefore again be impractical and have adverse unintended consequences.**

17. This is supported by GAD's 2019 report regarding the previous discount rate review process in England and Wales, where the Government Actuary considered that using three rates would not lead to materially superior outcomes or improvements, and that it is reasonable to keep the claims settlement process as simple as possible.

Different heads of loss approach

18. The courts in the Republic of Ireland have set different rates by heads of loss, with the rates set at (i) 1.5% for future pecuniary loss (excluding future care costs) and (ii) 1% for future care costs. In 2020, the Irish Minister for Justice and Equality consulted on the discount rate. She requested views on two issues: should it be up to the judiciary to decide on the appropriate rate on a case-by-case basis, or should the minister be tasked with setting the rate and reviewing it thereafter; and is there a need to update the investment strategy that a plaintiff is assumed to take (currently a very risk averse investment strategy) in determining the discount rate. The Department of Justice in Ireland is still reviewing the responses and no further action has yet been taken.

19. Contrary to some arguments which have been put forward, a different heads of loss approach is not needed to provide greater security for claimants whose awards have a larger care and care management cost element. This is because, in any event, both the PIDR model and rate(s) selected in Northern Ireland should be conducive to the overriding aim of Full

Compensation.

20. The practical effect, if a different heads of loss approach were introduced in Northern Ireland, would be to extend or cause additional disputes, delays and costs. In turn, this would likely impact on the court system and, particularly given the pressures resulting from court backlogs, impact on access to justice. Once you break the award of damages down into constituent parts, you start to run into significant difficulties around which are the appropriate indices to reflect earnings, care, etc. In the Republic of Ireland, where different rates are awarded for different heads of loss, we can already see the pattern for areas of dispute as both sides will argue over how individual heads of loss should be treated.

21. In the Republic of Ireland, care is assessed at a lower discount rate and there have been arguments that as care is "earnings related", other earnings related losses should also have the lower discount rate applied. This would also only lead to further debate as to what the right indices should be to measure care and earnings, giving rise to further questions: for instance, what type of care, what level of earnings? The concept of applying different rates for different heads of loss represents an artificial quest for precision, which in fact leads only to greater uncertainty – by creating more areas of dispute and more areas for disagreement as to the correct rate to be applied. **A different heads of loss approach would therefore again be impractical and have adverse unintended consequences.**

Summary

22. For the reasons we have outlined above, a stepped dual rate model, a multiple rate model and a different heads of loss approach would each be impractical, have adverse unintended consequences and should not be pursued in Northern Ireland. In addition, the blended dual rate model would result in significant over-compensation for those in receipt of long-term awards.

23. We note that the simplicity of the single rate approach provides practical advantages for parties and the courts i.e., it is relatively easy to calculate, provides a degree of certainty on the level of damages that may be awarded and forms a basis for negotiations between parties to reach settlements in cases. **However, we believe it is very difficult to determine a preference between a single rate or a switched dual rate model in the abstract. Instead, we have set out in our response above some conditions that we think need to be applied for both a single or dual rate to be fair, practically implementable and able to command our support.**

Personal Injury Discount Rate

Scottish Government, Justice Directorate

Department for Justice, Northern Ireland

July 2023

Introduction

APIL welcomes the opportunity to respond to this stakeholder consultation examining the range of factors to be taken into account when setting the personal injury discount rate (PIDR). We have a long history of involvement in this this work, campaigning to ensure that the rate is set at the right level to ensure catastrophically injured pursuers receive full compensation.

We recently responded to the Ministry of Justice call for evidence, exploring the option of a dual and multiple rates. Our full response to that consultation can be found here.

The setting of the personal injury discount rate is an emotive one. Whilst insurers will argue about the financial impact any change will have on their shareholders and bottom-line, the setting of the rate has the most significant impact on the injured individual. These are people whose lives have been devastated by negligence. PI awards are compensation, they are not a windfall. Cases where a discount rate is applied will often involve an individual who has suffered a catastrophic injury making them reliant on any award. In the cases with future losses for more moderate injuries that will usually be for shorter duration and/or lower value losses so fine adjustments to the PIDR will not make much difference to the award.

As a general aim when making an award of damages the court is to put the injured party in the same position as they would have been in if the delict had not occurred. Damages in delict therefore aim to restore the pursuer to their pre-incident position. If at any time their compensation in the future does not cover their full losses due to investment risk then we have failed in our ability to give that person the legal compensation they should be afforded under this basic principle of law. If the award in our legal system was a punitive award or a fine imposed where there was a windfall then the balance may shift back to concerns of over compensation but it must not be forgotten when considering the evidence that awards are merely compensation. However, we note that where there is a risk of overcompensation the Court of Appeal in England and Wales in *Swift v Carpenter*[1] said “The principles of law by which this Court are bound can be summarised in two propositions: firstly, that a claimant injured by the fault of another is entitled to fair and reasonable, but not excessive compensation. Secondly, as a corollary of that fundamental principle, in relation to the head of claim with which we are concerned, the award of damages should seek so far as possible to avoid a ‘windfall’ to a claimant, or more realistically to his or her estate … if it were to prove impossible here to award a claimant full compensation without a degree of overcompensation, then it seems to me likely that the principle of fair and reasonable compensation for injury would be thought to take precedence.”

[1] *Swift v Carpenter*[1] [2020] EWCA Civ 1295 at paragraph 205

With that in mind we must stress the importance of ensuring there is minimal investment risk for pursuers and set out our specific comments/responses below.

1. Adjustment factors

Make-up of the notional portfolio

It is crucial that the notional portfolio is reviewed. The reform to the way in which the PIDR is calculated exposed pursuers to both investment and inflation risk. Inflation is much talked about today, but historically it was also something that concerned the court in Wells v Wells[2]. One of the reasons for favouring index-linked gilts (ILGs) was as a means of addressing that. The approach under the Wells v Wells regime was that ILGs was only ever intended to be a proxy for an inflation proof low risk investment. It was not intended to reflect or influence how a pursuer invested their award. They were meant to be a simple means for the courts to calculate the losses that would remove the investment and inflation risk.

We remain deeply concerned about the large cohort of individuals that are likely to be under compensated due to the changes to the calculation. There is too much risk assumed in the current notional portfolio. Having moved away from the framework in Wells v Wells to consider how individuals invest is in our view flawed in principle, unsupported by credible evidence and too complex. Too much emphasis was place during the passage of the Bill's on the issue of over compensation. There was no evidence provided, as far as we are aware, on that being the case, nor on how most claimants invest over the long term.

The current notional portfolio in our view carries far too much risk. In 2015 the MoJ commissioned a report[3] on the discount rate from several experts in this field. They agreed that "Only ILGS/risk free investments can provide any certainty of returns relative to RPI, and a predictable level of return relative to other forms of inflation. They are an optimal fit to the view of the Courts that there can be 'no question about the availability of the money when the investor requires repayment of capital and there being no question of loss due to inflation'[4]. The majority view of that panel was that any truly low risk portfolio would require at least 75% of investments in index-linked gilts, with the remaining 25% invested between UK corporate bonds and global government inflation linked bonds and global equities[5].   We endorse this expert view.

Those affected by catastrophic injury must cope with substantial financial uncertainty for the rest of their lives. These are individuals that will be most dependent on their compensation. They are not ordinary investors; in fact, they are regularly inexperienced investors not wanting to take risks with their money. They are often vulnerable and concerned about their ability to provide for themselves and their family. They usually have little or no other financial security to support them and only invest because they must, to meet their lifelong needs.

As well as considering how pursuers approach investment after injury it is important to put at the centre of these considerations the principle of full compensation. In Wells, Lord Steyn referred to the '100% principle'. A principle to ensure that compensation does what it is required to do by law: return the injured person to the position that they would have been in, but for the wrong committed against them (Lord Blackburn in *Livingstone v Rawyards Coal*,

[2] [2008] EWHC919
[3] The Discount Rate, a report for the Ministry of Justice. Prepared by Paul Cox, Richard Cropper, Ian Gunn and John Pollock. (7 October 2015)
[4] Ibid page 56, paragraph 6.6
[5] Ibid page 103 D.6

1880). The debates in the UK about the setting of the rate focused heavily on overcompensating individuals as we have said, however, the modelling from the Government Actuary Department for England and Wales[6] shows the prevalence of undercompensating. In the absence of the publication of any modelling for Scotland and Northern Ireland we assume a similar level of under compensation, namely that one third of all claimants are under compensated[7]. This is far too high and the adjustment ought to be higher in order to reduce the level of under compensation.

Our member's experience is also that most will leave far in excess of the 10% that is assumed in the notional portfolio in the bank or building society. The notional portfolio assumes 10% cash or equivalents. In addition to that, pursuers often need to spend significant sums of money following the settlement of their claim, eg adapting their home, or purchasing aids and equipment, to make daily living easier. Advice is often given to hold a number of years anticipated expenditure in cash to allow immediate, and unexpected matters to be dealt with. This can mean many of the investments are delayed for several years because of this.

Assumed period of investment

We do not understand the rationale behind the different investment periods in the U.K. From discussion with our members the higher rate in NI (43 years) feels too high particularly when you are focusing on a cohort of individuals many of whom have impaired life expectancy and some of whom may already be over 40. Our member's view is that 30 years seems a more reasonable average projection period based on their experience.

We have not been able to find any data on which this 43 year assumption is made. We have therefore made a freedom of information request to the GAD requesting any materials, information and/ or associated narrative provided to the Government Actuary/ GAD which informed their belief that it was appropriate to assume that a representative pursuer has an investment period of 43 years. And, analysis undertaken by the Government Actuary/ GAD of the above materials and/ or information.

It maybe however, that we do not get a response in the timeframe required to respond to this consultation. We would encourage scrutiny of the evidence on this point.

Cost of taxation and investment advice

It is also crucial that the assumptions made in relation to tax and fees are reviewed as part of this work, if the government is committed to the principle of full and fair compensation. It is vital that these underlying assumptions are correct in order to ensure that the discount rate is set at the right level to avoid under compensation. We would recommend that the GAD's work from 2018 is revisited[8].

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[6] Government Actuary's Department, Setting the Personal Injury Discount Rate. Government Actuary's advice to the Lord Chancellor. 25 June 2019

[7] Even with the Lord Chancellor's 0.5% adjustment to reduce the projected level of under compensation, one third of claimants were expected to be unable to 100% meet their financial losses. See statement by the Rt Hon David Gauke MP, Lord Chancellor, 15 July 2019

[8] Government Actuary's Department, report for Scottish Government 2018

Changes to tax allowances introduced in 2023 for those in Northern Ireland will impact the assumptions made, see appendix A. A basic rate income tax paying claimant will be paying a greater level of tax in future years.

The additional tax bands in Scotland also require extra consideration due to their complexities. Appendix B shows that this along with the proposed tax changes, will both impact a tax paying pursuer in the future.

When compiling APIL's response to the call for evidence from the Economy, Energy and Fair Work Committee[9] we raised concerns about allowance for the impact of taxation and costs of investment advice being too low. We consulted three independent financial advisors in this field who gave a range of fees between 1.5% and 2.5%.

The charges proposed in the 2019 GAD report[10] do not reflect how a pursuer would invest in practice and are significantly lower than those experienced in practice. The Government Actuary Department considered different annual investment management costs ranging from 0.25 per cent to 0.5 per cent[11]. This is based on the client investing statically in low-cost passive funds and includes any VAT payable. Other associated costs of 0.10 – 0.20% are included for transaction and platform fees, however the GAD note that the view of respondents from the initial call for evidence suggested that platform fees alone would be closer to the 0.25% mark. With all of this in mind, GAD's analysis indicates that tax and expenses could be anywhere in the region of 0.60% - 1.70%. They settled on a deduction of 0.75% as they believed it was consistent with the returns analysis they modelled, based on the assumption that there is no active management involved.

Even by the GADs own analysis for expenses, this is a significantly low deduction and does not reflect the expenses associated with a pursuer's investment portfolio in practice. GADs reasoning for using a low level for expenses was that using higher rate would not accurately reflect the return assumptions which are based on a static asset allocation and investment into passive funds. Again, this is not a reflection of how investment portfolios for pursuers are established in practice.

Even if the client had a portfolio which was constructed using passive investment funds, the pursuer would require an investment professional (whether it be a financial adviser or a discretionary fund manager) to set the asset allocation and regularly adjust the portfolio so it does not fall out of kilter with the risk mandate or asset allocation. This would be required even if we were to consider a static asset allocation for the entire investment term as the allocation would naturally move based on market performance. In addition, the pursuers injury related needs are rarely static and adjustments to the portfolio will frequently be required to reflect a change in those needs and the related outgoings.

That said, it is unlikely that a pursuer would hold a portfolio constructed using only passive funds. Whilst passive funds can offer a cheap way to track an investment market, which can add value in times of market growth, there is little protection in a declining market, as the same funds would track the negative performance too. Whilst it would not be a pursuer's intention to achieve a high rate of growth, any individual making an investment would need to achieve a positive return to ensure their damages last their life time in line with the assumptions

[9] Call for evidence: Damages (Return on Investment) Bill – a response from the Association of Personal Injury Lawyers (APIL) – April 2021
[10] Ministry of Justice, Personal Injury discount rate: Exploring the option of a dual/multiple rate; call for evidence – page 2
[11] Ibid para 4.15 page 36

underlying the PIDR. The best way in which to do so is to restrict losses in times of market decline and take advantage of opportunities in times of market growth. To do this they would need to invest in an actively managed portfolio.

To look at what is happening in practice the Forum Of Complex Injury Solicitors obtained data as part of the 2019 MoJ call for evidence on the discount rate, which clearly demonstrated that an over whelming majority, some 64.3%, of the 389 portfolios, incurred investment charges of 1.5% and above (including 6.4% in excess of 2%). In comparison, only a small minority of claimants (4.9%) incurred charges below 1% and only 35.7% of the portfolios incurred charges of 1.5% and below. Furthermore, when looking solely at the 169 portfolios whose value fell below £1.5m, 74% of portfolios incurred charges between 1.5% and 2.0%, only 12.5% incurred lower charges and 13.6% incurred charges of 2% or more[12].

Likewise, in Irwin Mitchell response to the MOJ's 2023 call for evidence, they provided evidence from their Court of Protection team who had analysed investment charges over 953 portfolios collected from 22 providers. This analysis showed average fees of 1.51%. This is a close match to the above 2019 FOCIS data set.

We are also aware that Digby Brown have collated evidence relating to 22 portfolios, arising from Scottish cases, which have been established over the last 4 years. The average fees in respect of investment advice and management charges were 1.76%. In 20 of the cases, 90.9% of the cohort, the charges were over 1.6%. All of the cases involve active management as the needs of each individual client vary, and detailed discussions about risk, and required return are vitally important.

Taken together they are the best body of evidence of the actual investment charges faced by claimants and demonstrate that the current adjustment of 0.75% is around half of what is required before you even factor in the necessary further adjustment for the incidence of tax.

The principal aim of any reasonable financial advice to an injured pursuer is not to generate a greater return but to provide a structured financial plan to limit loss or recover loss where there has been an impact on their investment.

The data clearly suggests that when taken together, the adjustment for the cost of taxation and investment advice ought to be at least 2% and not 0.75%.

Additional margin

Many of the arguments during the passage of the Acts focused around the concern from the governments and insurers that individuals might be over compensated despite there being no credible evidence of that. We are concerned that a significant proportion individuals will be under compensated, and there is evidence of that in the GAD report[13]. Unlike the position for insurers, there are no swings and roundabouts for an individual. If they are one of the individual's that 'loses out' based on the adjustments, the financial impact can be significant and they cannot turn to other claimants who might have been luckier with their investments, nor the families of those who died earlier than expected. 'Losing out' means greater risk

[12] Page 19 FOCIS' response to the MoJ call for evidence on the discount rate 2019. See also Appendix 1 FOCIS data in relation to investment charges.
[13] Government Actuary's Department, Setting the Personal Injury Discount Rate. Government Actuary's advice to the Lord Chancellor. 25 June 2019

must be taken with their money, investing it in riskier assets, placing an additional burden on them.

The Government Actuary acknowledges that they are not currently factoring in the additional mortality risk. All investors and their clients, factor into their financial planning the probability that the individual will outlive their projected life expectancy[14] and then invest according. The mortality data is readily available from the Office of National Statistics. If that is not modelled into the calculations and adjusted for then, we would suggest that there should be an additional contingency applied. This should be looked at.

In England and Wales even with the Lord Chancellor's 0.5% adjustment to reduce the projected level of under compensation, one third of claimants were expected to be unable to 100% meet their financial losses. The financial instability and high inflation that have prevailed since then have in reality, greatly amplified that expected level of under compensation. In absence of the publication of any analysis in Scotland and Northern Ireland to the contrary we assume that this is the case UK wide.

The impact on individual claimants of not getting this right is substantial and ultimately could result it too little money to last their lifetime, shifting the responsibility to the state and failing to meet the fundamental principle of restitution.

Inflation

It is worth noting that the Retail Price Index (RPI) has always been an imperfect measure for the inflation of personal injury damages, primarily because many of the largest aspects of damages are earnings related and others involve items, such as disability related aids and equipment that are not included in the RPI 'basket'.

For personal injury investors who may be awarded damages for their lifetime, inflation creates a 'need' to invest the money rather than a 'desire,' as they must attempt to achieve a return which at least matches inflation simply to preserve the value of their capital.

There is also the added complexity of RPI being dropped as the official national statistic. HM Treasury announced that it would reform RPI by February 2030. RPI will be reformed in line with CPIH (Consumer Price Index including Owners Occupiers' Housing Costs). Since 2010, the annual rate of CPIH inflation has been, on average, one percentage point lower than RPI as currently calculated. The table below published on the actuaries' blog[15] illustrates the issue.

[14] In fact, more than 50% of individuals will outlive the expectation of life (because of the skewed nature of the distribution).
[15] https://actuaries.blog.gov.uk/2021/08/23/measures-of-price-inflation-rpi-cpi-and-cpih/

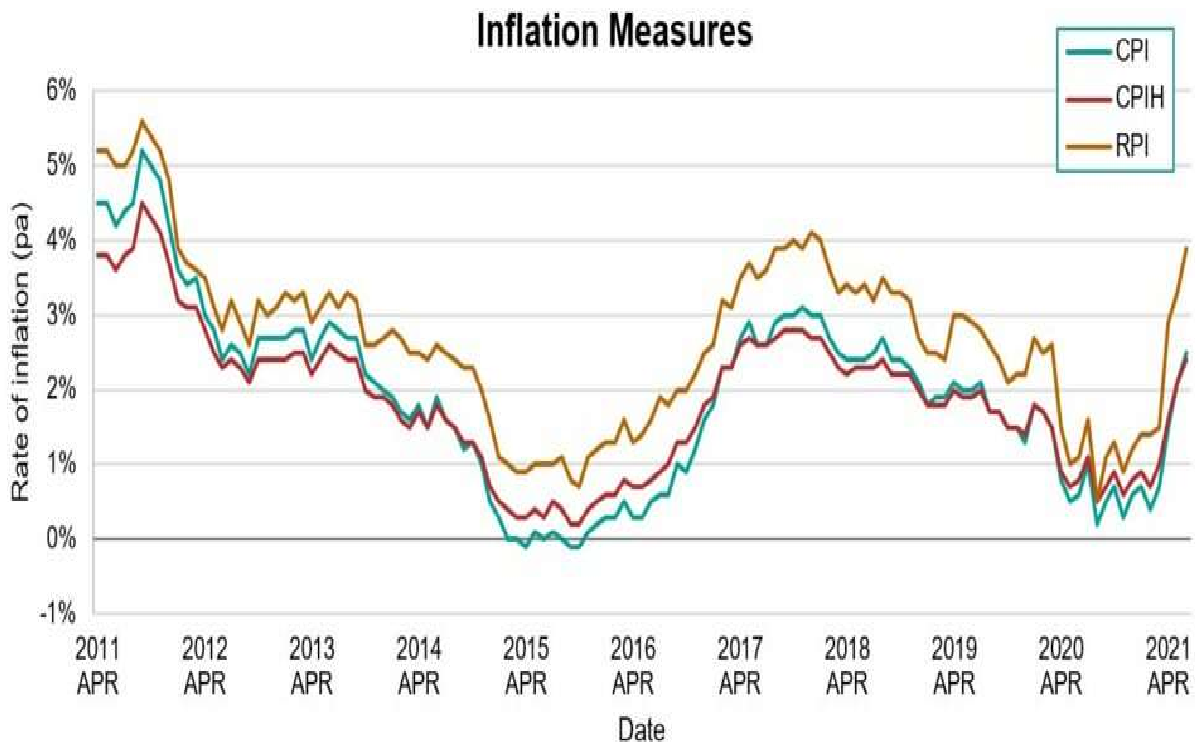

Figure 1, statistics taken from ONS

Figure 1 shows 3 different inflation measures, RPI is consistently higher than both CPI and CPIH but despite expectations that CPIH will be higher than CPI on average, we can see from the past 10 years that this has not consistently been the case[16].

As a result, these proposals are likely to result in a lower rate of inflation.

Inflation operates as a "deduction" from the injured pursuer's gross rate of return. A lower deduction for inflation will result in a higher personal injury discount rate which will, in turn, reduce the amount of damages paid to severely injured people. If it underestimates the inflation those people then experience in the remainder of their lifetime then their compensation is likely to run out early. It is therefore very important this is set at a fair level for the types of losses they will face.

We agree with the GAD's recommendation to the Lord Chancellor that CPI (Consumer Price Index) +1% is, in the round, an appropriate inflationary measure for the discount rate as the relevant losses contain a mixture of items many of which are driven by earnings inflation and/or by medical/technological advancements that cause rises in cost well above CPI.

If there is a move to adopt CPIH given the decision on RPI we would recommend that the same adjustment of +1 be adopted.

[16] https://actuaries.blog.gov.uk/2021/08/23/measures-of-price-inflation-rpi-cpi-and-cpih/

2. Consider whether a single or multiple rate should apply and if a multiple rate is preferred which model?

APIL has significant reservations about moving toward a dual/multiple rate system. Our paper to the MoJ in April 2023 sets out in detail why. In summary, it is our view, based on the modelling below, that it has the potential to erode damages and become extremely complex. We would suggest a more detailed consultation with relevant stakeholders be undertaken.

Setting a dual/multiple rate by duration

In the paper produced by Edward Tomlinson [17] for JPIL[18] he examined the impact of a dual/multiple rate. His analysis showed that, based on the figures in the Government Actuary Department report from 2019[19], where ongoing future loss is more than 18 years the claimant will likely recover significantly lower compensation. The report also showed that a claimant with a smaller settlement would be worse off under a dual rate when compared to a single discount rate. This creates an additional burden on this group of claimants to take greater risk with their money to ensure that it lasts for their lifetime.

The analysis assumed the GAD's 2019 example short term rate of CPI-1.75% and a longer-term rate of CPI+1.5% in its calculation as follows and arrived at the following conclusion:

Male Age, with normal LEx	Single PIDR (-0.25%)	Dual PIDR (-1.75% first 15 years 1.5% thereafter)	Percentage Difference
10	£868,900	£503,195	42.1%
20	£735,600	£465,621	36.7%
30	£608,300	£422,452	30.6%
40	£487,600	£373,532	23.4%
50	£373,000	£318,134	14.7%
60	£269,500	£258,943	3.9%
70	£178,100	£179,959	-1.0%

"As can be seen, under a dual discount rate the percentage difference in the value of a claim can be more than 40% and it is only for those aged 70+, with a normal life expectancy, where a dual discount rate may provide a higher settlement. Under the two PIDRs I have compared, the crossover point is a term of 18 years. Where the ongoing future loss is longer than 18 years, a claimant will receive a smaller settlement under a dual PIDR.

Despite the percentage chance of a claimant being able to meet 100% of need being quoted as similar (66% chance for single PIDR & 70% chance for dual PIDR) there is a **40% difference between the two settlement values**. This is one of the challenges of moving to a dual discount rate. If a claimant has a 66% chance of being able to meet all their need

[17] Edward Tomlinson is a Chartered Financial Planner at IM Asset Management Limited. Edward acts as an expert witness on the structure of claimant's settlements and is predominantly instructed by claimant solicitors. Edward also provides financial advice to claimants whose claims have settled. He has very recently been appointed by the MoJ to the 2023 expert panel to advise the Lord Chancellor.
[18] Journal of Personal Injury Law 2022, Issue 3 – Dual Discount Rate, by Edward Tomlinson
[19] Government Actuary's Department, Setting the Personal Injury Discount Rate. Government Actuary's advice to the Lord Chancellor. 25 June 2019

under a single discount rate, how do they have a 70% chance of being able to meet all their need under a dual discount rate with a 40% smaller settlement?

Knowing that both the single and dual PIDR are both “risk rates” then the claimant, under either discount rate arrangement, is expected to invest their compensation within a risk laden portfolio to be able to meet their ongoing need. If a claimant has a smaller settlement under a dual PIDR, when compared to a single PIDR, they will need to achieve a higher rate of investment return, when compared to a settlement under a single PIDR, to be able to meet their need. To achieve a higher rate of return the claimant under the dual PIDR must take more risk and therefore it is counterintuitive to suggest this claimant has the same or higher chance of meeting need.”[20]

We are not aware of any similar modelling for Scotland or Northern Ireland, but the broad principles are the same. The GAD report[21] suggests if a dual/multiple rate is to be adopted, there should be a higher discount rate for those with longer life expectancy over which their losses are expected to continue. This of course puts additional pressure on this group of pursuers. It requires them to take additional risks with their damages to ensure their compensation meets their needs for their lifetime. A longer life expectancy should not create an expectation of taking more risk nor that a pursuer would achieve higher returns if he did so. The longer period for which they are having to plan exposes them to greater levels of risk of material departures from other assumptions on which the discount rate is set (e.g. tax, inflation, longevity etc). All this would do is create financial benefits for defendants, many of whom are insured and hence much better placed to take and spread long-term risks.

There is also the issue of short-term investment rates being more volatile, and thus there is a significant risk that in a duration-based system those in the short-term rate cohort will have to avoid investing in higher risk investments. Consequently, the assumed portfolio to meet their short-term needs will have to be heavily based on retaining funds in cash. This volatility would be largely driven by inflation, rather than investment return. So, the short-term rate would need to be reviewed every year. We understand that to have been the position adopted in Ontario and in most years that has required an adjustment to their short-term rate[22].

APIL suggests that if a dual rate were to be adopted based on duration, the minimum and maximum points should be 10 and 25 years. In our view at the absolute minimum a short-term rate ought not to be less than 10 years as severe economic cycles can take 8 years or more to resolve. However, it would probably be more favourable to adopt the position from the GAD[23] report in para 3.18 and Figure 5[24] which suggests that “broadly speaking, the returns settle after around 15 to 25 years”.

It is clear that one small change to address a perceived problem for one group of pursuers, impacts on another. Whilst the current single rate is not perfect, if set at an appropriate level, it provides the most stability for pursuers’ and minimises the risk.

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[20] Page 174 Journal of Personal Injury Law, issue 3.

[21] Government Actuary’s Department, Setting the Personal Injury Discount Rate. Government Actuary’s advice to the Lord Chancellor. 25 June 2019

[22] Future pecuniary damage awards | Ontario.ca The table shows an adjustment in 15 out of 23 years.

[23] Ibid

[24] Ibid pages 25 and 26

Setting a dual/multiple rate based on heads of loss

If a dual rate system is to be introduced, APIL would favour the rate based on heads of loss rather than a rate based on duration. However, even then we would favour limiting the change to one head of loss: care and case management, this would align with the approach adopted in the vast majority of Periodical Payment Orders in England and Wales. In our members' experience in pursuing claims on behalf of those with injuries of the upmost severity, care and case management costs account for the most significant proportion of the claim. These pursuers will face regular outgoings to pay for carers, case managers and therapists for their whole life. Those costs are subject to earnings growth and these can be expected to rise at a rate over and above other losses.

Complexity of a dual/multiple rate

There would be considerable practical implications to administering a dual rate. Each item of claim would need to be calculated based on each rate. So, for example, if you are representing an individual who is a paraplegic, they will have a significant schedule of loss. Their claim will often have ten or more heads of future loss. Taking the example of just one of those heads of loss, disability aids, they might have 40 or 50 disability aids listed, some of which are short, medium or longer term use. Some of these will need to be purchased yearly, some purchased at longer intervals such as every 3, 5, 10 or 20 years. If there were two rates based on duration, there would need to be two calculations for each item claimed. This of course would increase further if there were multiple rates. Currently catastrophic injury claim schedules are frequently 50 to 100 pages long with hundreds of individual calculations, so changing the discount model would significantly increase the complexity of these calculations.

These schedules once finalised are shared with the defendant and in most cases a counter schedule will be produced by the defendants' representatives. In large value cases this will be a line-by-line response, especially if a case is getting ready for trial. This will increase the costs being incurred in preparing these schedules significantly, both in preparing the schedule and with arguments over the items claimed. There is also an increased risk of error.

Such a change would almost certainly need for parties to consider using forensic accountants to assist in the drafting of schedules. This, in turn would lead to higher out lays and expenses and increased potential disputes on costs.

We are concerned that, whilst the current rate is not perfect a dual or multiple rate will be no better. There will still be significant groups of pursuers that will be worse off under the reforms.

APIL would welcome the opportunity to discuss these issues further and provide additional information if it is thought that would be useful.

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Appendix A

Tax Rates and Allowances in NI

Northern Ireland follows the same taxation model as England and Wales.

The rates and allowances for the current (2023/24) tax year are as follows:

2023/24 Tax Year:

Tax Allowances:	
Income Tax Personal Allowance	£12,570
Income Tax - Personal Savings Allowance	£1,000 Basic Rate taxpayers, £500 for Higher Rate Tax Payers
Dividend Allowance	£1,000.00
Capital Gains Tax Annual Exemption	£6,000

Income Tax Bands & Rates

Rate	Tax Band	Income tax rate	Dividend tax rate
Starting Rate for Savings	£0 - £5,000	0%	N/A
Basic rate	£0 - £37,700	20%	8.75%
Higher Rate	£37,701 - £125,140	40%	33.75%
Additional Rate	£125,141+	45%	39.35%

The way in which tax is calculated is to combine the income from all sources to determine the individual's marginal rate. The tax after allowances is then applied at the marginal rate. For the current tax year an individual can earn up to £50,270 in income without becoming a higher rate tax payer, and this is now due to be frozen until 2028. However, of this income, a total of £1,000 can be generated from dividends and £1,000 can be generated from savings income without being subject to tax (for a basic rate tax payer).

Capital Gains Tax (CGT)

As with dividend and savings income, the rates of CGT depend on the UK rates and thresholds, with the CGT annual exemption of £6,000 for individuals also applying to the whole of the UK. Therefore, a Scottish taxpayer with both earned income and capital gains will also have to consider both UK and Scottish rates and thresholds.

The rates and allowances which apply are:

Rate	Capital Gains Tax
Basic rate	10% (18% for property)
Higher Rate	20% (28% for property)

Upcoming Tax Changes

The Capital Gains Tax (CGT) annual exemption is being reduced to £3,000 from the 2024/25 tax year. As such any gains realised above these exemptions will be subject to tax at the individual's marginal rate.

The dividend allowance will reduce from £1,000 to £500 from the 2024/25 tax year.

Some personal injury claimants are no longer able to work and may not be in receipt of any earnings income, however some state benefits are taxable. In addition, any ill-health pension benefits may also be taxable, therefore it is difficult to determine the tax drag as tax is a very personal matter.

However, if we consider a claimant who receives £2,000 in dividends from their investment portfolio, £1,000 from any savings they hold and has further income of £15,000, we can investigate how the recent changes in tax rates and allowances would affect their tax position.

The total income in this example would be £18,000 meaning the claimant would be a basic rate tax payer. £12,570 of the further income would be within the allowance, whereas the dividends and savings income would be within the allowances and therefore not subject to tax. The total income tax due would therefore be:

Further Income	-	(£15,000 - £12,570) x 20%	=	£486
Dividend Income	-	(£2,000 - £1,000) x 8.75%	=	£87.50
Savings Income	-	(£1,000 - £1,000) x 20%	=	£0.00
Total	**-**		**=**	**£573.50**

However, the same income would lead to a different tax liability in 2024/25 as illustrated below:

2024/25 tax year:

Further Income	-	(£15,000 - £12,570) x 20%	=	£486
Dividend Income	-	(£2,000 - £500) x 8.75%	=	£131.25
Savings Income	-	(£1,000 - £1,000) x 20%	=	£0.00
Total	**-**		**=**	**£617.25**

The above illustration shows that based on the upcoming changes to the tax allowances, the claimant would be paying a greater level of tax in future years, albeit remaining a basic rate tax payer with the same level of income. In 2024/25 their tax liability would increase by 7.63% compared to the current 2023/24 tax year.

Appendix B

Tax Rates in Scotland

The rates and allowances for the current (2023/24) tax year are as follows:

2023/24 Tax Year:

Tax Allowances:

Income Tax Personal Allowance	£12,570
Income Tax - Personal Savings Allowance	£1,000 Basic Rate taxpayers, £500 for Higher Rate Tax Payers
Dividend Allowance	£1,000.00
Capital Gains Tax Annual Exemption	£6,000

Income Tax Bands and Rates

	Taxable Income	Scottish Income Tax Rate
Starter Rate	£12,571 to £14,732	19%
Basic Rate	£14,733 to £25,688	20%
Intermediate Rate	£25,689 to £43,662	21%
Higher Rate	£43,663 to £125,140	42%
Top Rate	Over £125,140	47%

Dividend Tax

Dividend Tax in Scotland is aligned to the rest of the UK i.e.:

Rate	Tax Band	Dividend tax rate
Starting Rate for Savings	£0 - £5,000	N/A
Basic rate	£0 - £37,700	8.75%
Higher Rate	£37,701 - £150,000	33.75%
Additional Rate	£150,001+	39.35%

However, because of the additional tax bands applied in Scotland, there are some complexities to consider. If the individual has earnings income and dividend income, the earnings income is assessed using the Scottish bands and rates, however the dividends are assessed using UK bands and rates, but taking into account the income that is taxable according to Scottish Rates and Bands.

By way of example, a Scottish taxpayer with earned income of £49,000 and dividend income of £2,000 in 2023/24 will have to work out their tax liability as follows:
Their total income is £51,000, but this is reduced to £38,430 by their personal allowance (£51,000 – £12,570).

This means they have to pay income tax on £36,430 of their earned income (£49,000 – £12,570), according to the Scottish rates and bands – so at 19% on £2,162, at 20% on £10,956, at 21% on £17,974 and at 42% on £5,338.

They also have the £2,000 of dividends, but they must assess this against the UK rates and bands, while also taking into account the income that is taxable according to the Scottish rates and bands. Note that the UK basic rate band is £37,700 – the taxable earned income, subject

to Scottish income tax, has used up £36,430 of this band, leaving £1,270. Whilst the taxpayer is also entitled to the UK dividend allowance of £1,000 for 2023/24, this also uses up the basic rate band, leaving £270 available. Of the remaining £1,000 of taxable dividend, £270 is therefore taxed at the UK basic dividend rate of 8.75%, with the remaining £730 at the higher rate of 33.75%.

Capital Gains Tax (CGT)

As with dividend and savings income, the rates of CGT depend on the UK rates and thresholds, with the CGT annual exemption of £6,000 for individuals also applying to the whole of the UK. Therefore, a Scottish taxpayer with both earned income and capital gains will also have to consider both UK and Scottish rates and thresholds.

The rates and allowances which apply are:

Rate	Capital Gains Tax
Basic rate	10% (18% for property)
Higher Rate	20% (28% for property)

Upcoming Tax Changes

From the 2024/25 tax year. There will be a further reduction to the annual exemption to £3,000. As such any gains realised above these exemptions will be subject to tax at the individual's marginal rate.

From the 2024/25 tax year, the dividend allowance will also reduce from £1,000 to £500.

Some personal injury claimants are no longer able to work and may not be in receipt of any earnings income, however some state benefits are taxable. In addition, any ill-health pension benefits may also be taxable, therefore it is difficult to determine the tax drag as tax is a very personal matter.

However, if we consider a claimant who receives £2,000 in dividends from their investment portfolio, £1,000 from any savings they hold and has further income of £15,000, we can investigate how the recent changes in tax rates and allowances would affect their tax position.

The total income in this example would be £18,000 meaning the claimant would be a basic rate tax payer. £12,570 of the further income would be within the allowance, whereas the dividends and savings income would be within the allowances and therefore not subject to tax. The total income tax due would therefore be:

Further Income	-	(£14,732 - £12,570) x 19%	=	£411
Further Income	-	(£15,000 - £14,732) x 20%	=	£54
Dividend Income	-	(£2,000 - £1,000) x 8.75%	=	£87.50
Savings Income	-	(£1,000 - £1,000) x 20%	=	£0.00
Total	**-**		**=**	**£552.50**

However, the same income would lead to a different tax liability in 2024/25 as illustrated below:

2024/25 tax year:

Further Income	-	(£14,732 - £12,570) x 19%	=	£411
Further Income	-	(£15,000 - £14,732) x 20%	=	£54
Dividend Income	-	(£2,000 - £500) x 8.75%	=	£131.25

Savings Income	-	(£1,000 - £1,000) x 20%	=	£0.00
Total	**-**		**=**	**£596.25**

The above illustration shows that based on the upcoming changes to the tax allowances, the claimant would be paying a greater level of tax in future years, albeit remaining a basic rate tax payer with the same level of income. In 2024/25 their tax liability would increase by 7.9% compared to the current 2023/24 tax year.

<ends>

British Insurance Brokers' Association

Department of Justice
Civil & Family Courts Branch
Northern Ireland Executive
DOJCivilJusticePolicy.Division@justice-ni.gov.uk

11 July 2023

Consultation response: Personal Injury Discount Rate (PIDR)

1. BIBA supports the aim of settlements that are as close as possible to 100% of estimated total future losses - neither under nor over-compensating – so consideration of options to refine the PIDR mechanism are welcome. We believe it is crucial to consider the correct balance between the improved compensation outcomes from an amended PIDR mechanism and the implementation costs of such change that may arise from added complexity in settlement and time taken to do so. Ultimately these processing costs are reflected in the premiums paid by policyholders, directly impacting the affordability of motor and liability insurance.

2. Our members are intermediaries rather than insurers, so we do not provide any evidence on the implementation impacts of dual/multiple rate system or express a preference for a particular mechanism. However, we believe that a dual/multi rate system is likely to increase claims processing costs and time than would exist for a single rate system.

3. Motor insurance is compulsory insurance and essential for the livelihoods of thousands of people. As such, affordability is key and government policy on the personal injury discount rate should be made in this wider context. This is particularly pertinent due to the cost-of-living crisis, which impacts those on lower incomes disproportionately. Equally, employer's liability insurance is also a compulsory insurance required by all businesses which are facing a range of inflationary pressures.

4. The effect of discount rate changes on premiums can be observed in what transpired following the 2017 change for England and Wales from 2.5% to minus 0.75%. Insurers needed to significantly increase reserves for serious injury claims and to substantially increase premiums to reflect the higher awards that they would now have to pay. These increases were seen across motor, employers' liability and public liability insurance. Any changes to the rate mechanism could increase claims costs and, whilst supporting the principle of 100% compensation, it is the view of our Motor and Liability and Accident Committees that it is important to consider the wider context of premium affordability and insurer appetite and capacity for such risks.

5. In respect of the range of factors to be taken into account when calculating the PIDR, we question the need for the further margin of 0.5%. We share the ABI's and FOIL's belief that the margin is not warranted. It skews the discount rate away from the aim of 100% compensation; it is overly cautious, especially when combined with the existing notional portfolio, and is more likely to generate over-compensation in claims. A decision to adopt a dual or multiple rate option, which itself is designed to reduce the risk of over/under compensation, would further weaken the case for a further margin.

6. We would point out that the level of discount rate is one of several environment factors influencing claims settlement costs and, consequently, premium levels, insurer capacity and appetite in Northern Ireland when compared to the rest of the UK.

a. Compensation payments for larger claims are impacted by the lower discount rate. For example, a 40-year-old male with £100K per annum ongoing loss in NI would be 39.2% higher than England and Wales, and 22.5% higher than in Scotland.[1]
b. Smaller claims are impacted by the Green Book guidelines for the assessment of general damages in personal injury cases in NI. These guidelines were updated in 2019 and maintain a higher level of damages in personal injury settlements compared to other jurisdictions in the UK, which is another inflationary factor in the cost of writing insurance in Northern Ireland.
c. The implementation of the new Pre-Action Protocol for Personal Injury & Damage Only Road Traffic Accident claims including Credit Hire in the County Court is a welcome development. However, the benefit of the Protocol will be determined by its application and the absence of any sanctions for non-compliance by either side is a weakness.
d. In November 2021, the Department of Justice proposed an increase in the jurisdiction of the County Court to cases up to the value of £60,000 and an increase in the jurisdiction of the District Judges to £20,000. These are positive changes and should limit the associated legal costs incurred in contrast to the High Court. However, there is no timeline for the implementation of the new jurisdiction.

Contact details

To discuss any of the points raised in this response please contact Beverly Robbins at robbinsb@biba.org.uk

About BIBA

The British Insurance Brokers' Association (BIBA) is the UK's leading general insurance intermediary organisation representing the interests of insurance brokers, intermediaries, and their customers.

BIBA is a non-profit organisation and its membership includes just under 2,000 regulated firms, employing more than 100,000 staff. General insurance brokers contribute 1% of GDP to the UK economy; they arrange 74% of all general insurance with a premium totalling £85.5bn and 93% of all commercial insurance business. Insurance brokers put their customers' interests first, providing advice, access to suitable insurance protection and risk management.

BIBA helps more than 550,000 people a year to access insurance protection through its Find a Broker service, both online and via the telephone.

BIBA is the voice of the sector advising members, the regulators, consumer bodies and other stakeholders on key insurance issues.

[1] Figures provided by Forum of Insurance Lawyers and Harbinson Mulholland

Martin Moore
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30 June 2023

By e-mail only to martin.moore@justice-ni.gov.uk

Dear Martin

I am aware that the Northern Ireland Government has been seeking views in preparation for the next review of the personal injury discount rate (PIDR) for Northern Ireland which is due in July 2024. Although the consultation letter was sent only to a few organisations, I understand that you would welcome input more broadly, so I offer some brief comments below.

Investment portfolio

I welcome the clarity provided by setting out the assumed underlying investment portfolio in the Northern Ireland legislation. In principle I consider the portfolio prescribed for the Northern Ireland (and Scottish) PIDR calculation as more appropriate than that used by the Government Actuary in advising the Lord Chancellor for the England & Wales PIDR review in 2019. However, a portfolio with 35% in what might generically be considered to be risky assets (and 65% if investment grade credit is included) is a long distance away from being a 'low risk' portfolio, as I understand is the legislative intent, even though it is closer to meeting this intention than the 42.5% in the portfolio used for England & Wales.

One starting point for consideration of what might be a reasonably low risk portfolio could be the investment choices made by trustees of defined benefit pension plans, who are required to act as prudent persons, but do not have the same constraints as an individual claimant investing their compensation. In the past it was quite common for pension plans to hold 50% in equities and similar growth assets – some would even hold as much as 70%. However, this was in the days when many of these plans were open to continuing accrual and hence could assume a very long future scheme lifetime and underpinning financial guarantees from an employer. Table 7.2 of the latest edition of the Purple Book published by the Pensions Protection Fund in December 2022 (https://www.ppf.co.uk/purple-book) shows that, for defined benefit schemes in aggregate, the proportion invested in equities had fallen from 60% in 2006 to 19.5% in 2022. However, this is for a broad range of schemes, some of which are open to accrual and for all levels of maturity. More relevant to the PIDR discussion is Table 7.9 of the Purple Book, which shows the asset distribution where the majority of liabilities relate to pensions in

payment. With 75-100% of liabilities in respect of pensions in payment, the proportion of equities falls to about 7%. A very high proportion is held either in bonds or in insurance policies, this latter category reflecting buy-in policies with insurance companies, which are an exact matching asset for the liabilities. It is likely that even the limited exposure to equities is in respect of schemes which operate an LDI (Liability Driven Investment) policy, which, with appropriate gearing, permits a high level of interest rate and inflation hedging, whilst still leaving room for a small percentage in growth assets to achieve additional return.

Thus, even with the much greater flexibility available to pension fund trustees because of being able to spread their risks, use sophisticated products such as LDI and cover multiple cohorts of individuals, equities are not to any significant extent considered to be an appropriate and prudent investment for a portfolio heavily dominated by pensions already in payment. I doubt that insurance companies invest at all in equities in respect of their annuity portfolios, including inflation-linked annuities. In the very much more difficult investment environment facing a claimant with a lump sum award of damages specific to their own individual lifetime, with liabilities strongly affected by inflation, including earnings inflation and care cost inflation, and no additional future income sources, it seems to me to be self-evident that the proportion of equity investment assumed should be very low indeed.

Duration of compensation

In my view the 43 years duration used by Northern Ireland (following England & Wales) is far too long to be representative for personal injury claims. Although there are obviously some very long duration cases, the expectation of life of many seriously injured claimants is brought down substantially by comparison with normal population expectation of life. Clearly this assumption could be informed by an analysis of a wide range of actual cases. I don’t have access to such a database but, on the basis of my experience, would certainly support 30 years, as in the Scottish legislation, as being a more realistic measure than 43 years.

Taxation and investment management expenses

Taxation obviously falls very unevenly on lump sum compensation cases, with very large claims suffering significant taxation and smaller claims suffering little, if any. It should be noted, however, that the previous assumption of very limited impact of tax when setting the discount rate based on index-linked gilts (in respect of which the growth in maturity values from inflation is not taxed) is no longer relevant if investment is assumed to be to a significant extent in corporate bonds and equities. These have much higher income streams and equities are subject to capital gains tax on any increase in value.

Investment advice and management expenses were assumed for your legislation at 0.75%, including the presumably very small allowance for taxation. This does not seem at all realistic, given the need for significant ongoing investment advice and the limitations of investing in retail products, which are clearly much more expensive than the funds in which pension schemes can invest. Such analysis as I have seen on the level of investment management expenses which might be more realistic in practice for a claimant would suggest an adjustment more of the order of 1.25% to 1.5%.

Adjustment for further margin

My understanding is that the adjustment of 0.5 % as a further margin followed the decision of the Lord Chancellor in the review of the PIDR for England & Wales to shift the

probability of adequacy of compensation from 50:50 implicit in the Government Actuary's recommendations to approximately a two-thirds chance of receiving full compensation and a 78% chance of receiving at least 90% compensation. I believe this to have ignored the significant level of uncertainty about the future lifespan of the claimant. The 50% chance of proving adequate stated by the Government Actuary in his report for the Lord Chancellor was a measure of investment uncertainty and assumed that the claimant would live for exactly the expectation of life. Given that expectation of life is average future lifetime, and that more than 50% of individuals will outlive the expectation of life (because of the skewed nature of the distribution), significantly more than 50% of claimants will run out of money, even if they experience reasonable investment returns close to the average. The combined effect of investment uncertainty and lifespan uncertainty is significantly greater than implied, and a margin of much more than 0.5% is needed to achieve anything approaching a two-thirds chance of full compensation. Getting a better handle on this would require the actuary to model investment and survivorship uncertainty in the same model but I would expect the margin required to be over 1.0% to bring the probability of receiving full compensation up to the envisaged level.

Single or multiple discount rates

If a dual or multiple rate system were to be introduced, I would strongly favour a system distinguishing between the discount rates for different heads of damage, rather than differentiating by duration of claim. The clearest differential between the theoretical discount rates arises because of different underlying inflation characteristics of the expenses under different heads of damage. In particular costs of care and case management go up in line with earnings of carers. The difference between this and other heads of damage has already been recognized by the indexation provided in Periodical Payment Orders in England & Wales, where the ASHE 6115 earnings index is used for costs of care instead of the consumer price index. Having a separate discount rate for costs of care and case management would avoid the uncertainty introduced into the setting of a single rate by the need to interpolate between different inflation assumptions and decide what weight to give to each. The respective weights can be expected to be very different for different cases.

A discount rate taking into account real earnings growth would also in principle be appropriate for future loss of earnings. This could be the same as or different from the discount rate for costs of care and case management but should reflect earnings growth in general. Separate explicit assumptions would continue to be made if the pursuer had a clear expectation of career development earnings increases in excess of general increases.

An argument could also be made for having a separate discount rate for health care costs other than costs of care and case management, including elements such as medical consultations, treatments and therapies, since these costs rise faster than the general consumer price index, driven by a significant underlying earnings component. However, the justification for this is less clear-cut and there would be advantages in limiting the number of discount rates to just two: price-related and earnings-related.

I have direct experience of working in the personal injury compensation environment in the Republic of Ireland, where the judgments of the Courts are preeminent in arriving at the PIDR. The limitations of the *Gill Russell v HSE* judgment of 2015 are well recognized, since it was ostensibly based on the yields on UK Index Linked Gilts (ILGs) but the judge increased the 0% indicated at the time by ILG yields to 1.5% on the grounds that he expected interest rates to rise in the coming months (in practice the opposite occurred for

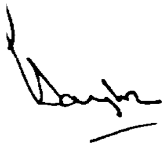
several years, underscoring the dangers of trying to second guess how markets will move in future). Future real earnings growth was also argued by expert evidence to be 1.5% or more but the Court instead adopted 0.5%. So instead of dual rates of 0% /–1.5%, as expected from the evidence, the judgment came out with 1.5%/1.0%. Although there has not yet been a subsequent Court judgment to change this, cases have regularly been settled in the last couple of years at effective discount rates ranging from –1.5% to –3.25%, reflecting real yields on euro-denominated bonds, such as French and German bonds, and real earnings growth in Ireland of 1% to 1.5%. Although the Republic of Ireland has a PPO regime, it is not regarded as a satisfactory route to settlement in practice because of limited indexation provisions.

A dual rate structure, with a lower rate for earnings-related heads of damage such as costs of care and case management, was approved by the Privy Council in 2012 in respect of a landmark Guernsey case (*Helmot v Simon*) and by the Court of Appeal in Bermuda in 2016 (in *Thomson v Thomson* and other conjoined cases). It is worth mentioning that this same sort of dual rate structure is typically used in UK Damages Act cases where the pursuer is now resident in another jurisdiction. As far as I know there are no Court precedents but many instances of cases being satisfactorily settled on this basis.

Inflation

It doesn't matter greatly whether the PIDR is set relative to RPI or to CPI. RPI has been the logical measure since the PIDR was set relative to real yields on Index-Linked Gilts, which are relative to RPI. However, since RPI is to be replaced by CPIH in 2030 and the two series will merge, there is an argument for moving sooner rather than later to CPIH.

Yours sincerely



Chris Daykin
Independent Consultant and Actuary

CLYDE&CO

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Extract from stakeholder letter dated 31 May 2023

(numbering replaces bullet points in the original)

The method for calculating the PIDR is set out for Scotland in Schedule B1[1] to the 1996 Act. The framework is designed to create a fair and accurate way to set the discount rate, taking account of a range of factors as follows:

(i) the make-up of the notional portfolio (as laid out in paragraph 12 of Schedule B1[1]) in the Act.

(ii) the assumed period of investment (currently 30 years[2]);

(iii) the impact of inflation (currently allowed for by reference to the Retail Prices Index); and

(iv) the standard adjustments that must be made by the rate-assessor to a rate of return (currently set at 0.75%, which represents the impact of taxation and the costs of investment advice and management; and 0.5%, which is the further margin involved in relation to the rate of return).

Scottish Ministers[3] may, by regulations, adjust these factors. We now intend to consider whether or not any such adjustments are merited. We would, therefore, welcome your views on the need or otherwise to adjust any of the above and request any evidence that you can provide to support these views.

These notes detail the correct citations for Northern Ireland.

1. At Schedule C1.
2. 43 years.
3. The Department of Justice.

Clyde & Co's response to numbered 'factors' set out above

A. Preliminary points

Areas of expertise

We do not, as an insurance litigation firm, have the requisite expertise to comment on detailed technical matters relating either to economic performance, metrics, and indices generally or to investment of damages in particular. Aside from those details there are, however, points of principle and/or policy which have informed the paragraphs of the near-identical Schedules B1 & C1 and on which we feel it is appropriate to respond.

Evidence-based approach

It seems to us essential that, in considering whether or not to make any adjustment to any of issues (i) – (iv), there should be a robust body of evidence in support of either the status quo or of any new approach. We would suggest further that such evidence should, as far as is possible, be published in full by the administrations.

Reconsidering differences

This theme runs through our brief responses below and they should be seen through its lens. The legislative frameworks in Scotland and Northern Ireland are very different from that in place in England & Wales, with the principal difference being the more prescriptive

approaches in the former as opposed to the Ministerial discretion in the latter. Both are equally valid approaches to the setting of statutory PIDRs.

We recognise that damages policy and civil justice are devolved matters but it nevertheless seems anomalous that there is such a broad spread of PIDRs across the UK's three jurisdictions given that each purports to be designed around the same objectives, ie: (a) to provide full compensation for future losses via the PIDR and lump sum system, (b) to assume a low risk approach to risks associated with the investment of damages over the duration of the award and (c) to adjust notional yields appropriately for inflation, tax and investment charges. Citizens in the UK will be subject to the same national economic conditions and challenges and, largely, to the same overall tax regime. They also will (or ought to) have access to the same investment advice regarding awards. It therefore seems to us that real or assumed investment behaviours are likely to be the same regardless of whether an individual in receipt of damages might be based in Stirling, Strabane, or Sheffield. This sort of conclusion might therefore point towards near-identical PIDRs across the UK rather than to the current 125 basis points spread (between -0.25% in England and -1.5% in Northern Ireland).

B. Questions raised

(i) Notional portfolio

We would regard the portfolio at Schedule B1 (and C1) as more cautious than that adopted in England & Wales where, as far as we know, there is no evidence of widespread under-compensation. It is not within our expertise to advise on what a differently constituted portfolio might comprise (and how it might be weighted) but we would point out that the current portfolio will tend to over-compensate when compared to awards in England & Wales.

(ii) Assumed period of investment

The analysis carried out by the Government Actuary's Department (GAD) in 2019 for the English rate review concluded that the average duration of relevant awards was 43 years. This was adopted there and, in 2022, in Northern Ireland. The use in Scotland of a period of 30 years departs from this evidence and, all other things being equal, would tend to produce over-compensation when compared to the other two jurisdictions.

(iii) Impact of inflation

As already noted, it seems to us that each part of the UK is subject to the same overall inflationary conditions and pressures. This would tend to suggest that taking account of inflation ought to be consistent across the three jurisdictions, which is not the case in practice. We are unable to advise on the detail of appropriate approaches to inflation, other than to suggest: (a) that the role of RPI in the process be reviewed, given its shortcomings[1] and (b) in any event, that a medium to long term view of future inflation should be taken when setting a PIDR rather than using a short-term snapshot (particularly during a volatile period such as at present).

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[1] See, for example: Measures of Price Inflation: RPI, CPI, and CPIH - Actuaries in government (blog.gov.uk) and Shortcomings of the Retail Prices Index as a measure of inflation - Office for National Statistics (ons.gov.uk)

(iv) Standard adjustments (impact of taxation and the costs of investment, further margin)

Taking account of inflation and investment charges is a logical and appropriate feature of setting a PIDR. Although the 0.75% figure is set out in Schedule B1 & C1, we note that the GAD 2019 advice (England & Wales) included this same figure, based on evidence analysed at that time. We would suggest that an evidence-based approach should be adopted if a change to this particular standard adjustment was to be contemplated.

In respect of the further margin, we remain of the view that its inclusion amounts to "double counting" and leads to an artificially low PIDR and hence real risks of significant over-compensation. Our reasons for this view were set out in our representations - in the name of our predecessor firm BLM Law - to the Northern Ireland Assembly in October 2021 which are available at: blm-law-r-letter-to-committee-clerk-docx.pdf (niassembly.gov.uk)

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CLYDE&CO

Personal Injury Discount Rate: Exploring the option of a dual/multiple rate

Response of Clyde & Co, April 2023

1 Damages for future pecuniary loss: overall context and preliminary remarks

1.1 In respect of compensation for personal injuries, we accept entirely that the aim of the law of damages should be, as far as is possible in monetary terms, to achieve full / 100% compensation[1].

1.2 When considering damages for future pecuniary losses, a lump sum approach will necessarily fix the calculation of the award at a single point in time, regardless of whether a single or dual/multiple personal injury discount rate (PIDR) is used. An inherent feature of the lump sum method is that all assumptions about the future are crystallised at the point of calculation and cannot subsequently be varied. This is simply an inevitable consequence of using a lump sum approach.

1.3 Given that the reality of the future after the award is made is unlikely exactly to match the assumptions at the time of calculation, there will be some cases which are over-compensated and others which are under-compensated (because the reality of the future will differ from the assumptions made about it). We would argue that if those outcomes broadly balance each other and if extreme examples of either effect are controlled, it is reasonable to say that the 100% compensation principle is satisfied at a systemic level.

1.4 The method of calculating the lump sum should balance accuracy with ease of application in practice.

1.5 We are concerned that introducing higher levels of complexity into the calculation could lead to significant delays and extra transactional/processing costs (due to the additional legal analysis and expert evidence required) in resolving claims - whether via settlement or via litigation - which we say is not in the interests of claimants in particular and other stakeholders more generally.

1.6 We have yet to see a comprehensive body of objective evidence that points to the current single PIDR model in England & Wales being fundamentally flawed. It may, of course, be capable of improvement. However, if proposed improvements were to introduce additional levels of complexity when compared to the present approach - as would strongly appear to be the case if a dual/multiple rate approach were to be adopted - it seems to us that the benefits of any improvements would need to be shown clearly to outweigh the consequences of the additional complexity. This concern would point to the need for a comprehensive impact assessment if a dual/multiple rate model were to be introduced.

1.7 We would observe that the government's main concern in examining dual/multiple PIDRs via the current call for evidence appears to us to be to establish if 'better' provision could be made for that cohort of claims involving short(er) life expectancies in particular. For example, this possibility is mentioned in the executive summary of the call for evidence

[1] Instances of partial liability and/or contributory negligence do not offend against this aim.

> *"The case for a dual rate is though, an interesting one, with the analysis providing some promising indications, particularly in relation to addressing the position of short-term claimants."*

and in the penultimate bullet point at page 2 of the Government Actuary's July 2019 advice[2]

> *"…adopting a dual PI discount rate is likely to more closely match the pattern of expected future investment returns which at the present time, are characterised by lower short-term investment returns but much higher long-term rates. As such a dual rate may lead to more equal outcomes between claimants investing over different periods, depending on how this is assessed"*

1.8 It is our view that financial planning across the duration of the award / life expectancy is likely to be a significantly stronger influence on assumed investment behaviours of claimants (both hypothetical and real) in receipt of awards for future pecuniary losses - and hence of the rate(s) of investment return(s) on notional portfolios – than particular measures of rising costs over time in any distinct elements of the award. If this is a reasonable premise, it appears to us to follow from it that if dual or multiple rates were to be adopted, an approach based on different PIDRs depending on the duration of loss would be much more clearly indicated than one which was predicated on different PIDRs according to heads of loss.

1.9 The formal rate-setting and review process is clearly set out in the Civil Liability Act 2018. It is therefore our view that when the next formal review of the rate required by the Civil Liability Act 2018 comes around[3], the Lord Chancellor at that time would not formally be bound by the reasons[4] given by the Lord Chancellor in post when the current single rate was set in 2019.

[2] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/817236/Setting_the_Personal_Injury_Discount_Rate__web_.pdf

[3] The review must be started no later than mid July 2024 and must be concluded within 180 days.

[4] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/816819/statement-of-reasons.pdf

Questionnaire

1 **Question 1:** Do you have a preferred model for a dual/multiple rate system based on any of the international examples set out in the Call for Evidence paper (or based on your or your organisations experience of operating in other jurisdictions)? Please give reasons with accompanying data and/or evidence.

1.1 We do not have a preferred model based on any of the international examples in the call for evidence.

1.2 Other jurisdictions will have different economies as well as different litigation systems, cultures, and practices. We would therefore caution against any simplistic 'cut and paste' of approaches to the PIDR(s) that may be in place in other jurisdictions, even those which operate under a common law system that may appear, superficially, to be close that of England & Wales.

1.3 However, if the problem which the call for evidence is seeking to address is an attempt to find a 'better', fairer way of dealing with those claims involving shorter periods of loss / life expectancy[5], then two points would seem to follow clearly from that.

(a) It is far from obvious that PIDR model(s) based on rates by head of loss address this problem in any meaningful way.

(b) The duration of loss model described in the call for evidence[6] as "*stepped*" may go some way to addressing this problem. However, because of the way the "*stepped*" approach operates, it will give rise to awards for periods marginally longer than the so-called "*switching point*" that are lower[7] than awards for periods at or marginally shorter than the "*switching point*". We suggest these are unfair outcomes which, in our view, render this approach not fit for purpose.

1.4 The single PIDR in force currently in England & Wales is a relatively straightforward model that is well understood by parties, compensators, legal practitioners, experts, and the courts. Legal advisers carry out the calculations and there is little need to instruct specialist actuaries or accountants in all but the most unusual claims.

1.5 If, however, the MoJ were to decide, on the balance of evidence submitted during this exercise and for clearly stated reasons, that a dual rate model should be adopted, we would tentatively suggest that the "*switched*" model as described at paragraph 67 of the call for evidence could be likely to be an appropriate approach. We believe that the "*stepped*" model at paragraph 66 is unfair because of so-called 'cliff edges' in those claims in which losses stretch just beyond the "*switching point*" (as explained above). We would caution against the "*blended*"

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[5] As we have pointed out at 1.7 of our preliminary remarks above.

[6] At its paragraph 66.

[7] How much lower these awards will be, and for how long past the "*switching point*" this aspect last, will depend on the difference in the PIDRs either side of the switching point.

model at paragraph 68 because of its inherent complexity, which could lead to additional delays and transactional costs in claims handling.

1.6 We foresee real difficulties in approaches that would adopt dual or multiple rates by head of loss. It seems to us that not only would this be likely to lead to increased 'gaming' of the system - costly satellite litigation around which losses fall in which 'pot' - it also fails entirely to address the problem of delivering fairer outcomes for those claims with short(er) life expectancies / durations of loss.

1.7 Terminology. In the paragraphs above and throughout this response, we use the descriptions switched, stepped, and blended in the same way as in the call for evidence. That said, it appears to us that it would be more logical to change the order of the first two of these. A model which features two (or more) operative discount rates but in which in practice only ever uses one of those to value the lump sum based on the duration of the loss in question seems to us to be better described as "*switched*". The multiplier / multiplicand calculation switches entirely from using rate 'a' to using rate 'b' if the loss extends beyond a specified period or "*switching point*". However, a model which uses rate 'a' for that part of award[8] that relates to the period before the "*switching point*" and then uses rate 'b' for the remainder (ie that part of the award represented by the total duration of loss minus the "*switching point*") seems to us to be better described as "*stepped*". This calculation involves two discrete mathematical steps as well as a step-change in the discount rate being used.

1.8 Ontario. We observe that there may be some confusion among stakeholders as to whether this model should be regarded as "*switched*" (as defined in the call for evidence rather than as we suggest immediately above) or as "*blended*". Based on our research and on contacts with colleagues in Canada, it is our very clear view that the Ontario model should properly be described as "*blended*". We would therefore strongly urge the ministry, when analysing responses to this call for evidence, to take particular care when considering any submissions which refer to and/or express views on 'the Ontario model' without a description of how the responder regards that model as operating in practice.

2 **Question 2:** What do you consider to be the main strengths and weaknesses of the dual/multiple rate systems found for setting the discount rate in other jurisdictions?

2.1 In broad terms, we agree with the analysis of the advantages and disadvantages of these models as set out in paragraphs 79 – 81 of the call for evidence.

2.2 As already noted in our preliminary remarks, and from a policy-setting perspective, the core question if a move to a dual/multiple PIDR model is to be contemplated is whether the benefits of implementing such an approach can be shown clearly to outweigh the downsides – in terms of added complexity and the associated risks of additional costs and delays to claims lifecycles – within that approach?

2.3 Despite the possible advantages set out in those paragraphs noted above, it is not clear to us that an evidence base has yet been established for such a move.

[8] It is only in those cases in which the duration of the loss is less than the switching point that both these models will produce the same valuation.

Although we accept that this call for evidence is likely to gather indications (and possibly data) to that effect, it seems to us that a comprehensive impact assessment should be prepared if any of the dual/multiple rate options are to be taken forward.

2.4 It may be helpful here to summarise our views at a high level of principle.

(a) The current **single PIDR** model is familiar to practitioners and is a straightforward approach which is readily understood by litigants, practitioners, compensators, and the courts.

(b) A **dual/multiple PIDR model based on heads of loss** does not appear to us to address the stated problem of dealing more equitably with cases involving shorter periods of loss.

(c) The **dual/multiple PIDR model described[9] as "*stepped*"** produces unfair outcomes just after the switching point.

(d) The **dual/multiple PIDR model described[10] as "*switched*"** could, as a concept, address the stated problem here, but would necessarily involve additional complexities[11] when compared to the single PIDR.

(e) The **dual/multiple PIDR model described[12] as "*blended*"** could, as a concept, also address the stated problem but would involve higher levels (potentially significantly so) of additional complexities[13] when compared both to the single PIDR and the "*switched*" model.

2.5 It may be worth noting at this point that we understand that there has been recent active debate in Ontario about the possibility of reverting from its particular variant[14] of a dual rate by duration of loss model to a single PIDR.

3 **Question 3:** What do you consider is the optimal point for the switch-over from a short to a long-term rate on a duration-based dual rate model? Please give reasons with accompanying data.

In our view, the question of the optimal duration of the switch-over is something on which expert economic and investment advice should be sought, if a dual rate by duration of loss model was to be taken forward. We would, however, like to make two general comments regarding the idea of a "*switching point*".

3.1 First, it seems to us potentially misconceived to refer to any initial period before the "*switching point*" as 'the short term'. We very much doubt that investment experts would classify periods of 10 or 15 years in this way.

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[9] At paragraph 66 of the call for evidence.

[10] At paragraph 67 of the call for evidence.

[11] In terms of delays in claims resolution, additional costs due to heavier involvement of legal advisers and greater need for expert financial/actuarial evidence.

[12] At paragraph 68 of the call for evidence.

[13] As described in footnote 11 above.

[14] The operation of which is described at 1.8 above.

3.2 Second, the initial rate should switch to the longer period rate at the earliest point in time that is consistent with the longer period rate reasonably reflecting stable long term economic yields. We would point out that paragraph 71 of the call for evidence "*suggests* [that] *the optimal period for a switchover would be at around 10 years to achieve a balance in the interests of short and long-term claimants and defendants in this scenario*".

4 **Question 4:** What would you consider an absolute minimum and maximum point for the switch-over between two rates to be? Please give reasons.

As a litigation firm, we do not claim to have the relevant expertise to answer this question.

5 **Question 5:** If a dual rate system were to be introduced, would you advocate it was established on the basis of the duration of the claim with a switchover point, on duration based on length of claim or its heads of loss (or a combination of the two)? Please give reasons for your choice.

5.1 It appears appropriate here to repeat the summary of views that we offered in our response to question 2 above, ie:

(a) The current **single PIDR** model is familiar to practitioners and is a straightforward approach which is readily understood by litigants, practitioners, compensators, and the courts.

(b) A **dual/multiple PIDR model based on heads of loss** does not appear to us to address the stated problem of dealing more equitably with cases involving shorter periods of loss.

(c) The **dual/multiple PIDR model described as "*stepped*"** produces unfair outcomes just after the switching point.

(d) The **dual/multiple PIDR model described as "*switched*"** could, as a concept, address the stated problem here, but would necessarily involve additional complexities[15] when compared to the single PIDR.

(e) The **dual/multiple PIDR model described as "*blended*"** could, as a concept, also address the stated problem but would involve higher levels (potentially significantly so) of additional complexities[16] when compared both to the single PIDR and the "*switched*" model.

5.2 In addition, and for the avoidance of doubt, it seems to us that "*a combination of the two*[17]" dual/multiple rate approaches is very likely to involve high levels of complexity in practice which we struggle to see as likely to be justified on cost / benefit terms.

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[15] In terms of delays in claims resolution, additional costs due to heavier involvement of legal advisers and greater need for expert financial/actuarial evidence.

[16] See footnote above.

[17] As is suggested in this question.

5.3 In points (a) – (d) below we outline our views on how the calculation under a "*switched*" model - if adopted - should be performed. We would be happy to provide the ministry with any further clarification of this calculation and to provide worked examples and other modelling analysis that we have performed.

(a) Part 1. Calculate the part of award for the period up to the "*switching point*" in the usual way, but using a multiplier for this period, based on the initial rate, which allows for the risk of mortality.

(b) Part 2: Calculate the part of the award for the second period (ie beyond the "*switching point*" and for the remainder of the duration of the loss) using a deferred multiplier commencing at the "*switching point*" derived using the second (ie long term) rate and which allows for the risk of mortality.

(c) We submit that the multipliers used in each of these parts should take proper account of the risk of mortality over the period in question. We do not think it is realistic to regard the periods either side of the "*switching point*" as terms certain.

(d) We also submit that in part 2 of the calculation, the computation of the deferred multiplier commencing at the "*switching point*" should, in allowing for this deferred period, use the second (ie long term) rate. We suggest that this is a realistic approach in that it clearly reflects the idea that the hypothetical investor should be able to secure the benefit of long term rates for this second part of the duration of the award.

6 **Question 6:** In dealing with volatility of markets over the short-term is it a reasonable assumption that short-term rates in a duration-based system should be more variable and set at a lower rate; and long term rates more stable and set at a higher rate? If you agree or disagree that this assumption is reasonable, please say why.

6.1 We do not agree with the assumption.

6.2 Superficially, we accept that it may *appear* likely that there may be more volatility in yields over shorter durations than in those over longer periods.

6.3 We would suggest however, that it is likely to be inappropriate to proceed on the basis of assumptions here. If dual rates by duration of loss are to be adopted, the level of the rates either side of the "*switching point*" - and the "*switching point*" itself - should be derived from a sound evidential basis[18]. This may be a matter for exploration by the Government Actuary and the expert panel which will advise the Lord Chancellor during the statutory review of the PIDR.

6.4 If adopted, we could envisage that this model may be associated with reviews of the initial period rate that could be more frequent that the five-year long stop set out in the 2018 Act. On our reading of it, more frequent reviews are permitted by the Act, although the prospect of more frequent reviews - and the associated volatility - could have an adverse and potentially 'chilling' effect on settlement negotiations and could lead to some 'gaming' by those who perceive that the next change would work to their advantage. We note that paragraph 43 of the call for

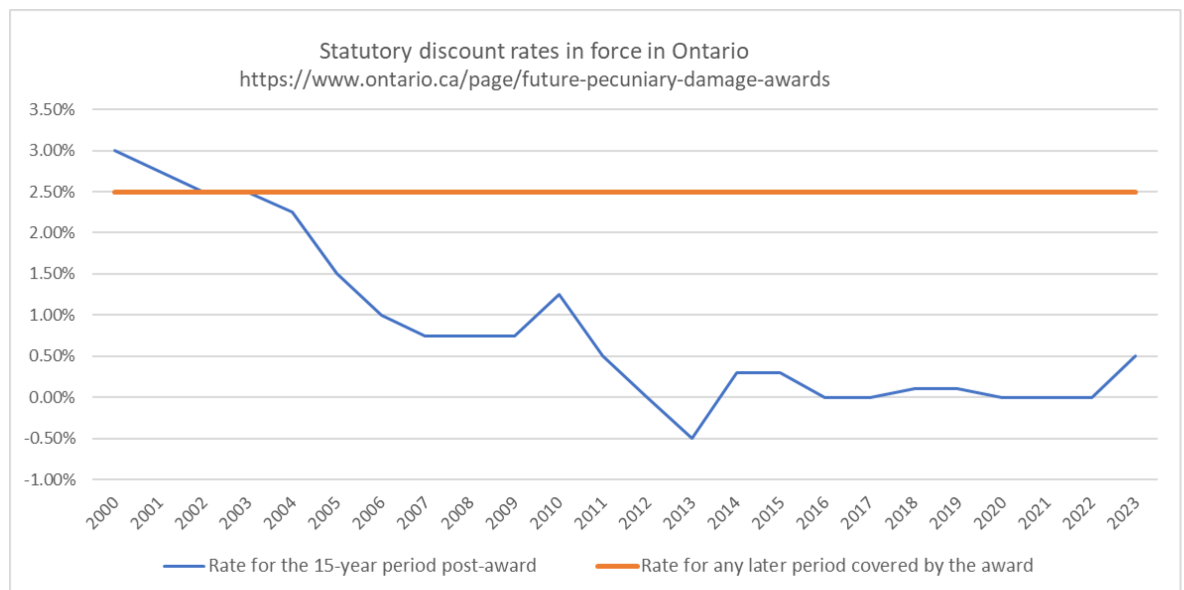
[18] Any such evidence would be likely to be provided by those experts properly qualified to answer questions 3 and 4 above.

evidence points out, in respect of Ontario, that "*in the 22 years since the dual rate system was introduced, the short-term rate has been amended 16 times*".

7 **Question 7:** If short-term rates are more volatile, should frequency of review be increased? Please explain your reasoning.

7.1 Please see our answer to question 6 above.

7.2 We would also suggest that the longer period rate is unlikely to require any significant adjustment if set – based on evidence – at a level that reasonably reflects stable longer term yields over economic cycles[19]. This appears to us to have been the experience in Ontario, as shown by the graph below.



7.3 We would repeat that any increased frequency of the rate reviews is likely to create further uncertainty and cost and could delay settlements.

8 **Question 8:** What would you regard as the advantages of a dual/multiple rate system?

9 **Question 9:** What would you regard as the disadvantages of a dual/multiple rate system?

9.1 Both these questions are addressed in our response above to question 2 in which we refer to the analysis at paragraphs 79 – 81 of the call for evidence.

9.2 In addition, these models may be (very) difficult for claimants to understand, particularly those for whom full capacity is a concern. This point is made in the second sentence of the second bullet point at paragraph 80 of the call for evidence:

[19] A point already made above in our response to question 3.

"Personal injury litigation is already overly complex, and this would add an additional layer making it harder for parties and claimants and their families, including in making decisions on settlements and investment of damages."

10 **Question 10:** What do you consider would be the specific effects on implementing and administering the discount rate if a dual/multiple rate is introduced?

11 **Question 11:** In addition to specific effects, do you consider there will be additional consequences as a result of implementing a dual/multiple rate? Please give reasons with accompanying data/evidence if possible.

11.1 Our answer to both these questions is predicated on the likelihood that a 'heads of loss' model would fail to address the stated problem of claims shorter durations of loss[20] and therefore addresses variants of the 'duration of loss' model only. We answer them together as we have not found it easy to separate "*specific effects*" and "*additional consequences*".

11.2 The possible effects of these models arise from the level(s) of complexity when compared to a single rate and are set out below in broad terms.

(a) Increased transactional cost. Due to the need for expert evidence, and legal advice, to assist in the calculation of awards. This might arise for a limited period until legal advisers and compensators become familiar with performing the calculations themselves. We understand, however, that lawyers rarely carry out calculations in Ontario despite that particular model being in place for more than two decades.

(b) Extended claims lifecycles. Another probable consequence of adopting a more complex approach.

(c) Greater uncertainty. It is foreseeable that any dual rate model may take time to 'bed in[21]' and, absent very clear guidance on the detail of the new model, it is foreseeable that appellate litigation might be required in order to test its scope and application. In addition, uncertainties would cause problems for compensators in preparing case reserves and in changing business models and systems.

(d) Ogden Tables. It seems to us that new sets of tables and new explanatory notes – with detailed worked examples – would be necessary to cater for a dual rate by duration model.

(e) Clear guidance. Stakeholders would need precise guidance – whether in the Ogden Tables or elsewhere – for each step of the calculation methodology[22]. This would have to cover the technicalities of the calculation while at the same time being couched in language that is accessible to parties, their advisers and to the courts. That does not appear to us to be an easy task.

[20] Please see the final paragraph of our response to question 1 above, which also refers to the risk of 'gaming' arising from this particular model.

[21] Although question 20 below does not use the phrase, it essentially seeks views on the prospect of any new PIDR model 'bedding in'.

[22] We have set out our understanding of the calculation at 5.3 above.

Any such guidance is also likely to be subject to close forensic analysis in, for example, the first wave of court approvals of new-style awards to protected parties.

(f) Outcomes over durations of loss less than the "*switching point*". Key assumptions here are (a) that the rate over the initial period would be lower than a single PIDR that achieves the same (systemic) level of over or under compensation and (b) that the rate over the longer period would be higher than that single PIDR. As long as these assumptions hold, it follows that those claims in which the duration of loss is lower than the "*switching point*" will receive higher awards than if the single PIDR had been in place. In this way, it might be said that the model provides 'better' outcomes for these cases. This appears to be a guiding principle that informs the call for evidence, as we noted above in our response to question 1.

(g) Outcomes over durations of loss longer[23] than the "*switching point*". These cases will be subject to the opposite effect and there will be a point in time, after the "*switching point*", from which the award under the dual rate model will be lower than would have been the case under the single PIDR. In our view, this is an inevitable and natural consequence of the arithmetic model and should be understood as such. It is **not** an arbitrary reduction in awards: rather, it is the balancing effect of making 'better' provision[24] for those claims in which the duration of loss is less than the switching point.

(h) Public confidence. The prospect of significant additional cost, delay and complexity associated with a dual rate model might, in our view, damage levels of public trust in the system for compensating the most severe cases of personal injuries involving significant future losses.

(i) Periodical payments. It is unclear to us how any dual rate system might affect, whether by intention or otherwise, the adoption and use of periodical payment orders for future losses. We will return to this in responding to question 21.

12 **Question 12:** If a dual/multiple PIDR were to be introduced would it be helpful to provide a lead in period to prepare processes, prepare IT changes etc. and if so, how long should this be? Please provide reasons for your answer.

12.1 Although it would be very helpful in theory for some lead time to be provided to stakeholders before moving to a dual rate model, in practice we believe doing so could prove extremely difficult.

12.2 The 2018 Act requires that the rate review must be completed, at the latest, within 180 days of mid-July 2024. It follows that *it is not possible to extend the rate review period to provide such lead time* without amending the Act; something which we regard as an unrealistic prospect. The question therefore changes to *whether such lead time could be signalled within the rate review period?*

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[23] Please refer to the explanation, at 1.3(b) above, of how unfair outcomes arise under the "*stepped*" model in those claims in which the duration of loss is marginally longer than the "*switching point*".

[24] We have referred above to this being the stated problem that the call for evidence appears to seek to address.

12.3 In our view, this would be fraught with difficulty. The expert panel's statutory role is to advise the Lord Chancellor on rate-setting. It seems to us that there would be a real risk of being seen to limit the scope of the panel's activity and analysis if the Lord Chancellor were to state, at the start of the 180 day review period, that he or she was minded to introduce a dual rate model. Furthermore, any statement to that effect seems to us likely to close down settlement negotiations completely given that all parties will be uncertain as to the outcome.

12.4 It is possible that a form of words might be found by which the minister could signal that, based on the responses to the current call for evidence and subject in any event to the deliberations of and the advice from the expert panel, he or she was minded to move to a dual rate at the conclusion of the review period. That said, such an approach seems not entirely to remove the prospect of been seeing to restrict the panel's role.

12.5 For these reasons we would therefore be extremely interested in seeing how the ministry reacts to responses to this question.

13 **Question 13:** What do you consider would be the effects of a dual/multiple rate on a claimant's investment behaviour and what would this mean for the design of a model investment portfolio?

Those who provide financial advice to claimants will be in a much better position to respond to this question than we are.

14 **Question 14:** What do you think would be the effects of a dual/multiple rate on drawing up assumptions for tax and expenses when setting the discount rate?

These are not matters on which we are able to offer detailed comments or evidence. Consequently, our response is limited to three general points.

14.1 Allowing for investment expenses. However, it seems to us very likely that claimants in receipt of awards for future loss of significant duration would *currently* - ie under the single PIDR in force for the time being - be being advised to invest in a shorter and medium to long term manner according to their needs. If that is correct, because claimants are already being advised in this way, there does not appear to be a need for further investment advice were a dual rate by duration of loss model to be introduced. If there is no further need, there should be no further allowance for investment expenses and the approach adopted in 2019 should be preserved.

14.2 For the avoidance of doubt, it is our view that the most appropriate method of dealing with the cost of investment advice in these claims is to make an appropriate adjustment for it when setting the PIDR, as was done in 2019. This may be regarded as a 'top down' approach.

The alternative, 'bottom up' approach of treating investment advice as a head of annual loss, subject to its own multiplier & multiplicand assessment in each and every claim, is very likely to lead to unnecessary cost, disputes, and delay.

14.3 Allowing for tax. Again, it seems to us that it would be more appropriate and efficient to address the impact of tax in a 'top down' way ie as part of the calculation of the applicable PIDR(s), as was done in 2019.

15 **Question 15:** What do you consider would be the effects of a dual/multiple rate on analysing inflationary pressures and trends when setting the discount rate?

This is not a question we are equipped to answer.

16 **Question 16:** What do you consider would be the effects on claimant outcomes of a dual/multiple rate being adopted for setting the discount rate?

16.1 Please see our responses (a) to question 1, which expresses our support for the 100% compensation principle, and (b) to question 11, which touches on likely claimant outcomes either side of the "*switching point*".

16.2 The additional 0.5% adjustment made in 2019. When last setting the rate, the-then Lord Chancellor deducted a further 0.5% from the +0.25% proposed in the Government Actuary's report. His reasons are set out at paragraphs 15 to 22 of his Statement of Reasons[25]. As noted in our preliminary remarks above, we do not regard those reasons as binding during the next formal review of the PIDR. It would therefore follow that the adjustment could be removed or reversed during the next review, even if that review was to conclude that a single PIDR should be retained. As already observed in our responses above, the underlying rationale for exploring a move to dual or multiple rates appears to be to provide 'better' outcomes for those claims with shorter durations of loss. In addressing this problem by implementing a dual rate, it seems clear to us that the case for making any additional adjustment to the rate(s) of return – as was done in 2019 – would be very significantly weakened, if not undermined entirely.

17 **Question 17:** If a dual/multiple rate was adopted would it be possible to return to a single rate in future reviews, or would a move be too confusing and complex and seen as irrevocable? Please give reasons.

17.1 If a dual rate were to be adopted, we have already identified that there will be additional complexity and hence the possibility for confusion. We would refer again here to our call for clear guidance on the detail of the calculation(s) in our response to question 11 above.

17.2 We do not see anything in the 2018 Act that suggests to us that a move to a dual rate would, were it made in 2024, be irrevocable. However, adopting a dual rate in 2024 and then restoring a single rate in a subsequent review (in 2029, say) would also lead to further complexity and confusion for all. In addition, all the cost and systems changes associated with the move to the dual rate would be wasted and yet more cost would need to be incurred in returning to a single rate.

17.3 The prospect of fundamental changes of this nature over relatively short periods would lead to very real practical difficulties: in reserving for claims, in future financial modelling for compensators, in the making and reviewing of settlement offers and in the conduct of case negotiations by parties and their representatives.

[25] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/816819/statement-of-reasons.pdf

17.4 We would add another level of potentially complexity: we are aware that solicitors and compensators are already dealing with notified claims (generally involving severely injured children) which are unlikely to resolve until after both the 2024 and 2029 rate reviews have concluded.

18 **Question 18:** What do you consider the respective advantages and disadvantages of adopting multiple rates would be, when compared with either a:

- single rate; or

- dual rate.

18.1 Please refer to our response to questions 2, 8 and 9 above.

18.2 In addition, if - as seems likely - the thrust of this question is to seek views on models which would adopt more than two PIDRs, it is our strong view that any such approach is very likely to involve levels of operational complexity which we would struggle to see as being justified by the apparent benefits of introducing such a model[26].

18.3 It seems to us that the greater the number of rates, the greater the complexity and risk of additional cost, delay, and confusion. There is also the somewhat more mundane but important risk that parties and their advisers may be more likely to make mistakes if operating under a highly complex model. It may well be worth re-emphasising here the extract from paragraph 80 of the call for evidence which we quoted when responding to questions 8 & 9 above.

"Personal injury litigation is already overly complex, and this would add an additional layer making it harder for parties and claimants and their families, including in making decisions on settlements and investment of damages."

19 **Question 19:** If a heads of loss approach were adopted, what heads of loss should be subject to separate rates – care and care management costs, future earnings losses, accommodation, or any other categories?

19.1 We do not support the heads of loss approach and repeat below the final part of our response to question 1 above, ie:

It seems to us that not only would this be likely to lead to increased 'gaming' of the system - costly satellite litigation around which losses fall in which 'pot' - it also fails entirely to address the problem of delivering fairer outcomes for those claims with short(er) life expectancies / durations of loss.

20 **Question 20:** Introducing a dual/multiple PIDR could result in increased levels of complexity for both claimants and compensators. Do you agree

[26] This is a very similar point to that made above at 5.2.

with the assumption that this complexity will stabilise and ease once the sector adapts to the new process? Please give reasons.

We do not agree with the assumption that complexity will stabilise and ease entirely. We would accept, however, that over time stakeholders[27] would become familiar with operating under a dual PIDR model and that one-off training costs, systems adjustments, and any new guidance (whether in the Ogden Tables or elsewhere) would 'bed in', meaning matters would appear clearer in practice. But it seems to us that a dual PIDR model would remain inherently more complex than a single rate even after any initial 'bedding in' period at the end of which stakeholders would have become accustomed to resolving claims in that way.

21 **Question 21:** The Government remains interested in exploring the use of PPOs in relation to high value personal injury settlements. We would therefore welcome any submissions, data and/or evidence stakeholders may have in relation to the effective use of PPOs.

21.1 We have been involved in settling a relatively low number of claims for damages for future loss by way of a PPO. Based on this small sample and on our understanding of the general personal injury sector (ie excluding clinical negligence claims), it is our impression that the take up of PPOs appears to have fallen since the 2017 change to the PIDR and is unlikely to have changed to any great extent since the current single PIDR was set in 2019 under the 2018 Act. The Institute & Faculty of Actuaries' Periodical Payments Working Group produces an annual analysis of PPOs numbers and trends based on surveying a significant proportion of the motor insurance market. Its most recent analysis[28] was presented in November 2022, capturing experience up to the end of calendar year 2021, may accessed via the link in the footnote.

21.2 The question refers to the government being *"interested in exploring the use of PPOs"*. We would be pleased to provide a representative of the firm to take part in any stakeholder activity taking this matter forward.

22 **Question 22:** Do you agree that using a higher PIDR to calculate the real rate of return in settlements which include a PPO element would result in a more appropriate way to adjust nominal investment returns for future inflation? Please give reasons.

22.1 We should say at the outset that we have not found this an easy question to interpret. It seems to us to incorporate two different elements: first, establishing what are the appropriate adjustment(s) to be made to nominal investment returns to allow for future inflation and, second, is there a basis for making a policy choice to adopt a different, higher PIDR than would apply to a 'lump sum only' award if a PPO is used to compensate some elements of the future losses?

22.2 In respect of the first, we have already expressed our view above (at 1.3, 2.4 and 19) that a dual/multiple PIDR based on head of loss has significant disadvantages

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[27] Including the judiciary.

[28] https://www.actuaries.org.uk/system/files/field/document/B3%20PPOs_0.pdf

and complications. This question, and the text which precedes it, would seem to introduce levels of complexity even in the case of a single rate model. We are therefore unable to agree with it for the purposes of this first element.

22.3 We turn to the idea of adopting a different, higher PIDR for the residual lump sum where a PPO is used. We are also unable to agree with it. Introducing further complication is again a very relevant concern. It also seems to us that such a proposal would be likely to disincentive the use of PPOs, because of the perception that a lower award would result. Both these concerns seem to us to run very much against the sense of paragraph 110, which envisages whether adopting a *"PPO could be made quicker/simpler* [and] *looking at the guidance available to claimants on whether to choose a PPO or a lump sum."*

22.4 An over-arching difficulty with the proposal is whether it would be permissible under the 2018 Act? The relevant provisions[29], new subsections A1(3) & (4) of the Damages Act 1996, permit different rates of return for different classes of case. It is not immediately obvious to us that the method by which the award is delivered would qualify as a different class of case.

23 **Question 23:** What impact would a dual/multiple rate system have on protected characteristic groups, as defined in the Equality Act 2010?

We offer no answer to this question.

[29] https://www.legislation.gov.uk/ukpga/1996/48/section/A1

(3) An order under subsection (1) may prescribe different rates of return for different classes of case.

(4) An order under subsection (1) may in particular distinguish between classes of case by reference to—

(a) the description of future pecuniary loss involved;

(b) the length of the period during which future pecuniary loss is expected to occur;

(c) the time when future pecuniary loss is expected to occur.

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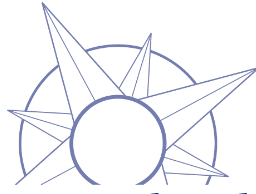


Compass Chambers

Response to the Request for Views on the Personal Injury Discount Rate issued jointly by the Scottish Government and Department of Justice for Northern Ireland

July 2023

About Compass Chambers

1. Compass Chambers is a stable of members of the Faculty of Advocates[1]. Our members include 22 Queens Counsel and 34 Junior Counsel practising in diverse legal fields. One of the stable's key specialisms is Reparation. Members of Compass Chambers act for pursuers and defenders in such claims. The use of the discount rate and the Ogden tables is an important and frequent part of the work of all of the members involved in quantifying damages in such cases.

Views Sought

2. The request for views is set out in a letter published online on the 12 June 2023. The letter sets out that the Government Actuary is due to start reviews of the PIDR on the 1st July 2024. The letter sets out the background to the PIDR and that one if it's aims is to avoid over or under-compensation. There are various factors set out, including the makeup of any notional portfolio, an assumption regarding the period of investment, the impact of inflation as allowed for by reference to the retail price index and standard adjustments to represent the impact of taxation, costs of invest advice and management. The Scottish Government may adjust these factors and intend to consider if any such adjustments are merited. Views are sought on the need or otherwise to adjust these factors and there is a request for any evidence.

3. Views are also being sought on whether a single or multiple rate should apply, as laid out in paragraph 21 and 22 of Schedule B1 of the act, if multiple rates were to be introduced what would views be in a preferred model.

Response to Request for Views

Views on the need to adjust the factors.

4. Our members do not propose that the factors taken into consideration in determining the PIDR require to be adjusted. We would, however, highlight the following.

5. The aim of damages is to restore parties, insofar as possible, to the position they would have been in but for any breach of duty. The use of the PIDR, as applied with the Ogden tables, is a method of calculation for future losses. Some examples would be future care costs for the seriously injured, future loss of earnings or lost years claims for those with reduced life expectancy. While periodic payment orders ('PPOs') are occasionally used in practice, they remain rare. Most cases with claims for future losses resolve this head of claim on a

[1] Members of the Faculty of Advocates who subscribe to the services provided by Faculty Services Limited each belong to a group of Advocates known as a 'stable'. Each stable has its own system of governance, including selection of its members.

lump sum basis. There is an assumption that the pursuer can invest that sum to attain investment benefit to meet the costs of their future needs/losses. An important aspect of the law is ensuring that injured persons are properly compensated but injured persons should not be overcompensated and receive windfalls because of any injury. It is a matter of balance, and the prevailing economic situation and the PIDR should reflect the reality of what investment will bring and the buying power of the currency.

6. With reference to the impact of inflation, the discount rate was last set by the Scottish Government in September 2019, at that time the RPI rating was 291. As of May 2023, this had increased to 375.3[2]. Along with this, the inflation rate and Consumer Price Index (CPI) has also significantly increased. The news outlets have described the current economic situation as a "cost of living crisis".

7. It should also not be lost sight of that, in terms of the standard adjustments made for the rate of return, the likely cost of advice and management will be more expensive in the future if inflation continues to rise.

8. Our members consider that the prevailing worldwide economic situation has changed significantly since September 2019, with reference to UK's domestic RPI, CPI and Inflation rate. Compass Chambers welcome a review of the PIDR at this stage. Anecdotally, clients (particularly pursuers) are concerned about rising costs when discussing damages that have to cover future losses.

Views on whether a single or multiple rates should apply.

9. Our members are neutral on this point. That said, no examples have been provided of members favouring a multiple rate model over the current single rate. It is not clear how and in what circumstances a multiple rate would apply in practice.

10. It is understood that a Consultation on this point was carried out between 17 January 2023 and 11 April 2023 in England and Wales and that the response is due sometime in July 2023.

11. We note that there has been concern raised in public responses to the Consultation in England and Wales that proposals for a dual or multiple personal injury discount rate could be seen as placing additional pressure on often catastrophically injured pursuers to take greater risks, when they are already in the position of requiring to take risks by investing compensation which they require to meet their needs for the remainder of their lives. Indeed, there are concerns that economic instability and high inflation give rise to under compensation since the last rate was set. Against that, it is often said that, in general terms, the longer an investor is prepared to invest their money, the more risk they can tolerate and the better returns they can expect.

[2] As per Kemp and Kemp Practice Tools

12. Compass Chambers would suggest further review of this point in Scotland once the results of the England and Wales consultation have been published.

DAC Beachcroft NI LLP's response to the Department of Justice's request for views on the future of the Personal Injury Discount rate.

DAC Beachcroft's Claims Solutions Group provides general insurance claims litigation and claims handling services to insurers in England, Wales, Scotland and Northern Ireland. As part of DAC Beachcroft LLP which services Scotland, Ireland and global markets, we have more than 500 insurance professionals and act for all of the top 20 UK general insurers and have expertise and experience across the entire sector. Our long history of commitment to, and investment in, the insurance sector means that we have an unrivalled depth of experience and breadth of insight. Our claims business reacts quickly to the dynamic claims industry and the changing needs of our clients whilst providing a local service with the support of a global network.

Our team has a deserved market-leading reputation for providing innovative and pragmatic solutions to liability claims disputes of all types and insurance issues generally. We pride ourselves on delivering commercial, value-driven legal services. With specialist expertise covering catastrophic injury, claims validation, costs, credit hire, disease and safety, health and environment law, the team covers the full range of personal injury work. Our strategic Advisory team offers a unique service for insurers dealing with emerging and important market issues.

DAC Beachcroft responded to the Ministry of Justice's Call for Evidence – exploring the option of dual/multiple rates. A copy of our response is attached. In large part our response was supportive of the Association of British Insurer's response. We have also seen and support the ABI's response to the Department of Justice's letter of 31 May 2023.

We note that the Department of Justice is now considering whether to adjust any of the factors applied to calculate the PIDR as set out in Schedule C1 of the Damages Act 1966.

The make-up of the notional portfolio

The notional portfolio is in our view overly cautious. One of the other factors set out in the schedule is that the rate of return should reflect the return that could reasonably be expected to be achieved by a person who invests (a) in the notional portfolio; and (b) for a period of 43 years.

DAC Beachcroft accept the 43 year period as accurate and based on the evidence originally supplied by the ABI following a data collection from its members. We take issue that any properly advised claimant investing for that period would invest in a portfolio with such an overly cautious allocation to equities. At present UK equities are at 7.5% and Overseas equities at 12.5%.

In GADs advice to the Lord Chancellor from 2019[1] table 5 sets out Low-risk portfolio allocation. The Lord Chancellor in assessing the PIDR for England & Wales adopted the middle of the 3 options, which allows for 32.5% equities. This is in our view a significantly more appropriate

[1] Setting the Personal Injury Discount Rate – Government Actuary's Advice to the Lord Chancellor – 25 June 2019

allocation of equities, especially when considered as against the 43 year investment period.

The assumed period of assessment

Whilst anecdotally we have heard that the period may now be 45 years rather than 43, we have not seen any evidence in support. The only detailed evidence that we are aware was submitted came from the ABI and that supported 43 years. We therefore support making no adjustment to that figure.

It should be noted however that the economic scenario generator as applied by GAD is overly cautious and does not reflect real-world rates of return. GAD should make reference to wide ranging market studies[2] to ensure that an overly-prudent approach is not adopted. We are aware that the ABI has encouraged GAD to consider such studies in the past and we would echo that encouragement.

The Impact of Inflation

DAC Beachcroft does not agree that RPI is the correct index against which to measure inflation. RPI lost its designation as a national statistic back in 2013 because it failed to meet international standards. CPI replaced RPI in 2011 as the UK Government's preferred measure of inflation for benefit and tax uprating purposes.

We adopt the ABI's comments on this issue and would urge the Department of Justice to make the relevant adjustment such that CPI is considered to be the appropriate index against which to measure the impact of inflation.

We would also highlight that GADs assumption for damage inflation of CPI + 1% in its report to the Lord Chancellor in 2019 is no longer appropriate. Again, we adopt the ABI's reasoning on this issue.

The standard adjustments

DAC Beachcroft adopts the ABI's response on these points. We would highlight that at present there is already a considerable degree of over-prudence built into the methodology used to calculate the PIDR (and the methodology applied by GAD in applying those measures). As such the additional adjustment of 0.5% merely adds another level of prudence to an already over-prudent calculation, which has led to the PIDR in Northern Ireland being the lowest in the world. The additional adjustment should therefore either be removed or set at 0%.

Single or Multiple Rates

We refer to our response to the Call for Evidence as attached for our detailed points on the options for a single rate or dual rate model. On a practical note, DAC Beachcroft also has

[2] For example the Barclays Equity Gilt Study 2022

significant concerns about the impact if different jurisdictions in the UK decided to apply different options for the discount rate model. This would create serious confusion and delay in the settlement of claims. DAC Beachcroft would urge the Department of Justice to work together with the Ministry of Justice and Scottish Ministers to ensure that a consensus is reached as to the preferred option, whether that be a single or dual rate model, to be chosen to apply across all jurisdictions.

DAC Beachcroft's Claims Solutions Group and Clinical Risk Group's response to the Ministry of Justice's Call for Evidence – Personal Injury Discount rate: Exploring the option of a dual/multiple rate.

DAC Beachcroft's Claims Solutions Group provides general insurance claims litigation and claims handling services to insurers in England, Wales, Scotland and Northern Ireland. As part of DAC Beachcroft LLP which services Scotland, Ireland and global markets, we have more than 500 insurance professionals and act for all of the top 20 UK general insurers and have expertise and experience across the entire sector. Our long history of commitment to, and investment in, the insurance sector means that we have an unrivalled depth of experience and breadth of insight. Our claims business reacts quickly to the dynamic claims industry and the changing needs of our clients whilst providing a local service with the support of a global network.

Our team has a deserved market-leading reputation for providing innovative and pragmatic solutions to liability claims disputes of all types and insurance issues generally. We pride ourselves on delivering commercial, value-driven legal services. With specialist expertise covering catastrophic injury, claims validation, costs, credit hire, disease and safety, health and environment law, the team covers the full range of personal injury work. Our strategic Advisory team offers a unique service for insurers dealing with emerging and important market issues.

DAC Beachcroft's Clinical Risk Group are the leading provider of legal services to the healthcare sector in England and are proud to have advised the NHS since its inception. We act for almost all of the major compensators in this field.

Executive Summary

- We do not consider that now is the right time to determine whether a dual or single rate is appropriate in order to ensure that claimants are neither over nor under-compensated. That can only be done at the point in time that a decision is being taken on the rate/rates during the review period. The answer will depend very much on what the economic forecasts are at the time.

- There are a range of pre-conditions that we consider need to be met before it is possible to determine whether a dual or single rate will achieve the most appropriate outcome.

- We are defining the appropriate outcome as the rate(s) that meets the requirements of the Civil Liability Act 2018 and ensure that there is no over or under-compensation on a broad brush basis. Any artificial quest for precision will undoubtedly lead to the wrong outcome.

- While we do not wish to comment at this point on whether a single or dual rate would lead to the most appropriate outcome, we do highlight that different rates for different heads of loss would never lead to an appropriate outcome. It is far more likely to

create inequitable outcomes. The same could be said of different rates where there is a PPO.

Question 1: Do you have a preferred model for a dual/multiple rate system based on any of the international examples set out in the Call for Evidence paper (or based on your or your organisations experience of operating in other jurisdictions)? Please give reasons with accompanying data and/or evidence.

1.1 We have seen and agree the ABI's response on this question. As part of our discussions with clients and colleagues in formulating this response it has become clear that there is significant confusion as to what each model means. We have therefore set out in response to this question how we are defining each model.

1.2 While the Call for Evidence itself refers to how versions of these models are applied in different jurisdictions, we do not accept that those versions are necessarily the right versions. We would highlight that when first introduced in Ontario, the switched rate model applied created significant confusion and the statute needed to be amended to clarify parliament's intentions.

1.3 Should a decision be taken to apply a dual rate, it will be vital that the process decided on is clear and understandable and we suggest, with a view to avoiding confusion, detailed worked examples should be provided alongside any announcement.

1.4 **Switched Dual Rate Model:** all damages within the short term period have a short term discount rate applied; all damages for the period beyond the short term period have a long term rate applied for all years including those years before the switching point. Assuming a switching point of 10 years and a duration of 25 years: short term rate is applied for the first 10 years of losses; for the 11th to 25th years, the long-term rate is applied for 11 to 25 years as appropriate.

1.5 **Stepped Dual Rate Model:** where the duration of damages is for a total period of less than the short term, then those damages are discounted by the short term rate in their entirety. Where the duration of damages exceeds the short term, then the damages will be discounted by the long term rate in their entirety.

1.6 **Blended Dual Rate Model:** use of a blended average of the discount rates which would have been applicable under the Switched Dual Rate Model. Damages for the short term period have a short term discount rate applied. Where the duration continues beyond the short term period, the long term rate will apply, but the short term rate will also continue to apply to the period up to the switching point. Assuming a switching point of 10 years and a duration of 25 years: short term rate is applied for first 10 years; in the 11th year, the short-term rate applies to the first 10 parts and the long term rate to the 11th part etc.

<u>Question 2: What do you consider to be the main strengths and weaknesses of the dual/multiple rate systems found for setting the discount rate in other jurisdictions?</u>

2.1 We have seen and agree the ABI's response to this question, but make the following additional observations.

2.2 Certainty and stability are key aspects in applying the personal injury discount rate (PIDR) successfully as part of the wider negotiation of settlement of a personal injury claim. A rate should be set that allows for appropriate outcomes to be reached and the application of the PIDR should not build uncertainty into the settlement process. That does not work to anyone's benefit; claimant and defendant alike.

2.3 There are also key considerations as set out in the Civil Liability Act 2018 (CLA) that must be taken into account when considering whether a dual or single rate will achieve the appropriate outcome:

(2)The Lord Chancellor must make the rate determination on the basis that the rate of return should be the rate that, in the opinion of the Lord Chancellor, a recipient of relevant damages could reasonably be expected to achieve if the recipient invested the relevant damages for the purpose of securing that—

(a)the relevant damages would meet the losses and costs for which they are awarded;

(b)the relevant damages would meet those losses and costs at the time or times when they fall to be met by the relevant damages; and

(c)the relevant damages would be exhausted at the end of the period for which they are awarded.

(3)In making the rate determination as required by sub-paragraph (2), the Lord Chancellor must make the following assumptions—

(a)the assumption that the relevant damages are payable in a lump sum (rather than under an order for periodical payments);

(b)the assumption that the recipient of the relevant damages is properly advised on the investment of the relevant damages;

(c)the assumption that the recipient of the relevant damages invests the relevant damages in a diversified portfolio of investments;

(d)the assumption that the relevant damages are invested using an approach that involves—

(i)more risk than a very low level of risk, but

(ii)less risk than would ordinarily be accepted by a prudent and properly advised individual investor who has different financial aims.

…..

(5)In making the rate determination as required by sub-paragraph (2), the Lord Chancellor must—

(a)have regard to the actual returns that are available to investors;

(b)have regard to the actual investments made by investors of relevant damages; and

(c)make such allowances for taxation, inflation and investment management costs as the Lord Chancellor thinks appropriate.

2.4 Whether these considerations and assumptions are best met by a dual or single rate will need to be at the heart of determining which should be applied. Many of these factors can only be determined at the point in time when the review is taking place by reference to contemporaneous economic forecasts.

2.5 It is however possible at this stage to highlight the benefits and flaws in the proposed dual / multiple rate systems that have been set out in the Call for Evidence.

Switched Rate

2.6 A switched rate based on duration can accommodate those with short life expectancies, allowing them to better ensure that they can meet costs at the they time they fall due to be paid. It equally allows for a higher rate to be set for the long term losses and ensures that over-compensation for those with longer life expectancy is properly addressed, without disadvantaging those with a shorter life expectancy.

2.7 One possible disadvantage of the switched rate is that it creates more uncertainty around settlement as it adds a layer of complication into the settlement process. It is certainly not so complicated that a properly advised claimant could not understand the process and agree settlement of their claim. Exploitation is however a concern and it may be that a switched rate process will lead to some claimants trying artificially to front load losses such that they will fall within the short term rather than long term rate. Furthermore, gaming of this sort may might unintentionally affect the choice of whether to take a PPO.

2.8 Certainty is key. In Ontario where a switched rate model is currently used, the long term rate has remained unchanged since it was originally set. This is to be expected given the investment horizon that this rate covers. The shorter term rate is however quite volatile having changed 16 times already. This is largely as a result of the methodology applied to fixing the short term rate. In our view, while the short term rate does need to be reviewed, there should be no need to it to change with such regularity (see comments in response to question 7).

Stepped Rate

2.9 This is in effect 2 single rates where duration is the key to which rate is to be applied.

2.10 This process has many of the same advantages as the switched rate, but may not work as well to ensure that the claimant is neither over nor under-compensated.

2.11 This is the method now applied in Jersey, where the short term rate of 0.5% will be applied in any case where the losses are for less than 21 years and the long term rate of 1.8% in any case where the losses are for 21 years or longer.

2.12 This does create a cliff edge, such that a claimant with a, say, 25 year loss would have the long term rate applied to the entirety of the damages. For a claimant with a significantly longer period of loss this may not create an issue, it does mean that a claimant with that 25 year loss could be under-compensated as they do not have the benefit of the short term rate in the way that is allowed for under the switched rate model.

Blended Rate

2.13 This model does not work well in our view. Whilst it has the benefit of smoothing cliff edges, that benefit is significantly outweighed by the likelihood of over-compensation of claimants.

2.14 The model also does not reflect actual investment management practice which would take a different approach across the short term and long term investment horizon but would not mix the short term effects into the long term period in the way that a blended rate proposes. Applying a blended rate would therefore not meet the assumptions required by the Civil Liability Act.

Multiple Rates

2.15 In our view, multiple rates would serve to increase uncertainty and to create issues around settlement of claims. The likelihood of gaming that has been referred to above is exacerbated in a system that includes multiple rates. We see no benefit to such a system (over and above a dual switched rate model) and significant disadvantages fuelled by the complexity of the system that would drive behaviours and lead to unintended consequences.

Different rates for different heads of loss

2.16 This system is in use in the Republic of Ireland where, despite the limited difference between the rates, it creates disputes around which rate applies to which heads of loss and undermines the ability to resolve cases as effectively as would otherwise

be the case.

2.17 Over time all heads of loss in a case will have a fluctuating correlation. On a broad brush basis, this will work to ensure appropriate outcomes. Seeking to apply a more precise approach to the correct index for different heads of loss will only work to fuel debate as to the appropriate indices to apply. If, for example, a general rate were to be applied for all earnings related losses, this would undoubtedly fuel argument as to whether the appropriate index had been applied when considering that individual claimant's earnings. This seriously undermines the parties' ability to negotiate settlement and will require courts to determine the correct outcome based on expert evidence. This would push us back to a pre-Damages Act scenario.

2.18 Claimants already have a basis available to them on which they can split out losses, where they do not consider that the discount rate adequately allows for their losses to be met, in periodical payment orders (PPOs). The very limited uptake of PPOs outside of NHS claims might suggest that there is no need for losses to be split out in this way.

Single Rate

2.19 The current rate has many layers of over-prudence built into it. The approach adopted by GAD in their 2019 report was, in our view, over-prudent in the approach to several factors.

2.20 GAD started with a portfolio of assets that was on the more cautious end of the range of appropriate portfolios. GAD then applied an ESG calculator that built in a further layer of caution in respect of equities which does not reflect a real world approach, especially when considered across longer time periods. This is quite clear when compared against the market reports which the ABI referred GAD to in their response to the Call for Evidence in 2019.

Table 14: Median asset class return simulations (in excess of CPI)

Median money weighted real return % pa in excess of CPI	5 years	10 years	15 years	20 years	30 years	40 years	50 years
Nominal gilts	-2.8%	-2.2%	-1.9%	-1.5%	-0.9%	-0.4%	-0.1%
Index-linked gilts	-3.3%	-3.2%	-2.7%	-2.2%	-1.3%	-0.8%	-0.4%
Investment grade credit	-0.1%	-0.4%	-0.2%	0.0%	0.4%	0.8%	1.1%
UK equities	2.2%	2.6%	2.8%	2.9%	3.0%	3.0%	3.1%
Overseas equities	2.6%	2.9%	3.0%	3.1%	3.2%	3.3%	3.4%
Cash	-1.2%	-0.9%	-0.6%	-0.4%	0.0%	0.2%	0.4%

2.21 This table is taken from the 2019 GAD report. The notes to that table state:

*Making regular withdrawals from a fund can have a significant impact on the effective returns achieved – for example, making a significant withdrawal from the fund following an early fall in asset values will hinder an investment manager's ability to recover the fund in subsequent periods. In technical terms – this is essentially the difference between Time-Weighted Rates of Return (which ignore withdrawals from the fund) and Money-Weighted Rates of Return (which are affected by withdrawals and additions to the fund)**. We are assuming that the assumed claimant included in this analysis has to finance regular withdrawals from the fund in order to meet their needs. As a result, the risk of withdrawals following a period of low returns is a significant risk. As such, references to projected returns in this report allow for the specified assumed withdrawals from the fund and the table below shows the median annualised effective real return achieved on key asset classes that will be modelled.** *These returns are real (in excess of CPI) and assume that regular withdrawals are made from a fund that is solely invested in a representative broad index for each asset class.*

For example, if the entire fund were invested in UK equities and used to provide regular CPI-linked damages over a 30 year period then the median effective real return is CPI+3.0% pa. Or equivalently, a PI discount rate of CPI+3.0% pa with an assumed investment strategy of 100% UK equities would result in the median level of over/under[1]compensation of 0%21 . Assets with higher returns also have higher risk. As a result, although a claimant would expect to benefit from investing in an asset with a higher expected return they are also increasing the probability of experiencing poor returns and hence incurring poor outcomes.

2.22 We have added our own emphasis to the section that demonstrates that over-prudence has been built in to GAD's calculations here. In 2019 GAD's table shows an increase in equity returns of just 7% over the 20 to 50 year period. The Barclays Equity Gilt Study 2022 (67th Ed.) for the same period shows an increase of 69%. GAD should make use of market studies like this one to ensure that the simulations they apply reflect a more real world outcome.

FIGURE 1. **Real investment returns by asset class (% pa)**

	2021	10 years	20 years	50 years	122 years*
Equities	9.8	4.7	2.9	4.9	4.9
Gilts	-12.6	1.0	2.4	3.0	1.3
Corporate Bonds	-10.0	3.1	2.3		
Index-Linked	-3.1	2.5	3.2		
Cash	-7.0	-2.5	-1.1	0.9	0.6

Note: * Entire sample.
Source: Barclays Research

2.23 GAD also adopted a historic approach when considering inflation which it was hard to understand as every other aspect of the calculation was considered by reference to forecasts. Our own view at the time, having obtained advice from economic experts at the time was that had forecasts been considered rather than historic analysis applied, the correct rate of inflation would have been CPI + 0.5% rather than CPI + 1% as adopted by GAD.

2.24 Overall, the rate as calculated by GAD placed too much emphasis on short term economic factors which taken together with the points above meant that GAD having built in a significant amount of over-prudence, proposed a rate of +0.25% which would allow a 50/50 prospect of full compensation.

2.25 When considering the report, the then Lord Chancellor decided to skew the outcome further in favour of claimants, setting the discount rate at minus 0.25% on the basis that this rate meant that 2/3 of claimants would receive full compensation.

2.26 This of course means that the prospects of a claimant being over-compensated are significantly higher than they would have been at a +0.25% rate. "Full" compensation should mean that a claimant is not over-compensated just as much as it means that they should not be under-compensated. This is very clear when the assumptions set out in the Act are considered.

2.27 As we have noted above, it is not yet clear whether a single rate or a dual rate is the appropriate outcome. It is however clear that whether a single or dual rate is adopted, the various levels of over-prudence should be addressed and not built into the calculations.

Pre-conditions

2.28 There are a number of preconditions that we consider need to be met before it becomes clear whether a dual (switched by duration) or single rate lead to the appropriate outcome.

2.29 For the dual rate to be acceptable the following preconditions should be met:

1. The mechanism is simple and certain
2. The two rates are set by reference to date of losses, with one rate for short term losses and another for long term losses
3. The switching point is at a maximum of 15 years to best reflect real world investment practice (or a minimum of 10 years to reflect economic cycles)
4. The long term rate properly reflects the returns on long term investments
5. No account is taken of short term volatility in setting the long term rate
6. No account is taken of any extra margin for prudence in setting the long term rate
7. It is accepted that the setting of a separate rate for short term losses itself removes some of the need for a margin of prudence

8. The short term rate is not factored into the rate for losses beyond the switching point
9. The long term rate is set on the basis that it is unlikely to change (accepting that the statutory mechanism requires a review every 5 years)

2.30 For the single rate to be acceptable the following preconditions should be met:

1. Short term economic factors should not be taken into account
2. The rate set should properly reflect returns on investment over a 43 year duration
3. An appropriate indexation for inflation should be applied based on forecasts rather than historic outcomes
4. The position of those with short term losses should not be given too much weight
5. The margins of prudence noted above should be factored out

Question 3: What do you consider is the optimal point for the switch-over from a short to a long-term rate on a duration-based dual rate model?
Please give reasons with accompanying data.

Question 4: What would you consider an absolute minimum and maximum point for the switch-over between two rates to be?
Please give reasons.

3/4.1 We have seen and agree the ABI's response to these questions, but make the following observations.

3/4.2 In our view a switching point should match actual investment practice. Whilst this may vary among practitioners, it is our understanding that a long term investment horizon is usually considered to be for a period of 15 years or more. This also matches with the period applied in the Ontario switched rate model.

3/4.3 As such we advocate, if a dual rate is deemed to be appropriate at all, that the maximum point for the switch-over should be 15 years.

3/4.4 As a minimum we agree with the ABI that there is no benefit in a short term rate of less than 5 years. Based on maximum economic cycle periods of 10 years, we would endorse the position that the minimum point for the switch-over should be 10 years.

Question 5: If a dual rate system were to be introduced, would you advocate it was established on the basis of the duration of the claim with a switchover point, on duration based on length of claim or its heads of loss (or a combination of the two)?
Please give reasons for your choice.

5.1 We have seen and agree the ABI's response to this question, but make the following observations.

5.2 If a dual rate is to be applied then a rate linked to duration is to be preferred to a rate linked to heads of loss. Any rate linked to heads of loss must be driven by an artificial quest for precision that will undoubtedly create difficulty in settling cases and increase the burden on the courts who will need to resolve disputes between the parties on the issue of the correct rate of indexation and which losses are covered by which rate. A broad brush approach to setting a rate (which would apply in a dual rate by duration or in a single rate) should be the preferred option as it is more likely to lead to the appropriate outcome.

5.3 For dual rates the preferred option should be a rate linked to duration with a switching point at 10 to 15 years (see above). As long as the preconditions for such an option as detailed in response to questions 1 and 2 are met, we would support such an option.

Question 6: In dealing with volatility of markets over the short-term is it a reasonable assumption that short-term rates in a duration-based system should be more variable and set at a lower rate; and long-term rates more stable and set at a higher rate?
If you agree or disagree that this assumption is reasonable, please say why.

Question 7: If short-term rates are more volatile, should frequency of review be increased?
Please explain your reasoning.

6/7.1 We have seen and agree the ABI's response to these questions, but make the following observations.

6/7.2 What is quite clear is that any long term rate should be set by reference to a long term investment horizon and as such should be stable. A long term rate should not be expected to change with any frequency.

6/7.3 A shorter term rate could well have greater volatility than a long term rate, and the fact that it will is a reasonable assumption to be made. However, if the switching point is to be in the range of 10 to 15 years (as we say is appropriate), it should not need to be reviewed any more regularly than the 5 years that the Civil Liability Act allows for. There is a real need for certainty and stability and to seek to ensure that awards neither over nor under-compensate claimants. Even a short term rate must be appropriate for the horizon for which it is set.

6/7.4 Any rate that is set as a reaction to short term economic events will undoubtedly

either over or under-compensate claimants.

Question 8: What would you regard as the advantages of a dual/multiple rate system?

Question 9: What would you regard as the disadvantages of a dual/multiple rate system?

8/9.1 We refer to our response to questions 1 and 2.

Question 10: What do you consider would be the specific effects on implementing and administering the discount rate if a dual/multiple rate is introduced?

Question 11: In addition to specific effects, do you consider there will be additional consequences as a result of implementing a dual/multiple rate?
Please give reasons with accompanying data/evidence if possible.

Question 12: If a dual/multiple PIDR were to be introduced would it be helpful to provide a lead in period to prepare processes, prepare IT changes etc. and if so, how long should this be?
Please provide reasons for your answer.

10-12.1 We have seen and agree with the ABI's response to these questions.

Question 13: What do you consider would be the effects of a dual/multiple rate on a claimant's investment behaviour and what would this mean for the design of a model investment portfolio?

13.1 We have seen and agree the ABI's response to this question and make the following additional observations.

13.2 We do not have details of claimant investment behaviour. However, it seems unlikely that moving to a dual rate by duration would significantly affect such behaviour.

13.3 Investment practice would already usually take account of short term (up to 15 years) and long term (over 15 years) needs and account for those differently, ensuring for example that there was sufficient in cash assets to meet the investor's needs in the earlier years.

13.4 Any investment portfolio for the short term would undoubtedly take less advantage of equities, whereas a long term investment portfolio would have a higher percentage of equities to take advantage of the greater returns that such investments generate when compared to other asset classes.

13.5 Any move to a rate by head of loss would not reflect investment practice. Investors

do not separate their funds in this way.

Question 14: What do you think would be the effects of a dual/multiple rate on drawing up assumptions for tax and expenses when setting the discount rate?

14.1 We have seen and agree the ABI's response to this question and make the following additional observations.

14.2 Most claimants have no other taxable income and therefore their tax liabilities are at most negligible. In the short term, risk of significant changes to the tax regime are unlikely and those with short life expectancy are very unlikely to have other sources of income available to them. Those with longer life expectancy are still unlikely to have other sources of income available to them, but will also most likely adopt tax wrappers and other methods to minimise their tax liabilities.

14.3 The position on tax should be considered alongside the assumptions in the Civil Liability Act. Overall where a claimant's risk appetite is low, the tax risk is likely to remain low. The tax risk may increase where a claimant has a higher risk appetite, but the assumption should remain that the risk appetite is low.

14.4 The position on expenses should similarly be considered against the assumptions in the Act. For a short term investor, expenses will be low given the investment horizon. However, even with longer term low risk investors, the expenses should remain low as there is little need for active asset management. Where there is active asset management there should be greater returns, but that will be because a claimant has adopted a higher risk appetite than the Act allows for.

Question 15: What do you consider would be the effects of a dual/multiple rate on analysing inflationary pressures and trends when setting the discount rate?

15.1 We have seen and agree the ABI's response.

Question 16: What do you consider would be the effects on claimant outcomes of a dual/multiple rate being adopted for setting the discount rate?

16.1 As we have noted above, it is not clear as yet whether a single or dual rate should be adopted, and this will not become clear until the review starts and consideration is given to economic forecasts at the relevant time.

16.2 Once it is determined, based on the prevailing conditions, which rate would best meet the principle of full compensation and neither under nor over-compensate claimants, then it will become clearer what type of rate should be adopted.

16.3 We have set out in response to questions 1 and 2 what we consider to be the issues with the various dual and multiple rate models. It should be noted that claimants will always be legally represented and have access to financial advice.

As such there should be limited impact on them as they should be properly advised.

16.4 The impact on claimants will be most relevant if a model is selected that undermines certainty in the process to the extent that it delays settlement and requires more cases to go to court for determination.

Question 17: If a dual/multiple rate was adopted would it be possible to return to a single rate in future reviews, or would a move be too confusing and complex and seen as irrevocable?
Please give reasons.

17.1 We have seen and agree the ABI's response to this question.

Question 18: What do you consider the respective advantages and disadvantages of adopting multiple rates would be, when compared with either a single rate, or dual rate.

18.1 See response to questions 1 and 2.

Question 19: If a heads of loss approach were adopted, what heads of loss should be subject to separate rates – care and care management costs, future earnings losses, accommodation, or any other categories?

19.1 We have seen and agree the ABI's response to this question, but make the following observations.

19.2 As we have stated above, we do not see any basis on which a separate heads of loss approach would lead to appropriate outcomes.

19.3 As has already been seen in Ireland (where the rates are split between future care and other losses) disputes can then arise as to which rate applies to which heads of loss – so for example disputes can arise around which is the correct rate for other earnings related losses. Further disputes would undoubtedly arise around the correct level of indexation for earnings based awards.

19.4 Separate rates for different heads of loss will undermine certainty which is a key component to settling these claims. Were the Lord Chancellor minded to adopt this approach then consideration should be given to limiting such an approach to (1) care and (2) all other heads of loss, as in Ireland.

Question 20: Introducing a dual/multiple PIDR could result in increased levels of complexity for both compensators and claimants. Do you agree with the assumption that this complexity will stabilise and ease once the sector adapts to the new process? Please give reasons.

20.1 We have seen and agree the ABI's response to this question, but make the

following observations.

20.2 Whether the complexity will stabilise will depend very much of the type of rate that is proposed.

20.3 As we have noted above, separate rates for different heads of loss will undoubtedly lead to disputes on both sides and will drive rather than reduce complexity. We do not see any basis on which such an outcome would stabilise over time.

20.4 As long as the model selected does not of itself drive the complexities, then we consider that complexities arising as a result of a change to a dual rate, should stabilise once the sector has adapted to the new process.

Question 21: The Government remains interested in exploring the use of PPOs in relation to high value personal injury settlements. We would therefore welcome any submissions, data and/or evidence stakeholders may have in relation to the effective use of PPOs.

21.1 We have seen and agree the ABI's response to this question and make the following additional observations.

21.2 The current discount rate is very attractive to claimants and as such the use of PPOs is now extremely low in the insurance industry. However, we recognise that for other compensators such as NHS Resolution there is higher take-up of PPOs by certain groups of claimants such as catastrophically injured children, for whom the security of a guaranteed annual sum can be attractive.

21.3 The Rules already in place around PPOs are effective and a claimant that wants a PPO will be able to have one unless the court decides it is clearly not appropriate in the circumstances.

21.4 There are many reasons why claimants don't want PPOs, including a desire to leave a legacy to their family. All claimants will have financial advice on the appropriate form of their award prior to settlement. Defendants do not have sight of that advice, but where required to approve the form of the award the courts do have that advice.

21.5 Given that claimants are properly advised; have access to PPOs should they wish them; and the Rules are adequate to allow a court to award a PPO in circumstances where it is in the claimant's best interests, there must be other factors at work as to why use of PPOs remains low outside of NHS claims.

21.6 It is not clear what those factors are, but they are likely to be multi-faceted and may be driven by no more than a seriously injured claimant's desire for some control over their own future.

Question 22: Do you agree that using a higher PIDR to calculate the real rate of return in settlements which include a PPO element would result in a more appropriate way to adjust nominal investment returns for future inflation? Please give reasons.

22.1 We agree entirely with the ABI's stance on this question.

22.2 The starting point for setting the discount rate within the statutory framework must be that the mechanism has to be broad brush, simple and workable in practice. That is made clear in the Call for Evidence where it is noted that: *In summary, the PIDR offers a relatively straightforward and simple way of avoiding complex and costly litigation as to what the adjustment to a damages award to reflect its investment should be in individual cases.*

22.3 Paragraphs 112 to 121 in the Call for Evidence contain suggested approaches which are far from simple and workable. We have set out above why any approach which seeks to set different discount rates for different heads of loss is unworkable and based on theoretical assumptions rather than practical considerations. The heads of loss premise underlies the ideas set out in paragraphs 112 to 121 and therefore the same points apply.

22.4 Paragraphs 119 and 120 in particular raise a different and novel idea: that in some way the discount rate should vary by reference to the type of award made. It is far from clear that this would be permitted by the Act. The Act allows for different rates as follows:

(3)An order under subsection (1) may prescribe different rates of return for different classes of case.
(4)An order under subsection (1) may in particular distinguish between classes of case by reference to—

(a)the description of future pecuniary loss involved;

(b)the length of the period during which future pecuniary loss is expected to occur;

(c)the time when future pecuniary loss is expected to occur.

22.5 It is clear from this that different rates of return may be set for different classes of case by reference to the nature and duration of the loss or the timing of that loss – but not by reference to the method of payment of the compensation. The idea that a different class of case could be defined by reference to the method of payment of the appropriate level of compensation is therefore a complex one – and as is conceded in paragraph 120, the approach might have to vary depending on what exactly was included in the PPO. The level of uncertainty generated by trying to fit this provision to every conceivable variation will make it much more difficult for both sides to agree settlement.

22.6 The MoJ also needs to consider the effect on claimants of setting the discount rate in this way. PPO uptake by claimants is already very low, due in large part to the level of

the current discount rate. As soon as a claimant is told that by taking a PPO, the discount rate applied to the rest of their damages will be higher (and therefore the level of their remaining lump sum damages will be lower), the natural reaction of any claimant will be to decline this option.

22.7 DAC Beachcroft, like the ABI, is concerned that the contents of paragraphs 112 to 121 demonstrate once more a quest for an artificial degree of precision in a process which is and has to remain broad brush and one in most cases for negotiation of an agreed settlement.

Question 23: What impact would a dual/multiple rate system have on protected characteristic groups, as defined in the Equality Act 2010?

23.1 The discount rate is typically only used in cases of more serious injury likely to lead to lasting disability. Accordingly, many of the claimants affected by the current level of the rate or by any change to the PIDR/model are, by their nature, likely to be considered as disabled. For the purposes of equality impact assessment, all claimants affected should be considered equally.

DAC Beachcroft Claims Solution Group and Clinical Risks Group
11 April 2023

Response to Department of Justice Correspondence 31st May 2023, PIDR Stakeholder Letter

The method for calculating the PIDR is set out for Northern Ireland in Schedule C1 to the 1996 Act. The DoJ invites comment and evidence upon whether adjustments are merited to the factors taken into account namely:

- the make-up of the notional portfolio (as laid out in paragraph 12 of Schedule C1);
- the assumed period of investment (currently 43 years);
- the impact of inflation (currently allowed for by reference to the retail prices index); and,
- the standard adjustments that must be made by the rate-assessor to a rate of return (currently set at 0.75%, which represents the impact of taxation and the costs of investment advice and management; and 0.5%, which is the further margin involved in relation to the rate of return).

Comment:

The make-up of the notional portfolio (as laid out in paragraph 12 of Schedule C1);

It is not possible to provide significant comment upon this issue as there is a distinct lack of evidence and analysis of plaintiff investment of awards.

In general, however, the following is of note, lump sum settlements for catastrophic injury claims already require a degree of measured risk in assuming investment returns. Further, it is important to note that the 'lower risk investor' model adopted in England and Wales is much less likely to generate over-compensation as opposed to the NI portfolio which is highly risk-averse and creates a significant disparity between compensation awards within the jurisdictions. This is further exacerbated when one considers the significantly higher rate of general damage awards within Northern Ireland when compared to the other jurisdictions.

The assumed period of investment (currently 43 years);

It is considered that adjustment is not required to the current period of investment in NI.

The impact of inflation (currently allowed for by reference to the retail prices index); and,

Reconsideration to this factor is encouraged. RPI has been dropped as an official National Statistic. It is generally accepted that RPI is considered a very poor measure of general inflation, with the Office of National Statistics noting it to at times greatly over estimate changes in prices and how these prices are experienced.

The standard adjustments that must be made by the rate-assessor to a rate of return (currently set at 0.75%, which represents the impact of taxation and the costs of investment advice and management; and 0.5%, which is the further margin involved in relation to the rate of return).

It is notable that Plaintiffs are generally low-risk investors and, as such, are unlikely to require ongoing or significant investment advice and management. It is arguable, therefore, that the current rate leads to overcompensation of Plaintiffs where investments are not under such envisaged active management.

The further application of 0.5% is not warranted and once again may well lead to overcompensation of plaintiffs in Northern Ireland as opposed to England and Wales.

DoJ has further sought comment upon whether single or multiple rates should apply and, if multiple, views on a preferred model.

A firm view on preferences between a single rate or dual rate model is impossible in the abstract.

Obviously, however, there are multiple advantages to a single rate approach for parties and the courts. As referred to in the Ministry of Justice's recent call for evidence a single rate 'provides a degree of certainty on the level of damages that may be awarded and forms a basis for negotiations between parties to reach settlements in cases.' Whereas there are merited concerns than multiple rates would be more likely to extend or cause additional disputes, delays and costs.

Any adopted model should not be overly complicated, should be accessible and provide clarity to all parties as to the outcome. Further information would be welcomed from the DoJ as to the anticipated proposed models, as was offered in the Ministry of Justice's call for evidence, to allow for meaningful consideration.

Caoimhe Connolly
Assistant Chief Legal Adviser (Acting)
Directorate of Legal Services
BSO
11th July 2023

From the Director of Primary Care

Department of
Health
An Roinn Sláinte
Männystrie O Poustie
www.health-ni.gov.uk

Email: Gearoid.Cassidy@health-ni.gov.uk

By email to:

Date: 17th August 2023

Andrew Dawson
Department of Justice

Email: Andrew.Dawson@justice-ni.gov.uk

Dear Andrew

REVIEW OF THE PERSONAL INJURY DISCOUNT RATE (PIDR)

Thank you for your emails of 26th July and 3rd August confirming that DoH will be able to contribute to the PIDR review process and extending the opportunity to feed into the current mini call for evidence.

DoH Finance and policy colleagues have reviewed the submission made by DLS to the mini call for evidence and are content to endorse their analysis.

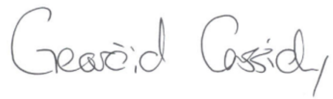
We support DLS's view that the current rate heightens the risk of overcompensation to plaintiffs given its reliance on a highly risk averse investment portfolio model and the application of the 'further margin'. Whilst we recognise that the PIDR must be fair to individuals who have experienced clinical negligence, the rate's calibration must also guard against the risk of overcompensation.

Given the constrained financial resources which are available for public service provision currently, it is of particular importance that the rate does not inadvertently lean towards overcompensation of individuals to the detriment of public service provision for the population of Northern Ireland as a whole.

In terms of DLS's position on whether a single or dual rate model is appropriate, we share DLS's view that any adopted model should not be overly complicated, should be accessible and provide clarity to all parties as to the outcome. We would similarly welcome additional information as to the potential models under consideration.

We hope that the information above is helpful and we welcome DoJ's commitment to ensure that DoH is fully engaged in the preparatory work for the Rate review going forward.

Yours sincerely



GEARÓID CASSIDY
Director of Primary Care

cc: Brigitte Worth
Fiona White
John Millar

2023 review of the Personal Injury Discount Rate (PIDR) in Scotland and Northern Ireland

About Us

FOCIS members act for seriously injured Claimants with complex personal injury and clinical negligence claims, including group actions. The objectives of FOCIS are to:-

1. Promote high standards of representation of Claimant personal injury and medical negligence clients;

2. Share knowledge and information among members of the Forum;

3. Further better understanding in the wider community of issues which arise for those who suffer serious injury;

4. Use members' expertise to promote improvements to the legal process and to inform debate;

5. Develop fellowship among members.

See further www.focis.org.uk

Membership of FOCIS is intended to be at the most senior level of the profession, currently standing at 24 members. The only formal requirement for membership of FOCIS is that members should have achieved a pre-eminence in their personal injury field. Seven of the past presidents of APIL are members or Emeritus members of FOCIS. Firms represented by FOCIS members include:

Anthony Gold	Hugh James
Switalskis	JMW
Ashtons Legal	Irwin Mitchell
Balfour + Manson	Leigh Day
Bolt Burdon Kemp	Moore Barlow
Dean Wilson	Osbornes Law
Digby Brown	
Fieldfisher	Serious Law
Fletchers	Slater and Gordon
Freeths	Stewarts
Hodge Jones & Allen	Thompsons NI

In line with the remit of our organisation, we restrict our responses relating to our members' experience, practices and procedures relating to complex injury claims only. We will defer to others to respond on the impact relating to other classes of case.

1. **Are the defined investment portfolios for Scotland and Northern Ireland an appropriate assumed level of investment risk for seriously injured claimants with significant future loss?**

FOCIS remains of the view that the mixed investment portfolios in Scotland and Northern Ireland are composed of an excessive amount of risk-based assets which means they cannot be said to be low-risk for the average claimant[1] with a significant future loss claim. Such claimants will by definition have long-term and often disabling injuries, that often reduce or end their earning capacity, and entail medical and care related needs the long-term provision for which they cannot afford to risk. We agree with the 2015 expert panel report[2] on the Discount Rate commissioned by the Ministry of Justice which concluded that any truly low-risk portfolio would require at least 75% investment in Index-Linked Government Security (ILGS), with the remaining 25% invested between UK corporate bonds, global government inflation-linked bonds and global equities; and that any other asset classes present an unacceptable level of risk.

As set out in the Damages Act 1996 (the 1996 Act) at Schedules B1(12) and C1(12), the Scottish and Northern Irish notional investment portfolios are the same, with only 10% invested in ILGS and 15% in nominal gilts. The English approach goes further and contains 42.5% growth assets, which are defined as assets "expected to generate higher returns over the longer term but at greater risk."[3] Our view is that the Northern Irish and Scottish portfolios are more appropriate than the English portfolios, however they still involve more risk than we believe claimant's should be assumed and obliged to take. The experience of our members and of the professional deputies and trustees who they work with is that most claimants with significant injuries will leave far in excess of the 10% assumed in the Schedules to the 1996 Act in a bank or building society, especially in the early years. Further, claimants may be required to spend significant sums on adaptations to their accommodation before investing the remainder. Therefore, the amount of the future loss claim ultimately invested is significantly less than the total amount awarded with many of those investments delayed for some years. Consequently, a significant proportion of the future damages award will not generate any investment return at all.

Comparable issues of long-term investment risk arise in the context of pension funds. Table 7.2 of the Purple Book 2022[4] shows that the proportion of defined benefit assets held in equities has continued to decrease and has been approximately 19% in the last two years. Yet in practice, most of the equities are held by open and/or immature funds. Table 7.9 demonstrates that the proportion of equities held against liabilities which are 75-100% pensioners (which is more comparable to a Claimant's portfolio) is about 7%. On average, the duration of these sorts of pensioner liabilities might be on 15 to 20 years, which is broadly in line with the 2015 MOJ experts' Portfolio 2 and distinctly less risky than any of the portfolios proposed by GAD in the 2019 Call for Evidence. It is also less risky than either of the defined investment portfolios of Scotland and Northern Ireland. There is no logical or fair reason why individual seriously injured claimants should be required to take more risk than the trustees of pension funds, many of which have the additional comfort of an employer covenant.

The expert IFA, Richard Cropper[5], has made the powerful observation that *"every long run ends with a short run"*. His persuasive point is that just as it is appropriate to assume a less risk-based investment portfolio for shorter periods the same applies towards the end of a longer

[1] We use the term claimant throughout this document, but this should also be read to include post-issue pursuers in Scotland

[2] Page 109: https://consult.justice.gov.uk/digital-communications/discount-rate/results/discount-rate-report.pdf

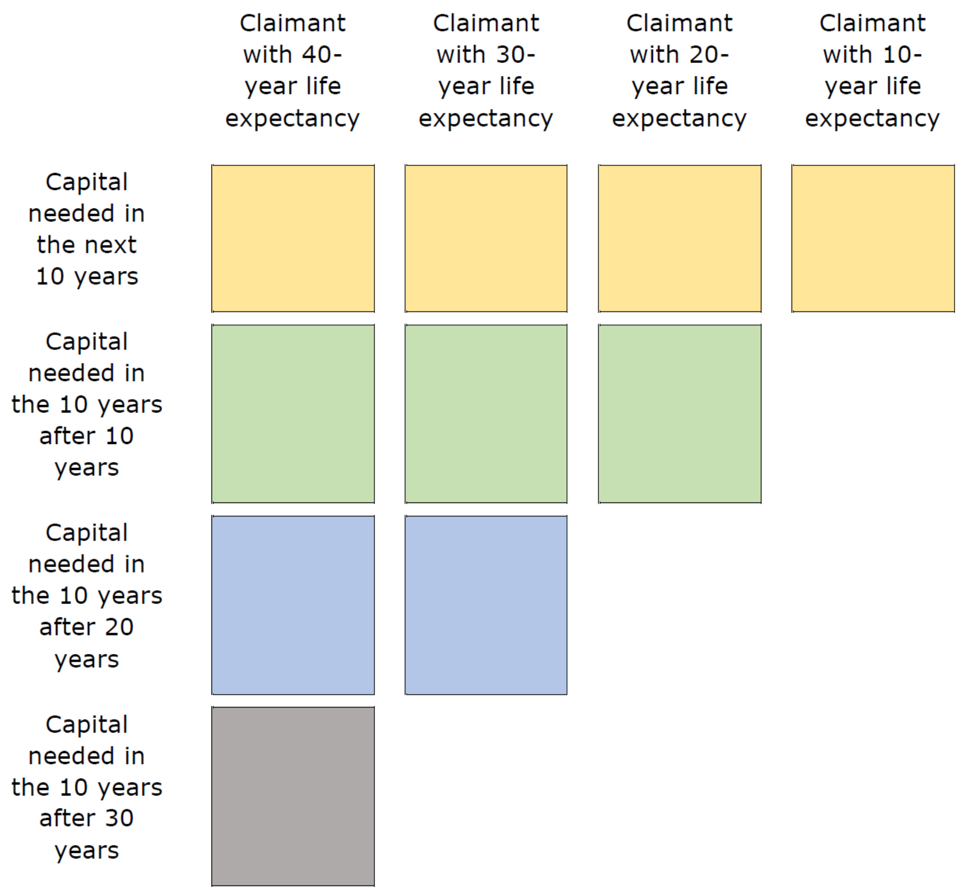
[3] Page 41: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/817236/Setting_the_Personal_Injury_Discount_Rate__web_.pdf

[4] Published by the Pension Protection Fund in December 2022

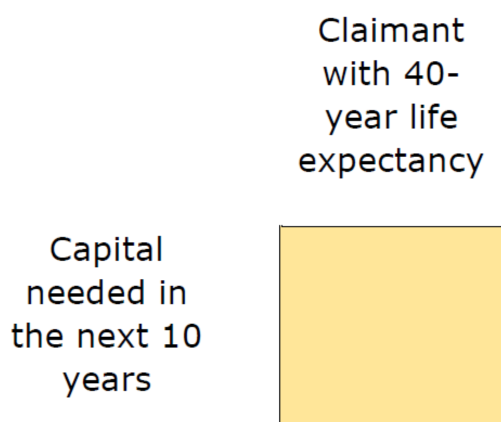
[5] Who is also a Member of the Ogden Working Party.

period. Seriously injured claimants in their later years cannot afford the risk of a down-turn in investments, which forces disinvestment to cash from even low risk investments. Their reduced 'capacity for loss' leaves them less likely to be able to meet their needs which may at the same time be increasing with the impact of ageing. They and their advisers also must plan for the more than 50/50 chance they will outlive their life expectancy.

Richard Cropper's helpfully prepared the following the illustrate the point:



After another 10 years, which is now within 10 years of the life expectancy of claimants originally projected as having a 40 year life expectancy, all the remaining capital is held on 'no risk' (yellow) basis.



One can see from the above that the only investment colour the claimant holds through every decade is the 'yellow', no risk, investment. The 'grey' investments are only held for 25% of the claimant's life expectancy.

Turning to the defined investment portfolios versus the discretion of the English Lord Chancellor to make their own decision regarding low-risk investment portfolios. Our view is that the method/decision of determining the defined investment portfolio, as in calculating the discount rate, should be depoliticized. It is clear that on each occasion that a discount rate adjustment has been contemplated in Northern Ireland, Scotland, England, and Wales the relevant minister has been reliant on the Government Actuary to calculate what that rate should be. Taking the responsibility away from the Department of Justice is preferred, which would entail amendments to sections 8, 15, 16 of Schedule C1 of the 1996 Act. Having a formula pre-determined by legislation and empowering government actuaries to review and implement the revised rate creates transparency which is important for all personal injury claimants in Northern Ireland. This has been recognised by the role given to the Government Actuary in Scotland in Schedule B1 of the 1996 Act. We believe that a similar approach should be taken to the defined investment portfolios. We also think that it would be wise at the time the PIDR is reviewed to convene a panel of experts to advise on the defined investment portfolios and whether they are low risk; our view is that they should be sufficiently low risk so as to have a 90+% probability of ensuring that the claimant's compensation meets their future needs.

2. **What is the appropriate measure of inflation for the future losses of seriously injured claimants?**

Inflation is a very important aspect of setting a fair discount rate as was acknowledged by the House of Lords in Wells v Wells when determining the previous approach of setting the rate by index linked government securities. The subsequent legislation in Scotland, Northern Ireland and England was primarily focussed on considerations of investment risk and was not intended to increase the risk of the compensation of seriously injured claimants being eroded by inflation and hence not lasting to meet their long-term needs. In England the Civil Liability Act 2018 changed the method for setting the PIDR. Although not prescribed by the CLA, RPI was no longer a 'national statistic'. The Lord Chancellor on advice from an expert panel, including the Government Actuary, decides what inflationary measure is used when setting the PIDR. When it was set in 2019, the Government Actuary believed it was reasonable to assume for damage inflation of CPI+1% pa. He also said:- "*.The appropriate level of inflation to assume is likely to vary significantly between claimants and between different components of their awards,*

depending on their needs. As such, alternative views are plausible and the decision on damages inflation should be taken in the round with other factors."[6]

In practice, the differences between the RPI and CPI +1% are small and in our view, it is a balanced, reasonable approach, for the reasons set out below. Claimants' damages are invested often over decades, and it is therefore appropriate to look at long-term economic trends and to not focus on the more recent spikes in CPI, which have certainly bucked the trend of recent years.

Claimants' costs are expected to rise over time owing to inflationary pressures, and this increase will vary depending on the head of loss. For example, consumer costs (e.g., buying goods and services) may be best measured with reference to a prices index, while care costs and loss of future earnings will be subject to earnings inflation, linked to earnings growth and hence are best tracked by earnings inflation indices (like ASHE 6115/6145/6146 for care). On closer inspection, however, those heads of loss that are, at first blush subject to price rather than earnings inflation require additional factors to be taken into account and which we think justify the additional +1% to CPI.

As has been repeatedly accepted by the courts, care and care management costs are subject to earnings growth and over the medium-to-long-term they can be expected to rise at a rate in excess of prices inflation. It is by far the largest head of loss in most serious injury claims and often accounts for well over half of the total award of damages.

Taking the other major heads of future loss in turn, loss of earnings is a head of loss which demonstrably rises in line with earnings inflation. It would be surprising if any reputable expert economist would argue otherwise and defendant's experts in the common law jurisdiction cases in which this point has featured have not even attempted such an argument. It was accepted by the Privy Council in Helmot v Simon[7] and by the Courts of Appeal in Bermuda (Thomson v Colonial Insurance)[8] and Ireland (Russell v HSE)[9]. Any argument to the contrary would be departing from full compensation and would relegate seriously injured claimants to a dwindling standard of living when compared with their 'but for' position.

Another major head of loss for seriously injured claimants is future medical treatment and therapies. Most of this head of loss is earnings-related and historically, inflation is on average materially higher than CPI.

Another major head of loss of is for disability aids and equipment. Whilst this predominantly relates to purchasing goods, the majority of disability aids and equipment are low production specialist equipment, of types which are not included in the CPI basket and are not subject to a large competitive market for goods. This means that producers will need to recoup significant research and product development costs across a relatively small number of customers. A key example of this is the comparative cost of a prosthetic knee. The cost has more than doubled (131%) in 25 years, whilst CPI inflation has increased by 78%. Likewise, the associated fees of the treating prosthetist have also risen at CPI +1%. The position for a lower limb amputee Claimant who was compensated in 1998 is even starker than that, as most of them will have subsequently been prescribed more recent models of prosthetic and now incur costs that are 200-500% more than that assumed by the calculation of their future loss claim[10].

[6] Setting the Personal Injury Discount Rate Government Actuary's advice to the Lord Chancellor 2019, paragraph 8.10

[7] Helmot v Simon [2012] UKPC 5

[8] Thomson v Colonial Insurance Company Limited [2016] CA (Bda) 6 Civ

[9] Gill Russell (A Minor) v HSE [2015] IECA 236

[10] Figures provided by Richard Nieveen, expert prosthetist.

For example, the cost of a C-Leg (a prosthetic knee) in 1998 was £12,150, and the cost of the same prosthetic today is £28,000. That is a cost increase of 130.5%. However, in the meantime many claimants who were originally prescribed a C-Leg and received compensation on that assumption have now switched to a more recently released model; the Genium which costs £66,345. The price increase between the cost of a C-Leg in 1998 and the cost of a Genuim in 2023 is a staggering 446%. As this example shows, when compared to the increase in CPI since 1998 (77.67%), it is clear that setting the PIDR based on the indexation of CPI alone would be woefully insufficient. The increase in CPI+1% over the same period is 129.58%, which is almost exactly in line with the increase in cost of a C-Leg, so would be adequate if one ignored the technological advancement and resultant higher (but unanticipated) costs now born by claimants who have switched to the Genium leg. It is also interesting to note the increase in the associated prosthetists costs. Whilst we do not have data from 1998, the increase in costs (using the example of prosthetist fees associated with a transfemoral socket) since 2006 is 142%. This is almost double the percentage increase of CPI but is again much closer to the increase in CPI+1%. See the comparison in the graph below. This evidence supports our suggestion that indexation by CPI+1% is more consistent with the rise in cost of many items of specialist disability related needs and therefore will ensure better alignment with the full compensation principle. In addition, the change in needs consequent to technological advancement is, like the longevity risk, a real-world factor. Whilst we acknowledge that losses are calculated on the basis of the known needs as of the date of the final award, this phenomenon should be born in mind when making a broad-brush adjustments to the PIDR to minimise the risk of under-compensation.

A further major head of claim for seriously injured claimants is housing costs. The impact of underlying inflation assumptions regarding this head of loss are, for the most part, negligible. Most funds are quickly spent on purchasing and adapting a property to suit the claimants' needs, and therefore there is no significant balance left to invest. The Supreme Court relatively recently reconsidered the law relating to compensating future accommodation expenses in *Swift v Carpenter* [2020] EWCA Civ 1295 and the court set a methodology for calculating the lump sum compensation based on the Claimant's remaining life expectancy and the set value of a reversionary interest in the property. The PIDR therefore no longer has any direct bearing on this head of loss

The cost of a professional guardian (Scotland) or a solicitor acting as a controller (Northern Ireland) can be a significant head of loss for claimants who lack mental capacity. This is an earnings-related cost as it mainly relates to the cost of time spent by that professional (in most cases, a solicitor). Consequently, in cases where periodical payments terms are agreed for this head of loss, they are usually indexed to the appropriate category of ASHE or RPI[11], and never to CPI.

To conclude, in serious injury claims the proportion of future losses that are subject to earnings related inflation is typically around 70% or more. It is well established, and recognised by the periodical payment regime, that earnings inflation in the long term rises at an average of at least 1.5% more than prices inflation. In the Scottish legislation, that factor was acknowledged and resulted in RPI being selected; in English legislation, an allowance for damages inflation of 1% above CPI was made. Our contention is that RPI is the minimum acceptable inflationary adjustment and if the alternative CPI (or CPIH which has in the last 10 years been a close match for CPI but not RPI) were to be contemplated it would then require an adjustment of at least +1% as in England.

[11] Which historically has been equivalent to CPI (or CPIH) +1% but over the last couple of years has been more than 2.5% a year in excess of CPI (and CPIH).

3. **In calculating the net real rate of return what is a fair allowance for investment charges and tax incurred by seriously injured clients in Scotland and Northern Ireland?**

Investment charges faced by claimants in Scotland and Northern Ireland are broadly the same as those faced by claimants in England. However, our Scottish and Northern Irish members have explained that their clients do rely more on smaller, regional IFAs who charge higher rates than average. We contend that the arguments and evidence submitted by FOCIS in our responses to the 2018 and 2023 MOJ calls for evidence regarding investment charges and tax are likewise applicable – if not even more so – to Scotland and Northern Ireland.

As part of our 2019 response to the 2018 Call for Evidence and at the request of the MOJ and GAD we sought data via FOCIS members and the professional deputies and trustees they engaged concerning investment charges incurred in relation to investments for their seriously injured clients. We collated and submitted a data set, which related to the investment portfolios of 389 clients provided by 9 different firms ranging in size between £67,336 and £7,450,000. The average total charge incurred across all 389 cases was 1.58%. The FOCIS data clearly demonstrated that an overwhelming majority, of 64.3%, of the 389 portfolios incurred investment charges of 1.5% and above (including 6.4% in excess of 2%). In comparison, only a tiny minority of Claimants (4.9%) incurred charges below 1% and only 35.7% of the portfolios incurred charges of 1.5% and below. Furthermore, when looking solely at the 169 portfolios whose value falls below £1.5m, 74% portfolios incurred charges between 1.5% and 2.0%, only 12.5% incurred lower charges and 13.6% incurred charges of 2% or more.

Similarly, in their response to the 2023 call for evidence, Irwin Mitchell's Court of Protection team analysed investment charges over 953 portfolios collected from 22 providers, which showed average fees of 1.51%. This is very similar to the above 2019 FOCIS data set. Collectively this is a compelling body of evidence that actual investment charges faced by claimants are circa 1.5%.

For this response, one of our Scottish members' firms, collated a dataset concerning investment charges incurred in relation to investments for their seriously injured clients. Given the relatively short period between the 31 May 2023 announcement and the 11 July deadline for responding to this call for evidence, the dataset is smaller than the above, but we think it is instructive. The dataset relates to the investment portfolios of 22 clients ranging in size from £340,000 and £4,000,000. The average total charge incurred across the 22 portfolios was 1.76%. Further, the dataset showed that 15 portfolios (68.18% of the total) all incurred charges of 1.85%. No portfolios incurred charges below 1% and only 2 portfolios (9.09% of the total) incurred charges below 1.5%. All of the cases involved active management as the needs of each individual client vary, and detailed discussions about risk and required return are therefore vitally important. As we outlined in the opening paragraph to this section, our Scottish and Northern Irish members explained that their clients rely on smaller, regional IFAs that charge higher than average rates; we believe this data reflects that observation.

In light of this evidence the current allowance in Scotland, Northern Ireland and England of just 0.75% for the combination of investment changes and tax is, we contend, far too low. That allowance was at the low end of the range (0.6%-1.7%) identified by GAD and was premised on passive management of a static portfolio. Both of those assumptions do not reflect the necessary behaviour of the vast majority of seriously injured claimants who need an actively managed portfolio that varies during their lifetime to reflect changes in their needs as they age and the economic environment.

The vast majority of claimants with significant future losses incur charges of circa 1.5% per annum (England & Wales) or circa 1.76% (Scotland) in investment management charges and that those charges are not and cannot be included in the damages claim and so do not feature in the damages award. Once the further allowance for capital gains and income tax liabilities is

made, we contend that a composite reduction in the discount rate of at least 2% is required, prior to factoring in a further adjustment for longevity and other risks.

In their submission for the 2018 Call for Evidence, Richard Cropper and Ian Gunn[12] of Personal Financial Planning ("PFP") indicated that "The financial climate is dynamic and constantly changing: constant reappraisal of plans is therefore necessary in order to ensure that Claimants have the best opportunity to meet their expected cash flow needs, taking account of their need to take risk (including the discount rate applied to their lump sum) and their ability and willingness to do so."

Enquiries within FOCIS and the investment professionals who work with their clients revealed that the primary aim of investment advisers is almost always to devise an investment strategy based on meeting the client's need for their lifetime (including the longevity risk). This requires regular review and reappraisal. Some funds may have an element of 'active' management in so far as a professional may need to review the portfolio bi-annually or annually, at a cost and undertake any necessary re- alignment. The charges revealed by this data would not have been incurred unless they were necessary to maximise the prospects of the investments lasting to meet the client's needs.

In addition to investment charges, another factor to consider is taxation. As taxation is inherently individual, two claimants receiving the same awards will have differing personal, financial and familial backgrounds that affect the amount of tax they pay. We do not have any data on taxation rates. We note the example (premised on a single PIDR) given by Christopher Daykin[13] in his 2019 Call for Evidence response that "In a recent large compensation case involving investment of the damages in the UK, the impact of taxation on some proposed portfolios amounted to a reduction in the discount rate of ½% to ¾%".

We contend that the PIDR ought to be rounded down by at least 0.5% to allow for taxation. We suspect that the tax adjustment on a dual or multiple rate (see further below) ought to be at or above that level. For short-term investments that will be heavily weighted in tax it is likely the interest earned will be immediately taxable as income, but this may be counter balanced by lower investment management charges.

The GAD's 2019 report considered the impact of taxation on a range of size of awards, however the highest was £3million, whereas many claims are far in excess of that sum. In the interest of brevity, we set out only a few of the tax changes that have recently come into force and some of those that are planned for the future. From 2023/24 tax year the additional rate tax bracket will be reduced from £150,000 to £125,140, meaning those with taxable income above £125,140, will pay an additional 5% in tax compared to the current tax year. From the 2023/24 tax year, the Capital Gains Tax (CGT) annual exemption is being reduced to £6,000, and will be further reduced to £3,000 from the 2024/25 tax year. As such any gains realised above these exemptions will be subject to tax at the individual's marginal rate. From the 2023/24 tax year, the dividend allowance will also reduce from £2,000 to £1,000, and further reduced to £500 from the 2024/25 tax year. In short, a basic rate income tax paying claimant will be paying a greater level of tax in future years. In 2023/24 their tax liability would increase by 18%, and in 2024/25 their tax liability would increase by 27% compared to the current 2022/23 tax year. There is some evidence that the investment charges reduce as a percentage of the award for very large awards (e.g. £3 million+). However, those larger awards are most likely to incur higher incidence of tax. Consequently, we contend that a composite reduction to the discount rate to allow for both investment management and taxation ought to be at least 2%.

[12] IFAs with significant experience and specialisation in advising seriously injured claimants who were appointed by the MOJ as experts for their 2015 report. Richard Cropper is also a member of the Ogden Working Party.

[13] Expert actuary, former Head of GAD and member of the Ogden Working Party.

We refer to APIL's submission to this call for evidence, which sets out in detail arguments relating to the impact of Scotland's tax regime; FOCIS agrees with the points made by APIL and will therefore not repeat them here.

4. The assumed average period of loss/investment

A significant proportion of claimants that FOCIS members represent have impaired life expectancies and, in our view, an assumed period of investment of 30 years is more reflective of the average than 43 years. We remain sceptical of the data underpinning the assumed period of investment of 43 years as it remains unpublished. Obviously, the output of the Economic Scenario Generator (ESG) modelling is very sensitive to both the data inputted as well as the assumptions made. Although the evidential basis is unknown at present, if, for example, the data relied on includes *all* injury claimants – the vast majority of whom do not have any significant or long term future loss claims nor an impaired life expectancy – then those claimants with catastrophic injuries/impaired life expectancies/future loss claims are being significantly and unjustly impacted and, ultimately, may be undercompensated.

It is vitally important in the interest of transparency that the underlying data and assumptions are published, particularly given that 43 years is a considerable period of time to assume as applicable to the average claimant. It is a period that would clearly be inapplicable to any claimant who was already over 45 years of age, or whose life expectancy has been significantly compromised by severely disabling injuries. There is a significant proportion minority of claimants with life expectancy of less than 30 years, and the rate should not undercompensate those claimants

Of course, every case varies as to its facts including in relation to life expectancy and in reality, the investment advisor and their client must plan for outliving the impaired life expectancy or they run the risk of compensation running out before the end of the claimant's life. This presents additional risk and impacts on investment decisions as further explained in the following section.

5. The 0.5% adjustment to reduce under compensation (as prescribed in the Scottish and NI Acts)

The 0.5% adjustments are absolutely necessary to reduce the percentage of claimants who are under-compensated. But they do not go far enough to achieve the often-repeated commitment to the full compensation principle. The compensation of circa 35% of claimants was likely to run out before the end of their lives, based on the GAD modelling of the assumptions[14] underlying the 2019 PIDR. Such a large proportion of claimants being under compensated is simply inconsistent with the claimed of a maintaining a full compensation regime. Additionally, a further 22% would suffer a shortfall in their damages of 10% or more, which could leave claimants unable to fund their care and equipment needs for four years or more. This is particularly concerning when one considers that in the later years of a claimant's life, they will, consequent to the compounding effects of ageing on their injuries, likely need increased care and equipment. We were pleased to note that the thrust of this concern was acknowledged by the Government Actuary's Department (GAD), the Lord Chancellor and in the legislation passed in Scotland and Northern Ireland, but our view is that the adjustment is too small to be sufficiently impactful. In the Bermuda case of *Thomson v Thomson and Colonial Insurance Company Limited*[15], at first instance in the Supreme Court of Bermuda, Chief Justice Kawaley observed at paragraph 38 that the case appeared to be the first occasion in which a common law court has been required to

[14] See the next section for our concerns around these assumptions adjustment to which could make significant differences to the proportion of claimants who are under compensated.

[15] Colonial Insurance Company Limited v Thomson (conjoined with Harvey v Warren) Court of Appeal for Bermuda CIVIL APPEAL No. 13 of 2015

consider the respective merits of an assumed investment of the entire lump sum to be awarded in ILGS as opposed to in a mixed basket of investments.

At paragraph 93 of the *Thomson* Judgment, it was observed that Mr Gorham, a Canadian Actuary whose expert evidence was relied upon by the Defendants:

"*…conceded under cross-examination by Mr. Harshaw that on his investment model between 50 and 33% of plaintiffs would not have sufficient funds. He viewed his approach as fair to both Claimants and defendants.*"

Chief Justice Kawaley commented:

"*I viewed his approach as a stunning dilution of the prevailing legal policy preference, in the future loss discount rate calculation context, for a hypothetical investment in an instrument likely to generate a risk-free rate of return.*"

We observe that an assumption that was considered by Chief Justice Kawaley to be a stunning dilution of the full compensation principle is very close to the assumed outcome of the -0.5% adjustment made by the Lord Chancellor in 2019 that, on rosier economic predictions than subsequently transpired, circa 35% of claimants would see their damages fund run out and so be under compensated.

At paragraph 100 in *Thomson*, Chief Justice Kawaley also made reference to the evidence of the Claimant's Actuary, Christopher Daykin, as follows:

"*As Mr. Daykin explained, institutional investors are able to safely invest in a wider range of investment instruments because they are investing on behalf of multiple ultimate investors whose needs to redeem their investments stretch out over multiple lifetimes. Such investors are also able to hedge against short-term risks in ways which are generally impossible for the typical individual personal injury Claimant. I find that there is a fundamental distinction between the investment goals of the hypothetical prudent investor, especially an institutional investor, (who is not investing sums received by way of compensation for tortious injury), and the investment goals of the hypothetical prudent plaintiff*."

The Bermuda Court of Appeal fully endorsed the Judgment of the Chief Justice. Bell JA commented at paragraph 23 that:

"*What Mr. Daykin was saying is essentially that Mr Gorham's theory of sufficiency demonstrated that, using his model, there is approximately a 50% chance of a Claimant receiving a fund sufficient to meet expenses and losses, with the other side of the coin being that 50% of Claimants would not have sufficient assets to do so. Consequently, Mr. Daykin concluded that these figures come nowhere near meeting the principle of full compensation which has been accepted over many years by the courts. What Mr. Daykin said in relation to the 90 to 95% figures was not that these represented over-compensation on the basis of the Chief Justice's ruling, but that if one were to test a model proposed in place of the Wells mechanism (as advocated by Mr Gorham), then there would have to be a demonstration that the payments were sufficient for the Claimants in at least 90 to 95% of cases in order to come close to providing full compensation*."

The concerns of the Chief Justice Kawaley regarding under compensation were shared by Irwin LJ in *Swift v Carpenter*[16]:

[16] [2020] EWCA Civ 1295

"The principles of law by which this Court are bound can be summarised in two propositions: firstly that a claimant injured by the fault of another is entitled to fair and reasonable, but not excessive compensation. Secondly, as a corollary of that fundamental principle, in relation to the head of claim with which we are concerned, the award of damages should seek so far as possible to avoid a 'windfall' to a claimant, or more realistically to his or her estate … if it were to prove impossible here to award a claimant full compensation without a degree of overcompensation, then it seems to me likely that the principle of fair and reasonable compensation for injury would be thought to take precedence."

Whilst institutional defendants like insurers and the NHS can offset any perceived over-compensation of some claimants against under-compensation of others, seriously injured claimants cannot play the numbers game. They only have one claim that they need to provide for their life-long injury related needs. Those with seriously disabling injuries will often be unable to work and will be very heavily reliant on their compensation without any other major source of finances.

An additional but related factor to consider is the longevity/mortality risk. As we mention above, investment advisors and their clients must plan for a scenario where they outlive their impaired life expectancy or run the risk of the compensation running out. In other words, in practice, investment advisors account for mortality risk when planning the investment of damages for which no such risk was taken into account. Ultimately, the burden rests unfairly on the claimant to try and bridge this gap.

Chris Daykin states that there is a significantly higher probability than 50% that people outlive their assumed life expectancy. He explains this point as follows :

"For a 30-year-old male the expectation of life on Ogden 8 is 55.5 years. However, the median future lifespan (for which there is a 50% chance of living longer and a 50% chance of not living so long) is 58.5 years to age 88.5, i.e. three years more. About 60% of a cohort of 30-year-old males will live longer than the expectation of life of 85.5.

The mode (the most likely age of death) is between 93 and 94, i.e. out of a cohort of 30 year old males, more will die between 93 and 94 than at any other age."

There are readily available statistics concerning longevity, and we contend that the GAD should factor them into any future analysis or modelling regarding the discount rate. To illustrate the point, if you look at the ONS statistics for a 20-year-old man in England & Wales their predicted life expectancy is to age 86, but there is a 25% chance they will live a further 10 years to 96. Pending the publication of any such modelling and recognising that calculating the impact of longevity has complexities, we propose that a contingency adjustment of 0.5% is applied to the discount rate. This adjustment could mitigate the longevity risk and the risk that funds are required in a different manner than when the award was granted. For the avoidance of doubt this is in addition to the existing margin adjustment of 0.5%, to "mitigate the broader risk of under-compensation."

6. Lack of transparency over the assumptions for the ESG

We remain concerned that there is a lack of transparency or understanding of the assumptions upon which the ESG calculates the assumed future returns on investments that have underpinned the discount rates set for Scotland, Northern Ireland and England. We would welcome a meeting with the Government Actuary to get a better understanding of these assumptions and for such detail to be put in the public domain with an invitation for comments on those assumptions.

7. Whether a single rate of PIDR is preferable to a dual/multiple rate by duration or by head of loss..

The legal systems of the vast majority of countries around the world favour a single PIDR, or to make life even simpler, no discount rate at all (claimants' future losses are just multiplied by the applicable number of years). FOCIS also favours a single PIDR approach. As part of FOCIS's response to the government of England & Wales's call for evidence 2023[17], our Chair[18] spoke to practitioners from countries where dual/multiple rate systems are in place.

Our Chair spoke with a committee from the Ontario Trial Lawyers Association (OTLA). They informed us that:

- It is standard practice for both parties to instruct an accountant or economists to calculate the multipliers and the future loss claims when preparing cases for trial. The lawyers on the call expressed the view that there was too much risk for them to attempt these calculations themselves as that could result in error and professional negligence claims. However, to explore settlement in the early stages of the case they may attempt their own rough and ready calculations.

- Annual reviews and frequent changes to the short-term rate cause delays to settlement and notably to the preparation of claims. The expert economist Dr Eli Katz made the point that if he was working as an expert on a case with the trial listed early in 2024, he would not be able to calculate the final schedule of loss until after the annual rate announcement in August (of each year). During the life cycle of a long running case, he may have to recalculate the multiplies several times. This adds cost and causes delay.

- Neither their PIDR nor Structured Settlement (akin to PPO) regimes provide a fair solution to address inflation of the claimants' lifetime losses. In cases in Ontario there are arguments about this issue, notably in relation to healthcare costs including arguments relating to the rapid rising costs consequent to technological improvements. They felt that the English regime for earnings inflation of PPOs was patently fairer and closer to full compensation than their structured settlements.

Alongside APIL our Chair also spoke to a group of experienced legal practitioners, including a former Judge of the High Court in-charge of the Personal Injuries List from Hong Kong who informed us that:

- The current triple rate in Hong Kong has not been challenged since Chan Pak Ting in 2013[5]. Mohan Bharwaney SC SBS[6] commented that probably means it no longer provides full compensation as the economic landscape has deteriorated. A party could try and challenge this through expert evidence but would need permission of the court and that has not yet been attempted. To do so would expose the Claimant to cost risk if they ran but lost the argument.
- For the first review under the current draft bill in Hong Kong they do not anticipate any change from their current triple rate (inc the short periods 1-5, 5-10 and 10+). Conceptually this could be considered, and changes proposed by their expert panel but (as under our CLA 18) they will not report until after the 1st review and before the 2nd review.
- Their stepped triple rate involves cliff edges and they agreed that could cause unfairness (e.g. a Claimant with an 11 year loss period (calculated at 2.5%) contrasted with up to 10 year loss (at 1%)).

[17] https://focis.org.uk/news

[18] Julian Chamberlayne, who is also the Risk and Funding Partner and Head of Aviation and International Injuries at Stewarts Law LLP. He has for many years been a commentator on the PIDR, notably through a series of articles in the New Law Journal.

- They do not have ILGS in HK which is one of the reasons they did not follow Wells v Wells. Nor do they have tax on interest income.
- Unlike the UK they do not think they have any significant long-term differential between prices and earnings inflation.
- They have an equivalent to the Ogden tables, known as the Chan tables, where you select a multiplier by combining the period of loss and the discount rate. This appears to be a simple table that makes no provision for switched or blended discount rates over the period in question.
- Similarly, where a period of loss (or expenses) would only start at a point of time in the future (say 6 years from judgment) which will continue for a period (say 4 years), there may be a debate on whether the -0.5% PIDR or 1% PIDR should be applied. Again, this argument can be resolved by resorting to first principle (i.e. the duration of time available for the damages awarded by way of lump sum to generate income).

In 2019, Jersey rushed through legislation to introduce a dual rate by duration, with highly questionable assumptions on investment returns. The consequence is that both the short-term and long-term rates are too high to provide anything close to full compensation to claimants. Their dual rates also have a cliff edge that is likely to produce inequitable results for claimants falling just the wrong side of the 20-year dividing line between their short and long-term rates. We illustrate the cliff-edge phenomenon with an example, the term-certain multiplier for a duration of 19 years, for which a discount rate of 0.5% per annum, real and net, applies is 18.13, whereas the term-certain multiplier for a duration of 21 years, for which a discount rate of 1.8% per annum, real and net, applies is (unfairly) lower at 17.51.

Our reservation in moving to a dual/multiple rate system is evidenced by the experience in Ontario, Hong Kong, and Jersey. In Ontario, after over a 20-year experiment with a dual-rate system, they are considering returning to a single PIDR. In 2020 and again in 2021, a very experienced sub-committee of their Civil Rules committee submitted detailed reports recommending a return to a single discount rate based on an average of yields from Government of Canada real return bonds (which are indexed to inflation).

<u>Duration of Loss – various approaches</u>

FOCIS considers that implementing a dual/multiple rate system by duration of loss will add complexity and cost. It also carries enhanced risk of unintended consequences which might well further deviate from the full compensation principle.

A Stepped Rate[19] which applies a rate depending on the overall duration of the loss would be likely to lead to unfairness for claimants with losses falling just beyond the switching point. That would encourage attempts at manipulation by claimants and defendants to frame losses which border the stepping point in the most favourable way (i.e., so that the duration claimed falls within a higher or lower rate). This artificial treatment of a claimant's identified losses would be an unfortunate departure from the actuarial approach, which we believe would lead to additional disputes (and therefore costs) between the parties. It is also unclear how the Stepped Rate methodology would compensate periodic losses, such as the regular purchase of equipment every say 3 years for the rest of a claimant's life. Where longer losses are split into smaller phases with varying levels of loss (e.g., where the level of the Claimant's lost earnings or care needs fluctuate) it is unclear whether the short-term rates could be applied to the early phases prior to the stepping point, with the long-term rates applicable after. Clearly if a Stepped Rate were introduced, careful guidance would need to be given on its application. However, given the complex and variable types of loss that make up a claim, attempting a complete rewrite of the

[19] Where the claimant was on either a short or long-term rate based on the award duration

current methodology is likely to lead to unintended consequences and additional litigation to clear up any ambiguity.

A Switched Rate[20] moderates the worst impact of a cliff-edge drop in the discount rate immediately after the switching point. However, this methodology adds in additional complexity with multiple rates needing to be split into smaller phases prior to, at and beyond the switching point.

The Blended Rate[21] would also avoid the cliff-edge in a way that might be fairer than a Switched Rate, but we anticipate that the period over which the short-term rate is blended/tapered to the long-term rate would need to be a set number of years, as to do so over the course of a Claimant's life would render it impossible to produce tables with the blending period built in. A manual calculation would be extremely complex and would necessitate the involvement of an expert.

General disadvantages of dual/multiple rates

The most significant disadvantage of changing to a dual or multiple rates by duration is that it is likely to assume a high level of positive net real return for claimants in the longer-term which is highly speculative. That creates further risks for seriously injured claimants, most of whom are highly reluctant and risk averse investors.

A shift to dual, let alone multiple, rates by duration would significantly increase complexity and may well require expert input from an actuary and/or forensic accountant, as FOCIS understands regularly occurs in Ontario, for example, where there exists a dual rate system with a 15-year switching point.

To give a sense of scale, a schedule of loss for a claimant with a spinal cord injury will often have ten or more heads of future loss including a vast array of equipment and assistive technology to be purchased at varying intervals in the future. In such a claim, the basic calculation of future losses under the current single PIDR involves the calculation of around 300 multipliers. Even adding one more step to the calculation of each item of future loss to cater for a dual rate by duration will add significant levels of complexity and cost to the production of the schedule. It also increases the risk of error.

Dual or multiple rates by duration do not address the inflationary issues and short-term rates would be much more heavily impacted by inflationary pressures. Also, frequent changes to the short-term rate cause delays to settlement and notably to the preparation of claims.

If there is to be a move from the simplicity of the current single PIDR to a dual rate, then of the options we are firmly of the view that a dual rate to reflect long-term earnings inflation on care and case management needs would be fairer and would not add any significant complexity to preparing schedules of loss. It is also conceptually very similar to PPO indexation. It is, for good reasons, the solution arrived at after careful consideration of the expert evidence, by the common law courts (including the Privy Council) and who were not ham strung by legislation e.g., Guernsey, Ireland, and Bermuda. However, we reiterate that our primary position is that it would be preferable to stick with the simplicity of the current single PIDR.

[20] The short-term rate applies initially but is switched if the duration exceeds the short-term period

[21] Where all periods before the switching point could be discounted at the short-term rate and any cashflows beyond this discounted further at the long-term rate, for each year after the switching point.

8. **Periodical Payments**

Schedule 2 of the Damages (Investment Returns and Periodical Payments) (Scotland) Bill 2019 has not yet been implemented. Accordingly at this time, PPOs are only ordered in Scotland where the parties are in agreement and make a request for such an order. Despite there being a statutory framework in place in Northern Ireland, PPOs are rarely used. At the current time, the vast majority of insurers are not offering periodical payments during settlement discussions in either Scotland or Northern Ireland. An increased utilisation of PPOs by insurers would, to an extent, reduce uncertainty for Claimants and reduce the impact of the risks inherent in managing and investing a lump sum. For the applicable heads of loss[22] PPOs remove the longevity risk as they last for the Claimant's life and be linked to the appropriate index to address real earnings growth.

NHSR and the MIB are notable exceptions in that they have from the outset endorsed the PPO regime and made PPO related offers in most claims involving serious lifetime losses. That in part is due to the funding of those organisations.

FOCIS have found in England and Wales that it is commonplace for insurers to attempt to force a lump sum settlement on a Claimant by making 'lump sum only' Part 36 offers, even though the Claimant had expressed a clear preference for a periodical payment package and/or has actually made offers themselves on that basis. It takes a brave Claimant to turn down a lump sum Part 36 offer purely on the basis that they would prefer a periodical payment if all other components of the offer may not be bettered at Court. Such lump sum Part 36 offers are usually a complete 'take it or leave it' package. This means the Claimant cannot choose to accept the underlying sub-components and can only go to Court on the form of award. However, the insurer in that scenario would then put the Claimant at risk of litigating all or most issues in the hope of bettering the Part 36 offer. This position exposes the Claimant to the full risks of what could be a 1, 2 or even 3-week trial. If the Claimant did not then better the offer the insurers had previously made during said trial, they may be faced with a costs order against them running into 6 figures. To avoid this problem occurring, the rules in Scotland governing Pursuer's Offers and Minutes of Tender, and those in Northern Ireland governing Lodgements, should be amended to require any offer to settle in cases involving significant injuries and future losses to be put on PPO terms as well.

According to the Institute and Faculty of Actuaries' latest research[23] on PPOs, the uptake of PPOs in personal injury claims is very low despite the change to the discount rate in 2019. The research indicated that against all cases valued over £1m[24], the weighted average PPO propensity for 2009-2020 is 24%, but has been just 5-12% in the years 2017-2020. Insurers report that the driving force behind the decision to have a PPO was overwhelmingly the claimant's preference (75%) and in only 24% of cases did the claimant and defendant have a shared preference for PPOs. In just 1% of cases a PPO was awarded by the court. It is understood that in Scotland and Northern Ireland, PPO's are not routinely ordered such that this information likely relates to the position in England and Wales, where, defendant insurer settlement behaviour appears to be a large factor behind the very low rates of PPOs for personal injury claims, which can readily be contrasted with the materially higher rate of PPOs for clinical negligence claims against the NHS.

The recent experience of our members is that most insurers still see lump sum settlement as their preferred (cheaper) option, undermining their claims that the current discount rate is unfair

[22] Most commonly care and case management only and never for all future losses so the discount rate remains relevant to the other heads of loss.

[23] Institute of Actuaries' 2021 report

[24] As of 2011, with this report and assuming 7% claims inflation from then onwards. We observe that is materially in excess of CPI+1%.

for them. Unless and until insurers proactively seek to settle the majority of cases on a PPO basis it is safe to assume that the current discount rate is too high.

Data from a YouGov poll commissioned by APIL suggests over 50% of respondents would prefer to receive some or all of their compensation in the form of a PPO should they be seriously injured as a result of someone else's actions. The poll also found that just 35% would prefer to receive compensation in a lump sum payment. APIL also conducted a survey of its members in 2020, which revealed that:

a. 88% said that, in their experience, insurers always or very frequently sought to undertake negotiations on a lump-sum only basis.

b. 82% said that insurers, in their experience, rarely or never proactively offer a PPO.

c. In stark contrast 79% found it easy to obtain a PPO from NHS Resolution.

We believe that more should be done to increase uptake of PPOs. There is a strong claimant appetite for PPOs, as evidenced by the polling mentioned above and the more extensive use of PPOs in cases involving NHSR[25] (and MIB).

In November 2022, the government published its response to the Solvency II consultation[26], which stated that it would ensure the risk margin is changed to reduce the risk margin for long-term life insurance business, including PPOs. It was hoped that this would make available substantial amounts of capital, safeguard against the risk margin becoming too large and too volatile during future periods of low interest rates and retain a risk margin that ensures that insurers hold sufficient assets to transfer their liabilities to another insurer if required. The changes may help insurers, but nowhere near enough to make a real difference. Claimants have a countervailing concern as to whether the paying insurer will remain solvent to keep making the periodical payments for the decades ahead. Despite this recent change, the experience of FOCIS members remains that most (but not all) insurers remain resistant to offering PPOs unless and until faced by a claimant who feels so strongly about the issue that they are prepared to reject a lump sum offer in the millions and press on towards a trial.

PPOs provide regular payments which enable seriously injured claimants to meet their needs, particularly in relation to care. In comparison to lump sums calculated using PIDR, PPOs remove from the claimant the very significant risks posed by:-

a. longevity;

b. inflation; and

c. tax.

The governments of Scotland, Northern Ireland and England should make it a policy objective to take steps to encourage the use of PPOs in appropriate cases, such as:

(1) requiring Pursuer's Offers, Minutes of Tender, or Lodgements in cases involving future care claims of greater than £500,000 to include a PPO variant, or detailed written explanation of why such an offer would not be possible or not be in the Claimant's best interests; and

[25] Data obtained by APIL through a FOI confirmed that 219 claims with a value of > £1.7 Million were settled by NHSR in 2019/2020, 160 (73%) of those were settled by PPO.

[26] https://www.gov.uk/government/consultations/solvency-ii-review-consultation

(2) pro-active case management by the courts of the PPO issue at an early stage in proceedings.

By contrast, the MOJ's 2023 Call for Evidence worryingly suggested consideration of a higher differential PIDR for cases involving a PPO. Such a move would discourage their use without any associated clear-cut policy benefit. We are unaware of any other jurisdiction in the world that has adopted such an approach.

In addition, it would also add further complexity. When drafting the schedule of loss and counter schedules, the parties would not know whether the court would award a PPO. The parties would have to produce variant calculations applying the standard and PPO variant PIDR for each item of claim. If combined with the suggestion of a dual rate by duration, then at least four variant calculations would be required for every item of future loss claim.

In any event the concept of a variant PIDR for PPO cases would appear to be contrary to s4(3)(a) of Sch A1 of CLA 2018 which mandates that in determining the rate the Lord Chancellor must assume that the relevant damages are payable as a lump sum (rather than under an order for periodical payments). Similar prescriptive clauses can be found at s18(b) in both Schedule A (Northern Ireland) and B (Scotland) of the Damages Act 1996.

The case for the governments to make policy decisions which encourage the use of PPOs is compelling, whereas the policy reasons and evidence for a dual rate are, at best, mixed. Any change to the PIDR that makes PPOs less attractive would be a serious backward step.

FOCIS[27]

[27] Lead author – Julian Chamberlayne assisted by James Philpott. Co-authors Oonagh McClure, Kim Leslie and David Short.

Informing Progress - Shaping the Future

FOIL Northern Ireland – Response to the Department of Justice Call for Evidence on the Personal Injury Discount Rate (May 2023)

This response is made on behalf of the Forum of Insurance Lawyers (FOIL) in respect of the above Call for Evidence. FOIL represents over 8,000 members across Northern Ireland, England, Wales, Scotland and the Republic of Ireland. It exists to provide a forum for communication and the exchange of information between lawyers acting predominantly or exclusively for insurance clients. This response has been compiled in consultation with FOIL Northern Ireland. FOIL has also submitted a separate response to the parallel Call for Evidence in Scotland.

The Call for Evidence asks for views and evidence on two related areas: (1) the method of calculating the Personal Injury Discount Rate (PIDR) in Northern Ireland under Schedule C1 of the Damages Act 1996; and (2) the options and preferences in terms of a single or multiple rate model for calculating the PIDR.

(1) The method for calculating the PIDR in Northern Ireland

The key points that FOIL wants to make can be summarised as follows:

a. The current framework and negative rate (-1.5%) are causing adverse financial and claims implications for a broad range of stakeholders.
b. The existing notional portfolio is too cautious and creates a framework for over-compensating Claimants.
c. The current framework causes economic distortions in the claims and insurance markets in Northern Ireland and in comparison to England, Wales and Scotland. **Appendix 1** highlights some of the discrepancies and financial burdens this creates for Defendants and compensators of claims. This exacerbates existing variables given the higher level of General Damages payable in Northern Ireland than elsewhere in the UK.
d. Often, the burden of over-compensation falls on those less able to bear the financial cost and/or risks the diversion of essential resources from public services:
    i. These additional claims burdens are adversely impacting the availability <u>and</u> cost of insurance in Northern Ireland.
    ii. Further, these burdens risk contracting the insurance market in Northern Ireland even further.
    iii. This environment may have adverse consequences for stakeholders, including Claimants if their claims are not covered by insurance, or if Defendants are unable to meet claims as a result of shortfalls or under-insurance.

The notional portfolio: the current portfolio is too risk-averse and the ‘lower risk investor’ model used in England and Wales would be preferable and less likely to generate over-compensation. The reliance on passive returns and an unchanging investment objective/portfolio are overly cautious

approaches. The portfolio is also cautious in terms of its equity spread (20% UK and overseas equities).[1] This overall approach is exacerbated by the use of an additional (0.5%) margin of prudence (see below).

Assumed period of investment: No change is required.

The impact of inflation and the use of RPI: a balanced and broad temporal view needs to be taken into account when assessing the impact of inflation. It would be unfair and artificial to fix the PIDR using a short-term temporal snapshot of inflation, especially given the application of any rate to future claims over an extended period. FOIL's view is that the RPI is not the best instrument for assessing the impact of inflation in this context given the current socio-economic volatility.

The standard adjustments: FOIL considers that the 0.5% margin of prudence is not warranted but if it is to be retained as a statutory adjustment, it should be modified to zero on the next review (Schedule C1, paras 10-11). It is an overly cautious adjustment (especially when combined with the existing notional portfolio) and is more likely to generate over-compensation in claims. Further, if a decision is made to use a dual or multiple rate option - to reduce the risk of over/under compensation - the case for the margin of prudence is weakened even further.

(2) Single or multiple rates?

FOIL agrees that the PIDR and any structural model for implementation should aim to achieve full (100%) compensation as far as is reasonably practicable. This will necessarily involve balancing the pursuit of full compensation against the complexity and cost of any solution, and the consideration of a range of factors including claims culture, behavioural practices and conceptual understanding of the discount rate process. Whilst it is appropriate to explore options to deliver fairer outcomes for the key stakeholders, sufficient time must be allowed for preparatory work, system change and training before any implementation deadline. This involves careful consideration of whether different options can be integrated within the claims process within the current review cycle provided by the Damages Act 1996. It also involves an examination of the broader costs associated with any change.

The Department of Justice Call for Evidence does not offer any specific options or models for Stakeholders to consider. FOIL offers the following summary of possible alternatives to the current single rate mechanism. The latest Ministry of Justice (England & Wales) Call for Evidence identified three basic options for a dual or multiple duration-based discount rate:[2]

i. **Stepped** - In essence, this is an either/or model – either a short-term discount rate applies to the whole of the future loss claim or a long-term rate does.
ii. **Switched** – The UK Government Actuary describes this option as *'all cashflows prior to the switching point could be discounted at the short-term PI discount rate and all cashflows after the switching point could be discounted at the long-term rate'*[3]
iii. **Blended** - The UK Government Actuary describes this option as *'all periods before the switching point could be discounted at the short-term PI discount rate and any cashflows beyond this discounted further at the long-term rate, for each year after the switching point.*

[1] The Government Actuary Department's (GAD) report to the Lord Chancellor in 2019 reviewing investment practices showed that a cautious, low risk portfolio would hold 32.5% of equities (Setting the Personal Injury Discount Rate, Government Actuary's Advice to the Lord Chancellor dated 25 June 2019).
[2] Minstry of Justice, Personal Injury Discount Rate: Exploring the option of a dual/multiple rate, Call for Evidence dated 17 January 2023
[3] GAD 2019 (Setting the Personal Injury Discount Rate, Government Actuary's Advice to the Lord Chancellor dated 25 June 2019)

For example, the claimant with a 16-year award would have the first 15 years of their damages discounted at the short-term rate ***and then the cashflow in the final 16th year discounted for 15 years at the short-term rate and one year at the long-term rate'***.[4] The blended model might be seen as just another example of a switched system, albeit with a different method of calculation.

FOIL considers that the Switched model has some advantages over the other duration-based options:

a. This option can generate more accurate outcomes for Claimants and Compensators and reduce the risk of 'cliff edges' at the switching point.
b. It would limit the unfairness, adverse behavioural practices, gaming and delay that is likely to arise with an either/or Stepped option.
c. It is a simpler mechanism to apply and understand than the complex Blended option. The Blended option is likely to generate higher legal advice costs than the Switched option.
d. The implications for stakeholder comprehension arising from the increased complexity of the 'Switched' mechanism should be capable of management with appropriate legal and forensic expert advice. It is certainly easier to understand and explain than the Blended approach.
e. This option more closely aligns with the investments and returns that Claimants make in practice.

FOIL does not favour additional switching points (i.e., multiple options) because of the additional complexity this introduces to the claims process. We are not convinced that this would produce fairer outcomes for key stakeholders and would probably increase the duration of the claims journey.

FOIL does not favour the alternative Heads of Loss model - with different discount rates applicable to different categories of loss:

The **Heads of Loss** option caters for different inflationary rates for different heads of loss and might be relatively easy to implement in the short term. However, the option increases the likely incidence and persistence of disputes over categorisation and additional resulting costs. The idea that Claimants invest different heads of loss variably appears unrealistic in practice. Further, it does not address the problem that Claimants with short investment opportunities cannot achieve the same investment returns as those with a longer investment possibilities – meaning under compensation for those with short term loss periods. In these circumstances, it is FOIL's view that this option should be avoided.

[4] GAD 2019

The main disadvantages of each of these alternative approaches are summarised below:

Stepped	Blended	Switched	Heads of Loss
Claimants with losses beyond the short-term period are likely to have under compensation in the early years	High complexity issues	No account for short-term risk during the longer term	Under compensation for short-term loss periods
Creates unfairness for Claimants with losses around the switching point	Persistent complexity issues		Persistent complexity and incidence of categorisation disputes
Increases the prospects for adverse behavioural practices and adverse impacts on settlement negotiations	Increases the prospects for adverse behavioural practices and adverse impacts on settlement negotiations		Increases the prospects for adverse behavioural practices and adverse impacts on settlement negotiations
	Higher advice costs		Higher advice costs
	Involves false assumptions		Involves unrealistic investment assumptions

The key point that FOIL wants to make is that the discount rate, the model for setting the rate and any switching point are interdependent. It is artificial to consider any one element in the abstract when assessing the overriding goal of achieving fairer outcomes for stakeholders. At this stage, and in the abstract, FOIL is unable to offer a decisive case for a change from the existing model in Northern Ireland.

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Appendix 1[5]

20 year-old male with £100k per annum ongoing loss

Discount rate	**Annual Loss**	**Multiplier**	**Claim (£)**	**Impact of the NI -1.50% rate**
-1.50% (NI)	£100K	117.78	11,778,000	
-0.75% (Scotland)	£100K	87.19	8,719,000	35% higher than in Scotland
-0.25% (E&W)	£100K	72.46	7,246,000	62.5% higher than in E&W

40 year-old male with 100k per annum ongoing loss

Discount rate	**Annual Loss**	**Multiplier**	**Claim (£)**	**Impact of the NI -1.50% rate**
-1.50% (NI)	£100K	66.32	6,632,000	
-0.75% (Scotland)	£100K	54.10	5,410,000	22.5% higher than in Scotland
-0.25% (E&W)	£100K	47.63	4,763,000	39.2% higher than in E&W

60 year-old male with 100k per annum ongoing loss

Discount rate	**Annual Loss**	**Multiplier**	**Claim (£)**	**Impact of the NI -1.50% rate**
-1.50% (NI)	£100K	31.10	3,110,000	
-0.75% (Scotland)	£100K	27.67	2,767,000	12.3% higher than in Scotland
-0.25% (E&W)	£100K	25.68	2,568,000	21% higher than in E&W

[5] FOIL is grateful to Nora Tallon at Harbinson Mulholland for these examples.

Institute and Faculty of Actuaries

14 July 2023

Northern Ireland Department of Justice Personal Injury Discount Rate Review

IFoA Response

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide and oversee their education at all stages of qualification and development throughout their careers.

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the Northern Ireland Department of Justice letter of 31 May 2023 on the review of the Personal Injury Discount Rate in Northern Ireland (PIDR NI). We are also reverting (with a similar response) to the equivalent letter of 31 May 2023 from colleagues in the Scottish Government. We hope both the Department of Justice and Scottish Government colleagues find our responses helpful.

2. As with our previous responses to relevant consultations on PIDRs, members of our General Insurance Standards and Consultations sub-Committee provided input to this response. Members of our sub-Committee have more than a decade's experience of working on personal injury claims.

3. The IFoA is clear that the needs of injured parties should be at the centre of any personal injury compensation paid. We also support the principle that settlements should aim to provide 100% compensation, but neither more, nor less. We note the aim of the PIDR NI is to avoid over- or under-compensation.

4. It is important to note that, as for any IFoA response, we have considered the PIDR review from an independent, public interest perspective. We have interpreted the public interest in this context to be the requirement to provide the claimant with 100% compensation.

5. The 31 May 2023 letter explains that the NI PIDR was set at -1.5% in March 2022, with the rate allowing for the following factors:

    i. the composition of a notional portfolio;
    ii. an investment period of 43 years;
    iii. the impact of inflation by reference to the Retail Prices Index (RPI); and
    iv. allowances for taxation, costs and a further margin adjustment.

6. The letter asks for views on the need or otherwise to adjust any of these factors and requests any evidence to support these views. Given the relatively short consultation window, we have focussed on the question over the need for review, although we also make some qualitative points which we hope are helpful.

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7. As you may be aware, the Ministry of Justice (MoJ) consulted on the pros and cons of a dual or multiple rate PIDR in England and Wales, and we responded to this consultation in April 2023. We include a link to that response below, but also reiterate some relevant key points from this, and note that a dual/ multiple PIDR impacts the operation of framework elements i. – iv. above.

8. As already mentioned, the IFoA supports the intention to achieve as close to 100% compensation as possible. We also believe the needs of the injured party should be central to any compensation paid, as their needs may be greatest. We note further that the investment needs of injured parties - and their attitude to risk - may differ from those of the wider population, as a result of suffering a life-changing injury. Our view is that the discount rate should be derived from a risk-free rate of return, reflecting the risk appetite of a risk-free investor. Lump sum settlements expose claimants to uncertainty over the adequacy of their compensation, and using a higher discount rate increases this risk.

9. We acknowledge however that the Damages (Return on Investment) Act (Northern Ireland) 2022 sets out the legislative basis for determining the PIDR NI, including the use of a representative investment portfolio to inform the setting of the rate. Our comments below therefore reflect our views on the need to adjust the framework for setting the PIDR NI, rather than revisiting earlier discussions on risk appetite/ risk-free rates of return.

10. **We are firmly of the view that elements within the PIDR NI framework should be reviewed given the significant change to the economic landscape since the rate was last set in March 2022**. This is particularly relevant to both the investment return derived from any notional portfolio (element i.) and inflation (element iii.) More generally, we support the need for reconsideration of the PIDR where it becomes clear that it is no longer reflective of the current/ future economic outlook, rather than maintaining current rates until the next due review date. Any approach to rate review should also however consider the need for stability in the PIDR.

11. We continue to support the use of a longer investment period (i.e. the 43 years used rather than the 30 years used in Scotland), in determining the PIDR. It is not uncommon for a lump sum settlement to be provided to claimants in their 20s and 30s, with a corresponding need for care for the rest of their lives. As touched on above, the use of an assumed investment term in any PIDR framework is potentially impacted by the use of dual or multiple rate PIDRs, with there being a variety of options possible, even for adoption of a dual rate. Similar comments also apply in relation to adjustments to the rate for taxation and other costs, which may be term-dependant.

12. As noted above, the PIDR NI derivation includes an inflation allowance based on the RPI index; a similar adjustment is made in setting the PIDR in Scotland. The corresponding PIDR in England and Wales allows for inflation by reference to the Consumer Prices Index (CPI), with adjustment. Without commenting on the relative merits of these approaches, we note that the RPI index is to be phased out in 2030. We therefore suggest considering an alternative derivation for the PIDR inflation allowance, given that the RPI index now has a limited future ‘shelf life’.

13. In our recent response to the MoJ consultation on a dual/ multiple rate PIDR, key points made included the following:

    - for lump sum settlements, a multiple or dual discount rate may be ‘fairer’ for claimants than the current single rate system;
    - there is however a balance to be struck between:
    - introducing operational and legal complexity (which a dual rate may bring) that would slow down final payments to claimants and
    - a fairer solution;

- a much more complex system would necessarily introduce costs (to claimant lawyers and insurers) that would ultimately be paid for by all impacted claimants and increased premiums paid by policyholders
- more generally, a further source of personal injury – and corresponding claims – arises through the NHS, with corresponding taxpayer impact.

14. We therefore suggested that a dual rate is practically the fairest compromise. In our view none of the PIDR systems used internationally is perfect.

15. We strongly suggest that an adequate lead time is given to all stakeholders before any changes to any PIDR methodology (in terms of rate structure) is introduced.

16. Our response to the MoJ can be found here:

https://actuaries.org.uk/media/4ksb3jyk/ifoa-response-to-moj-call-for-evidence-on-personal-injury-discount-rate.pdf

17. In looking at whether to adopt a dual or multiple PIDR or otherwise, the relative merits of a consistent methodology for setting the PIDR in England/ Wales and Scotland should be considered.

18. We would welcome the opportunity to discuss our response with the Department of Justice in more detail, or to provide any wider insight as the review of the PIDR NI progresses.

Should you want to discuss any of the points raised please contact me, Steven Graham, Technical Policy Manager (steven.graham@actuaries.org.uk) in the first instance.

Yours Sincerely,

Steven Graham
On behalf of Institute and Faculty of Actuaries

IUA OF LONDON
INTERNATIONAL UNDERWRITING ASSOCIATION

IUA Response to Scotland and Northern Ireland Request for Views – Personal Injury Discount Rate

Introduction:

The IUA is the representative body for companies in London providing international and wholesale insurance and reinsurance coverage. Its mission statement is to secure an optimal trading environment for London (re)insurance companies.

The IUA's London Company Market Statistics Report shows that overall premium income for the company market in 2021 was £35.654bn. Gross premium written in London totalled £30.114bn while a further £5.540bn was identified as written in other locations but overseen by London operations. The wider London Market generated premium of £74.970bn in 2021 (calculated by combining the IUA total of £35.654bn with £39.216bn declared by Lloyd's in its annual report).

The IUA's 73 ordinary members provide insurance and reinsurance coverage across a range of classes of business, including motor (£1.6bn GWP in 2021) and liability (£5bn GWP in 2021), which are the two classes of (re)insurance which are the most significantly impacted by the Personal Injury Discount Rate (PIDR). This response has been contributed to by both our liability and motor insurance and reinsurance practitioners, the latter of which provide reinsurance coverage to the world's largest motor insurers. Our members provide reinsurance cover to almost all motor insurers in the UK.

The IUA appreciates the opportunity to contribute to the discussion over the future of the PIDR model in Scotland and Northern Ireland. Our response is split into two sections. Section 1 provides our general comments relating to dual / multiple discount rates and Section 2 considers the factors that must be considered when setting the PIDR. We would be pleased to discuss any part of this response further.

Executive Summary:

The fair compensation of claimants is a priority for (re)insurers and is central to the PIDR framework. To compensate personal injury claimants more fairly, accurately and to better meet the 100% compensation principle, we make the following key recommendations in this response:

1. A switched dual PIDR model by duration should be adopted within Scotland and Northern Ireland.
2. The switched dual PIDR model should include a switching period of between 10 and 15 years.
3. Within the switched dual PIDR model cashflows beyond the switching point should be discounted at the long-term rate from the date of award.
4. The long-term PIDR in this switched dual PIDR model should be as stable as possible with minimal changes over the long-term.
5. The short-term PIDR in this switched dual PIDR model should be reviewed every 5 years.
6. The -0.5% further / "prudence margin" should not be retained.
7. If a switched dual PIDR model is not adopted then the single PIDR model should be retained, as opposed to adopting another form of dual/multiple PIDR model.

During this review process we believe that careful consideration should be given to the impact of future rate and methodology changes on three key areas:

- cost of motor and liability insurance premiums in relation to household expenditure.
- availability and affordability of motor and liability reinsurance products.
- direct cost to government and taxpayers through clinical negligence claims against NHS Scotland / Health and Social Care in Northern Ireland (HSC).

For certainty, where referring to a 'switched' model we are addressing a model whereby all cashflows up to the switching point (e.g. 10 years) are discounted at the short-term rate. Cashflows beyond the switching point are discounted at the long-term rate from the date of award, for the full period. This is demonstrated in the table below:

Example of Discounting Using Switched Dual PIDR

Assumptions:
- *13-year award period*
- *Short-term PIDR of -1% per annum*
- *Long-term PIDR of 1% per annum*
- *Switching point of 10 years*
- *Award amount £15,000 per annum*

Award year	Award amount	PIDR to apply	Discount factor	Discounted Amount
0	15,000	-1%	1.000	15,000
1	15,000	-1%	1.010	15,152
2	15,000	-1%	1.020	15,305
3	15,000	-1%	1.031	15,459
4	15,000	-1%	1.041	15,615
5	15,000	-1%	1.052	15,773
6	15,000	-1%	1.062	15,932
7	15,000	-1%	1.073	16,093
8	15,000	-1%	1.084	16,256
9	15,000	-1%	1.095	16,420
10	15,000	-1%	1.106	16,586
11	15,000	1%	0.896	13,445
12	15,000	1%	0.887	13,312
13	15,000	1%	0.879	13,180

A 'stepped' model operates differently, so that only one PIDR can ever apply to a whole award; in respect of an award shorter than the switching period this will be the short-term rate, but for any award that extends beyond the switching period this will be the long-term PIDR, for cashflows at all durations of the award.

A 'blended' model we understand to be one where all cashflows before the switching point are discounted at the short-term rate. Cashflows beyond the switching point are discounted at the short-term rate up to the switching point and then at the long-term rate, for each additional year after the switching point.

Any PIDR model should provide certainty to claimants, allowing them to meet their needs over both the short and long-term. This can be achieved by the switched dual PIDR model we have demonstrated above. However, we believe that if this model is not adopted a single PIDR should be retained, as we see a range of negative implications of other forms of dual or multiple PIDR models, discussed throughout this response.

Section 1 – Dual or multiple rates

Introduction

It is our recommendation that a switched dual PIDR model should be introduced with a switching period of between 10 and 15 years to compensate personal injury claimants more accurately and fairly. We would also encourage the removal of the unnecessary -0.5% prudence margin. Fundamentally, any model introduced must provide certainty to both claimants and compensators, and it is our view that a switched PIDR model is the only dual/multiple PIDR model proposed which can do so effectively. If this model is not adopted, we believe that a single PIDR should be retained.

The priority of any PIDR framework must be to uphold the well-established principle of 100% compensation. However, any framework should also provide balance, ensuring that 'the relevant damages would be exhausted at the end of the period for which they are awarded', as stated in the Damages Act 1996 (as amended).

International examples

Switched approach

The main strength of the switched dual PIDR model we are advocating is fairness. It recognises that not all claimants have identical investment horizons and more accurately reflects the specific needs of short and long-term claimants than other PIDR models, bringing us closer to achieving the desired 100% compensation principle. Overcompensating claimants has the risk of introducing additional costs to the (re)insurance process, which are ultimately passed on to those purchasing motor or liability insurance policies.

In our view, a switched dual PIDR model can provide fundamental stability, which in turn leads to certainty. Whilst the adoption of an Ontario-style 'blended' model in its current form is not supported, we recognise that similarly to the switched model we propose, greater long-term certainty is provided. In Ontario, the current short-term PIDR (2023) is 0.50%, and the long-term PIDR is plus 2.5%; whilst the short-term PIDR has been amended 16 times in the 22 years the model has existed, the long-term PIDR has remained unchanged. We envisage that under the switched PIDR model we propose, the long-term PIDR would be similarly stable.

One significant advantage of a long-term PIDR is that it can overcome short-term volatility in the financial markets and therefore needs to change less often. The certainty in a long-term PIDR that remains as stable as possible is best for all stakeholders impacted by PIDR changes, as it will result in less drastic movements in the size of awards. Stability in the size of awards can provide confidence to claimants in settling claims, reducing pressure to either expedite or delay a settlement to maximise an award as the review time approaches. Equally, the certainty that less volatile awards brings can allow (re)insurers to operate with confidence in a complex marketplace that involves the settlement of individual personal injury claims worth tens of millions of pounds. Under Solvency II, requirements imposed on regulated insurance and reinsurance firms requires the careful balancing of large loss reserves and, of course, robust pricing and risk management strategies to be employed. Any change in the PIDR has very real and significant implications on the (re)insurance process and so should be minimised where possible.

Heads of Loss approach

We do not consider a PIDR model by heads of loss, such as that used in the Republic of Ireland, to be appropriate, as it may introduce both complexity and a significant gaming risk. A model focusing on heads of loss is very likely to result in protracted negotiations. It also introduces a higher possibility of gaming as it could be argued that specific elements of loss be considered as different, more favourable, heads of loss. These points are already negotiated in practice, with schedules of loss commonly being many hundreds of pages; a model focusing on heads of loss may contravene one of the core aims of compensators which is

to ensure the speedy settlement and payment of personal injury claims. This model also fails to address one of the biggest criticisms of a single PIDR, which is that it does not adequately reflect the different needs of short and long-term claimants. Any model focusing on heads of loss will continue to be unable to accommodate the varying needs of claimants over the short and long-term. We also have no evidence that claimants segment and invest their award by heads of loss. Furthermore, anecdotal evidence has pointed to the potential for claims forum shopping between Northern Ireland and the Republic of Ireland due to the differing PIDRs available for future loss.

When considering a heads of loss approach, it should be noted that all but very minimal elements of catastrophic personal injury claims are labour-related and thus depend on earnings inflation. We do not believe care inflation would differ from general earnings inflation other than for short-term fluctuations. Therefore, the added complexity and cost of a head-of-inflation dimension outweighs any benefit. Between 2011-2022, the annualised increase of ASHE has been 2.6%; the general earnings index KA5H has been 2.7%.

Stepped approach

A stepped PIDR model, as operated in Jersey and Hong Kong, is in our view flawed and does not represent a fair approach. It is inappropriate that, were a 10-year switching point to be selected, two claimants with a 9-year and an 11-year settlement period respectively should receive such drastically different settlement outcomes with all other aspects of their claim being equal. In doing so the model is not appropriately meeting the needs of both claimants.

Blended approach

The Ontario model is a 'blended' dual PIDR model by duration. A blended model is more complex than the switched dual PIDR model we advocate and poses the key risk of introducing complexity and uncertainty for claimants and compensators alike; IUA does not support this model. We believe blended models can introduce a risk of overcompensation for claimants with losses over the longer-term that would not be present were a switched dual PIDR approach to be adopted. This is because in the blended model the short-term PIDR is applied to all long-term cashflows for the period up to the switching point. Effectively, this model assumes that the entirety of a claimant's award is invested from the date of award in a very low-risk portfolio, which we do not believe reflects the way in which claimants invest their awards. We encourage you to request data as to how claimants actually invest their lump sum and the returns that are commonly achieved on their investments. If such data is not forthcoming, we would encourage independent analysis to be undertaken.

Most importantly, a blended dual PIDR approach does not provide the stability of award sizes which we believe to be so beneficial. In the switched dual PIDR model we are advocating, a change to the short-term PIDR would only impact the element of the award up to the switching point, whereas with a blended PIDR approach a change to the short-term PIDR would impact the whole of the award, thereby making the size of awards more volatile.

Switching Periods

It is our view that the optimal switching point is between 10 and 15 years. It is difficult to say with absolute certainty which year is optimal, and we would encourage economic / financial analysis being undertaken to consider:

i. the typical duration of economic cycles, which we believe to be of a maximum of 10 years, highlighted by the Government Actuary in stating that "economic cycles can be expected to last for approximately 5 years, but longer cycles can last for up to 10 years".
ii. the likely returns of investments over different periods, with it being our opinion that more certain results can be achieved over an investment term of 10 years or more.

In seeking to understand the duration of economic cycles we referred to *An Examination of UK Business Cycle Fluctuations: 1871-1997* produced by the University of Cambridge, University of Reading, and Bank of England. This paper states that "the average UK business cycle, from peak to peak or from trough to trough, lasts some 62 months, with a standard error of some 28 months."

We acknowledge that during the 2019 review the Government Actuary recommended a switching period of 15 years, were a dual PIDR based on duration to be adopted. It is our view that a switching period of less than 10 years could necessitate more frequent change to the long-term PIDR and be less appropriate for claimants with longer investment horizons, whilst a switching period beyond 15 years could give too much weighting to the short-term PIDR and lead to overcompensation in some cases.

Our view was formed with reference to the modelling of the Government Actuary Department (GAD) in 2017 (Table 1 below) (gad-analysis.pdf (justice.gov.uk)), which demonstrates the expected real returns on claimant portfolios over 5-50 years. The table illustrates that the expected real returns, greater than zero, on investments begin at approximately 10 years and a significant proportion of the overall return that could be achieved over 50 years is being gained by year 15. Therefore, the likely investment returns of claimants between 0-10 years are substantially different than from 10 years onwards and so the switching period should lie between 10 and 15 years.

Table 1 – Expected real returns on claimant portfolios

Median money weighted real return %pa	Award period / investment horizon					
	5 years	10 years	15 years	20 years	30 years	50 years
Portfolio A	0.0%	0.6%	1.0%	1.2%	1.3%	1.6%
Portfolio B	0.0%	1.3%	1.7%	1.9%	2.0%	2.3%

Note: returns are in excess of RPI, which over 30 years is projected to be 2.7% pa on average.

The switching period should be set such that the long-term PIDR can be as stable as possible. In our view, a slightly longer switching period would be preferable if it meant that the long-term PIDR had less requirement for change.

Frequency of rate reviews

Dealing first with the review period for the long-term PIDR. We strongly believe there is a case for the long-term PIDR to be reviewed far less frequently than every 5 years as long-term investment returns have been shown to be far more stable. We believe the long-term PIDR should only change where absolutely necessary, and any amendment should be proportionate to the likely minimal changes to the long-term outlook. This will enable the benefits of a stable award environment to be felt. The impacts of PIDR changes can be significant in unsettling the claimant and compensator communities and should only be made where absolutely necessary.

Stability in the long-term PIDR in the switched dual PIDR approach we are advocating can lessen the impact of the large swings in (re)insurers' reserves which can be caused by changes to a single PIDR. Equally, it would also provide claimants with a more understandable and predictable environment in which to settle their claims.

Dealing with the short-term review, for stability and certainty around rate reviews we believe that the rate should be reviewed every 5 years, alongside the long-term PIDR. However, if amendments to the calculation method of the short-term PIDR were made to link the rate adjustment to a set of published economic indicators, then we may support more frequent review of the short-term PIDR, for example every

3 years. Using a set of indicators would introduce a level of predictability as to the next rate change, reducing the risks of instability that more frequent reviews can otherwise bring. We would invite further consultation and / or discussion on this point.

Advantages of a dual rate

Fairness has always been at the centre of discussion around the PIDR. The advantage of a switched dual PIDR model is that it provides a more accurate and fairer approach to lump sum settlements, ensuring that any under or overcompensation of claimants is minimised. It is also our view that this model is the only dual/multiple PIDR model that provides greater accuracy and fairness, whilst maintaining simplicity, when compared to a single PIDR model.

Since the last series of reviews (starting with England & Wales in 2019), the PIDR has been set at -0.75% in Scotland, -1.5% in Northern Ireland and -0.25% in England & Wales; these rates are some of the lowest in the world. The effect of this environment is to generate some of the largest bodily injury settlements globally, the costs of which are subsequently passed on to business, consumers and taxpayers through insurance premiums and funding NHS Scotland / Health and Social Care in Northern Ireland (HSC).

We believe that NHS Scotland / Health and Social Care in Northern Ireland (HSC) could be impacted positively were the switched dual PIDR model we are advocating introduced. There remains a very significant impact of PIDR changes to the NHS Scotland / Health and Social Care in Northern Ireland (HSC). Given the importance of clinical negligence awards, there could be a detrimental impact to governments and taxpayers were a single PIDR to fall further. We noted that following the PIDR review in Northern Ireland in 2022, the NHS stated that "the recently announced PIDR in Northern Ireland provides an indication that, if the PIDR in England and Wales had been reviewed and updated recently then the rate might be around 1% lower than it currently stands". The NHS's "sensitivity analysis shows the impact of changing the PIDR and shows the CNST *(Clinical Negligence Scheme for Trusts)* IBNR *(Incurred But Not Reported)* would be around £1.3 billion higher if the PIDR was 1% lower." (*NHS Resolution Annual report and accounts 2021/22)*

One of the key benefits of more accurate compensation is to alleviate significant concerns held by the (re)insurance industry about the growing nature of lump sum settlements posed by PIDR reviews that lead to less accurate and unfair compensation. The certainty that could be brought by a more stable long-term PIDR in a switched dual PIDR model will be a stark contrast to the current uncertainty that surrounds the PIDR in Scotland, Northern Ireland, England and Wales. At present there is a real risk that market stakeholders seek to delay or accelerate lump sum settlements depending on their view of the outcomes of the 2024 review. The ability for stakeholders to predict the future PIDR is challenging, as it remains probable that key factors could vary significantly, such as the composition and performance of the notional portfolio of investments used to inform the rate.

Inevitably, finding more balance between the risks of over and under compensation will have a smoothing effect on (re)insurers' claims payments and will provide a more certain operating environment. This in turn will make the territory a more attractive environment for insurers and reinsurers to transact business, which will favourably impact the cost of insurance for customers and in turn household expenditure.

Despite motor insurance being compulsory in the UK, there are many uninsured drivers. This already places a burden on the Motor Insurers' Bureau (MIB) and the insurance market which funds it. The potential increase in motor insurance premiums resulting from the costs related to changes to the PIDR, or from changes to the approaches of (re)insurers in the uncertainty that arises from a less stable PIDR environment, could exacerbate this issue, particularly in the higher risk categories of young drivers and those with motor convictions. This may increase the burden on the MIB and it is possible that an increased levy would be required.

Single Rate

If a single rate were to be maintained the methodology used should not be subject to material deviations caused by short-term volatility of the economic environment.

The UK "low-risk" approach need not be complex and opaque. One of our members pointed out that the PIDR could be based on a blend of a low-risk return and a high-risk return. The high-risk metric could be a liquid widely understood global equity index, like the S&P 500. The S&P 500 exceeds inflation by 6.7% over the long-term, noting the median annualised return over all 20-year rolling periods since 1871 is 6.7%, its worst annualised 20-year rolling period is -0.2% and its best 13.6% (http://www.econ.yale.edu/~shiller/data.htm). A simple approach like this should not be materially less fair or accurate than an Economic Scenario Generator with multiple subjective parameters. To provide stability in the PIDR, it may be appropriate to use a rolling average approach that looks at historical annualised returns over multiple periods of time.

This simple investment approach is likely to have very low transactional costs. For example, Vanguard charges 0.07% per annum for its S&P 500 ETF fund. Any increase in costs towards a more managed fund would be likely to produce a higher rate of return.

Investment behaviours

It is important to note the statutory requirement in the Civil Liability Act (CLA) 2018 for the Lord Chancellor, in making the rate determination, to assume the 'relevant damages are invested using an approach that involves (i) more risk than a very low level of risk, but (ii) less risk than would ordinarily be accepted by a prudent and properly advised individual investor who has different financial aims' (*Determining the rate of return* – Paragraph 4(3)(d)). In drafting our response we acknowledge that short-term claimants will still receive adequate financial advice and, when compared to longer-term claimants, may be subject to less tax and investment management costs. Were a switched dual PIDR model to be adopted it remains key to ensure a consistent view of the claimant is taken in both the short and long-term, namely that they be considered a properly advised low-risk investor.

It is anticipated that the switched dual PIDR model that we are advocating will better match the pattern of future investment returns. It would allow claimants to invest in a more appropriate investment portfolio to address both their short and longer-term needs. The yield curve is not horizontal, not even for risk-free government securities, so having dual duration-based rates will more accurately reflect actual investment returns. A dual discount rate is a reasonable compromise between extreme accuracy of an entire yield curve, and the frictional costs/potential mistakes associated with complexity. For simplicity of calculation and communication, we do not think there should be more than two rates.

A claimant with a longer-term investment horizon may choose to retain more liquid assets for the short-term and to develop a separate longer-term strategy with less liquidity. When considering model investment portfolios, it is likely that a claimant with a long-term investment horizon will have more tolerance for risk than a claimant with a short-term investment horizon. This is because a longer-term investment horizon will benefit from a greater duration within which to achieve a return and will be less impacted by short-term volatility.

In reviewing the impact on a claimant with a shorter investment horizon, a switched dual PIDR model which features a lower short-term PIDR will ensure that they are likely to receive the necessary funds to meet their needs. If their investment horizon is below 10 years, it is probable that the majority of their award will be retained as more liquid assets. Equally, they may choose to invest in less volatile assets, rather than assets such as equities which are generally considered to be more volatile over a short-term period.

In general, we would expect that where large financial sums are involved, a claimant would naturally seek appropriate financial advice and, in such cases, as Independent Financial Advisers (IFAs) are regulated by

the FCA, adequate advice is likely to be readily available. We believe that the measures currently taken by the Courts also ensure that claimants will be fully and properly advised regarding their settlements.

From our own research it is our view that IFAs typically expect to achieve significantly positive returns on low-risk investments for their clients. For example, Flying Colours Conservative portfolio ("aiming for moderate growth without extreme volatility") performed at 17.1% (5 years to last month end – 28th February 2023) (Our Performance - Investment Management | Flying Colours). Similarly, Intelligent Money achieved an annualised 10 year return in its IM Optimum Income portfolio of 5.49%, 3.97% within the IM Optimum Cautious portfolio and of 2.41% within its IM Optimum Defensive Portfolio (Our Portfolios – Intelligent Money | IFA).

The value that IFAs can contribute to investment returns should not be understated and was considered by Fidelity, which stated that "Industry studies estimate that professional financial advice can add between 1.5% and 4% to portfolio returns over the long term, depending on the time period and how returns are calculated". This statement is supported by the following summary of research undertaken (Why hire a financial advisor | Fidelity):

"Envestnet, Capital Sigma, The Advisor Advantage (PDF) estimates advisor value add at an average of 3% per year, 2019; Russell Investments 2019 Value of a Financial Advisor Update estimates value add at more than 4% per year; and Vanguard, Putting a Value on Your Value: Quantifying Vanguard Advisor's Alpha 2019, estimates lifetime value add at an average of 3%. The methodologies for these studies vary greatly. In the Envestnet and Russell studies, the paper sought to identify the absolute value of a set of services, while the Vanguard study compared expected impact of advisor practices to a hypothetical base case scenario."

Implementation

Noting that a shift to a dual PIDR system would represent a significant change from the current PIDR model, we believe that as much notice as possible should be given to all stakeholders to ensure sufficient preparation time. This would allow stakeholders to familiarise themselves with the new model to ensure that it operates as effectively as possible upon implementation. It must be recognised that many practitioners' IT systems would require updating. Therefore, we believe that a lead in time of around 6 months would be valuable to market practitioners.

The Solvency II Directive requires insurance companies to hold capital in relation to their risk profiles to guarantee that they have sufficient financial resources to withstand financial difficulties. Without sufficient lead in time to a change in PIDR approach it is possible that (re)insurers may be unable to make the necessary changes to their systems and therefore be unable to hold fully accurate reserves based on the prevailing PIDR.

If it is not possible to give notice of the full details of the new model, at the very least the key features of that model should be provided to stakeholders at the earliest convenience, with full details provided closer to implementation. These features would include:

- how many PIDRs will be in operation.
- whether those PIDRs will apply by duration or by heads of loss.
- if by duration, then the specific durations and if by heads of loss then the specific heads of loss.
- if by duration, whether the PIDRs will apply in a switched, stepped or blended format.

Section 2 – Factors when calculating the PIDR

The makeup of the notional portfolio (as laid out in paragraph 12 of Schedule B1 in the Act)

It is our view that it is inappropriate for one single portfolio to be considered. Claimants should be considered to have one low-risk portfolio for the short term immediately after settlement which does not contain volatile assets and another portfolio with more equities for the longer term.

In 2019 the Government Actuary suggested the following three low-risk portfolios when providing advice in respect of England & Wales:

Table 5: Low-risk portfolio allocation

Allocation	Cautious	Central	Less-cautious
Lower risk / matching Assets	70%	57.5%	45%
Cash	12.5%	10.0%	7.5%
Gilts	35.0%	30.0%	22.5%
Corporate bonds	22.5%	17.5%	15.0%
Higher risk / growth assets	30%	42.5%	55%
Equities	22.5%	32.5%	42.5%
Alternatives	7.5%	10.0%	12.5%

We note that Scotland and Northern Ireland have a 20% notional portfolio allocation to equities. That is a lower percentage in equities than even the 'Cautious' portfolio suggested for England & Wales. We think this is too cautious for a low-risk portfolio. Scotland and Northern Ireland should adopt a notional portfolio like the 'Central' portfolio shown in Table 5 above. The Government Actuary seems to suggest that the 'Central' portfolio was suitable for his advice to the Lord Chancellor in 2019 for England & Wales.

IG have published total returns on the FTSE 100 since it was introduced in 1985. See below:

Source
https://www.ig.com/uk/trading-strategies/what-are-the-average-returns-of-the-ftse-100--200529

The graph shows that the worst returns for any 10-year period is an annualised 0.3% p.a. There has never been a negative total return over a 10-year period. But depending on which 10-year period you select, the returns are still quite variable with the highest being 17.3% p.a. The 20-year returns are more stable.

For long term investments we believe that a diversified portfolio of equites is suitable where you would expect significant positive returns in excess of inflation. The 20-year returns are stable and positive.

The assumed period of investment (currently 30 years)

The current 30 year assumed investment period for Scotland is far too short. The largest settlements are often in relation to young individuals, who even with some reduction to normal life expectancy, can have assumed award periods of longer than 60 years.

The Government Actuary, in his advice to the Lord Chancellor in 2019, states the following in paragraph 5.8 "the Institute and Faculty of Actuaries suggested that 30 years is too short a term, with their responses suggesting a period of around 40-45 years." This is based on the information submitted to a Call for Evidence by the Ministry of Justice (MoJ) and reviewed by the Government Actuary. The Government Actuary chose to use 43 years for the period of damages in advising the Lord Chancellor on the PIDR in England & Wales. In Northern Ireland we note that 43 years is used and recommend that the same be used in Scotland.

We acknowledge that there will always be significant variation in the period of investments for a given set of claimants. Therefore, consideration should be given to a model which reflects this. Instead of having one assumed period of investment, a discount rate model should be adopted which adequately caters for both claimants with long term investment horizons and claimants with shorter term investment horizons.

The impact of inflation (currently allowed for by reference to the Retail Prices Index)

Both claimants with longer-term and shorter-term investment horizons are susceptible to inflationary fluctuations. Depending on the nature of the economic environment encountered over a short-term investment horizon, it is possible that a claimant could be subject to more or less inflation than that accounted for in the PIDR. The important point to reiterate is that the economic conditions encountered by the claimant can be more or less favourable than anticipated and it will not be possible in all cases to ensure that a claimant is not impacted by adverse economic conditions.

When considering the option of dual/multiple rates, a switched dual PIDR model will more accurately and fairly compensate claimants with both short and long-term horizons, reducing the risks of inflationary pressures that may be experienced over different investment periods.

We believe that the complexities involved in tracking inflation in respect of individual heads of loss highlights the benefits of a switched dual PIDR model based on duration, rather than by head of loss. As previously stated, all but very minimal elements of catastrophic personal injury claims are labour-related and thus depend on earnings inflation. We do not believe care inflation would differ from general earnings inflation other than for short-term fluctuations.

The standard adjustments that must be made by the rate-assessor to a rate of return (currently set at 0.75% which represents the impact of taxation and the costs of investment advice and management; and 0.5% which is the further margin involved in relation to the rate of return)

We think that the current assumption of 0.75% for tax and expenses is reasonable. This is consistent with the Government Actuary's advice for England & Wales and the current law for Scotland / Northern Ireland.

We note that active investment management may vary. We agree with what the Government Actuary set out in paragraph 7.15 of his report for England & Wales:

"A substantial cause of these differences in the levels of expenses is the different approaches to investment that are adopted. Broadly speaking, the more active or engaged investment approaches lead to higher

expenses. However, I would expect these to be compensated by better returns – as otherwise such approaches would not be profitable and sustainable in a rational and competitive market."

If the Government Actuary uses Economic Scenario Generators based on the whole market returns of different asset classes, this is effectively using a passive investment approach to gain returns. If an active approach is used, higher expenses may be incurred but far higher returns are more likely to be achieved. We agree with the GA advice that 0.75% is a reasonable assumption for expenses and tax.

IUA, July 2023

Dear Department of Justice / Scottish Government,

Thank you for issuing the recent joint request for views.

By way of background, Kennedys is a global law firm dealing with dispute resolution in many jurisdictions across 72 offices, including in Scotland and Northern Ireland. We engage with governments and regulators on a range of matters including the personal injury discount rate across a number of jurisdictions.

We welcome the devolved administrations' call for views to explore whether any changes should be made to the range of factors to be taken into account when calculating the respective Personal Injury Discount Rate in Northern Ireland and Scotland.

However, in the absence of access to claimant investment data we are not currently in a position to submit views and supporting evidence on the need or otherwise to adjust any of the factors set out in Schedule B1 (for Scotland) and in Schedule C1 (for Northern Ireland) of the Damages Act 1996.

We note the request for views also provides the opportunity to offer views and evidence on whether a single or multiple rates should apply, and on a preferred model. As part of Kennedys' response to the England & Wales call for evidence launched in January 2023, we engaged with our global colleagues in Hong Kong and Ireland to offer the key strengths and potential weaknesses of dual/multiple rates in other jurisdictions. We refer you to our response to Question two on the attached document which we hope will be of interest, although we recognise this document was created in response to an England & Wales consultation.

We note that at this stage, the devolved administrations have not put forward any recommendations as to a change in personal injury discount rate. We would therefore welcome the opportunity for any change to be explored further by way of specific proposals within a formal consultation. This would allow us to consider the proposals with our clients, undertake modelling and offer evidence to support our opinion(s). To a certain extent, based on the current call for views, stakeholders are considering the various PIDR models in a vacuum.

If you have any questions, please do not hesitate to contact us.

Yours faithfully,

Amanda Wylie, Managing Partner, Kennedys Belfast LLP
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Kennedys’ response to the Personal Injury Discount Rate: Exploring the option of a dual/multiple rate Call for Evidence

11 April 2023

About Kennedys

Kennedys is a global law firm with expertise in dispute resolution and advisory services. Founded in 1899, we have a rich history of delivering straightforward advice, even when the issues are complex.

With over 2,400 people and 72 offices, associate offices and co-operations around the world, including twelve offices across the UK, we are a fresh-thinking firm and are not afraid to bring new ideas to the table beyond the traditional realm of legal services. Our lawyers handle both contentious and non-contentious matters, and provide a range of specialist legal services, for many industry sectors including insurance and reinsurance, marine, aviation, banking and finance, construction and engineering, healthcare, life sciences, public sector, rail, real estate, retail, shipping and international trade, sport and leisure, transport and logistics and travel and tourism.

Corporate Affairs team

Kennedys have a dedicated Corporate Affairs team responsible for generating insights on emerging industry risks and trends, as well as the impact of legal and political shifts on the international business environment.

We regularly engage with governments and regulators to create, confirm or build on their knowledge base about an industry. Industry and government engagement helps us and our clients stay informed and align our activities and business objectives with current and emerging industry activities.

Our Corporate Affairs team are experts in the political process and provide valuable insights into government and issues shaping today's corporate landscape. The interest of the Corporate Affairs team is in the big issues facing the industry, including geopolitical risks, the future of transport, sustainability, reputational risks and others.

Executive summary

Kennedys shares the Government's commitment to the principle of 100% compensation.

As observed in the Foreword to the Call for Evidence, the reforms within Part 2 of the Civil Liability Act 2018 were "designed to create a fairer and more accurate way to set the discount rate, taking account of a range of factors". As such, continued reflection on and consideration of the current personal injury discount rate (PIDR) system is an important part of ensuring a fair, efficient and modern civil justice system in England and Wales. Consultation is an important part of this process to ensure stakeholders have the opportunity to engage with Government.

Kennedys therefore supports and welcomes the Ministry of Justice Call for Evidence on exploring the option for a dual/multiple rates more widely which fulfils the Government's commitment in 2019 to seek additional views and evidence on this.

We appreciate at this stage of the Government's review the purpose of the Call for Evidence is to simply explore the options of dual/multiple discount rates. However, in the absence of specific proposals or recommendations on what the rate(s) may be, it is very difficult to put forward a preferred model. To a certain extent, stakeholders are considering the various PIDR models in a vacuum. We would therefore welcome the opportunity for the options to be explored further by way of specific proposals, in order to consider which mechanism is most appropriate, be that a single rate, dual or multiple rates.

Nonetheless, of the four scenarios identified within the Call for Evidence, we consider a dual rate system would provide a mechanism that may deliver a fairer outcome to a wider range of claimants. This would allow claimants with a shorter life expectancy to take lower investment return risks to generate adequate investment return. However, issues relating to complexity, increased costs and the potential risk of 'gaming' the system (particularly around any switchover point) are concerns.

We have instructed The Centre for Economics and Business Research (CEBR) to assist with our response in order to provide an economics perspective at questions 13, 14, and 15.

Response to questions

Question 1: Do you have a preferred model for a dual/multiple rate system based on any of the international examples set out in the Call for Evidence paper (or based on your or your organisations experience of operating in other jurisdictions)?

Please give reasons with accompanying data and/or evidence.

We appreciate at this stage of the Government's review the purpose of the Call for Evidence is to simply explore the options of dual/multiple discount rates. However, in the absence of specific proposals or recommendations on what the rate(s) may be, it is very difficult to put forward a preferred model. To a certain extent, stakeholders are considering the various PIDR models in a vacuum. We would therefore welcome the opportunity for the options to be explored further by way of specific proposals, in order to consider which mechanism is most appropriate, be that a single rate, dual or multiple rates.

Nonetheless, of the four scenarios identified within the Call for Evidence, we consider a dual rate system would provide a mechanism that may deliver a fairer outcome to a wider range of claimants. As a dual rate facilitates the ability to have a lower short-term rate, such an approach mitigates against the possibility that a claimant with a short life expectancy may be under-compensated. Longer-term investors have more time to ride out the volatility of a higher-risk portfolio, which would be expected to generate higher returns. However, issues relating to complexity, increased costs and the potential risk of 'gaming' the system (particularly around any switchover point) are concerns.

Question 2: What do you consider to be the main strengths and weaknesses of the dual/multiple rate systems found for setting the discount rate in other jurisdictions?

In summary, we list below what we consider to be the key strengths and potential weaknesses of the dual/multiple rate systems in other jurisdictions referred to within the Call for Evidence.

Strengths

- A dual rate provides the opportunity to have a lower rate for the short-term period which enables a claimant to avoid having to take a higher risk approach to investment in circumstances where there is less time to recoup any potential losses during the investment period. Greater comfort on the part of claimants in such circumstance in respect of assessment of their damages, may in turn assist in facilitating earlier settlement.

- A dual rate facilitates the opportunity to have a lower rate for the short-term period to ensure claimants with a short life expectancy are compensated in line with the 100% compensation principle. This would allow claimants with a shorter life expectancy to take lower investment return risks to generate adequate investment return. Longer-term investors have more time to ride out the volatility of a higher-risk portfolio, which would be expected to generate higher returns.

- There is an argument that a dual rate provides fairer outcomes for more claimants.

Potential weaknesses

- Complexity – a move to dual/multiple rates will inevitably add an element of complexity which potentially increases costs and causes delay in resolving claims. However, as has been the case with all civil justice changes, we anticipate practitioners would get to grips with the changes in a relatively short period of time. Further, our colleagues in Ireland, Hong Kong and Canada have informed us that the PIDR models in their respective jurisdictions do not currently add an additional layer of complexity, although many practitioners in these jurisdictions rely on actuarial/economist evidence.

- Disruption and increased cost – there is a risk, at least in the short term, that a move to dual/multiple rates could result in delays/and or possible disputes between parties, which in turn will lead to increased costs. We specifically highlight that in many of the jurisdictions with dual/multiple rates the parties obtain evidence from actuaries and economists.

- The potential risk of 'gaming' behaviour - especially around the switchover point. However, we understand from our colleagues in Hong Kong, Ireland and Canada that they are not aware of gaming behaviours.

- Periodical Payment Orders (PPOs) potentially become less attractive to claimants.

We explore a number of these points in more detail below.

- In Ireland, we understand there are some disputes regarding which losses are subject to the lower discount rate (with a higher multiplier). For example, some claimants seek the lower rate for other heads of damage that are 'wage related'. This can then become a point for negotiation between the parties.

- We consider the Hong Kong experience from practitioners is a positive one, although we consider a multiple rate system would be too complex if implemented in England and Wales.

- In Ontario, the challenge is the fact the short term rate has in the last 22 years been reviewed 16 times which in our view is disruptive to practitioners and creates uncertainty. Further, there is a risk of over-compensation because the lower rate applies to all claimants.

- We understand that in Jersey there is ambiguity in relation to losses in excess of 20 years duration. For example, if the loss covers a 25-year period it is generally felt to be unclear whether the 1.8% rate should apply for the entire period or only the last 5 years with the lower rate applied for the first 20 years. As a result, some claimants plead a position based on 0.5% for 20 years and 1.8% for the last 5 years, whereas the defendant will plead a multiplier based on

1.8% for the entire period. This will then become a feature in the negotiations. Ambiguity in the drafting and application of a revised system can therefore lead to increased costs and delay arguing and negotiating avoidable points. The compromise will also result in a difference between the actual outcome and that intended by those who devised the system. We understand that with losses expected to last around 20 years, tactical decisions are made to accept a shorter period to enable the 0.5% rate to be used or it may be argued the loss would be incurred for longer so creating an argument for the 1.8% rate throughout. Tactical decisions are made with losses close to the switchover point.

- Practically, Ogden tables are not available in Jersey for a 1.8% rate and so parties need to extrapolate between 1.5% and 2% or in high value claims seek expert advice on the appropriate multipliers to use for a 1.8% discount rate. It may be an obvious point but to avoid unnecessary costs and delay it would be helpful if any revised system in England and Wales used rates with readily available tables or steps need to be taken for them to be produced as part of the reform process.

- We understand PPOs are an option in Jersey but are not widely used. It is felt the current system disincentivises their use. One reason cited is that the regime allows for either party to apply for a variation on their being a 'material change in circumstances' without defining what that means. This is felt to create uncertainty around potential future liabilities. This is not currently an issue in England and Wales.

Question 3: What do you consider is the optimal point for the switch-over from a short to a long-term rate on a duration-based dual rate model?

Please give reasons with accompanying data

Determining the optimal point for the switch-over is dependent on a number of factors, including what discount rates are applied to the period prior to and after the switch-over. It will also depend on the economic environment which is variable. Ultimately, a balance must be reached with a mechanism to provide fair compensation for claimants avoiding both under and over compensation. We recognise that the period prior to the switch-over point must be long enough to enable the claimant to generate a sufficient investment return. Equally, the time periods must be such to mitigate against the potential risk of over-compensation.

With reference to paragraph 3.17 of the Government Actuary's report 'Setting the Personal Injury Discount Rate' dated 25 June 2019, we note that whilst "economic cycles tend to last for around 5 years there are economic cycles that last much longer than this" and "there is the general consensus the current economic cycle started around 10 years ago in the aftermath of the global financial crisis". The report (also at paragraph 3.17) adds that "economic forecasters, such as the Office for Budget Responsibility or the Bank of England tend to have short- and medium-term projections reflecting current economic conditions and tending towards long-term trends over the next 10 to 15 years."

In our view, a short-term period of between 10 to 15 years is logical, however, we consider this would need further exploration to determine the optimal point for the switch-over.

Question 4: What would you consider an absolute minimum and maximum point for the switch-over between two rates to be?

Please give reasons for your choice.

We refer to our response at question 3 above, as we believe the considerations referred to above apply when considering the absolute minimum and maximum point for the switch-over between two rates.

In our view, it seems logical that the minimum point for the switch-over should be ten years to enable sufficient time for a claimant to generate an investment return. It is foreseeable that economic fluctuations during a period of less than ten years could lead to challenges for a claimant to generate an appropriate investment return.

Finally, when considering the switchover point, the possibility for 'gaming' must be taken into account.

Question 5: If a dual rate system were to be introduced, would you advocate it was established on the basis of the duration of the claim with a switchover point, on duration based on length of claim or its heads of loss (or a combination of the two)?

Please give reasons for your answer.

We do not advocate for a heads of loss system, which we consider to be potentially more complex and could lead to extended negotiations and increased costs.

Looking at the duration of claim models, our preference would be a dual rather than a multiple rate system. Multiple rates, in our view, have even greater complexity and as we are keen for practitioners to apply any new system, as opposed to instructing experts such as actuaries/economists, a dual rate would be preferable.

We query whether the Ontario model potentially benefits all claimants with a lower discount rate in the short term, rather than having a lower discount rate for those that have a short life expectancy. We also query whether having a dual rate with a switchover is an added layer of complexity.

Moving from a single to a dual rate system, as in Jersey, may be easier to put into practice but we would suggest rounding rates to the nearest 0.25 percent to enable practitioners to use the Ogden Tables.

Question 6: In dealing with volatility of markets over the short-term is it a reasonable assumption that short-term rates in a duration-based system should be more variable and set at a lower rate; and long-term rates more stable and set at a higher rate?

If you agree or disagree that this assumption is reasonable, please say why.

We recognise that a short-term rate in a duration-based system should be set at a lower rate than the longer-term rate, to enable claimants with a shorter life expectancy the opportunity to generate an adequate investment return. We are, however, concerned that an assumption that short-term rates should be more variable could lead to disruption and uncertainty for compensators, insurers and public bodies in terms of both setting premiums and reserving. Further, too frequent reviews of the PIDR could potentially lead to gaming and delays in settlement. We note, for example, that in Ontario the short term rate has been changed 16 times in a period of 22 years. In our view this is unacceptable.

Question 7: If short-term rates are more volatile, should frequency of review be increased?

Please explain your reasoning.

We consider the timeframe for review provided under the current statutory framework, namely the Civil Liability Act 2018, works well from a practical perspective and provides stability to all stakeholders. As mentioned in our answer to Question 6, we are concerned that if the short-term rate is reviewed and subsequently changed too frequently, this could lead to disruption of the market and operating models of compensators, insurers and public bodies.

Question 8: What would you regard as the advantages of a dual/multiple rate system?

We consider the principal advantage of a dual or multiple rate system is the opportunity to address any potential concern there may be in relation to the outcomes for claimants with a shorter life expectancy. A dual rate provides the opportunity to have a lower rate for the short-term period which enables a claimant to avoid having to take a higher risk approach to investment in circumstances where there is less time to recoup any potential losses during the investment period.

Greater comfort on the part of claimants in such circumstance in respect of assessment of their damages, may in turn assist in facilitating earlier settlement.

Question 9: What would you regard as the disadvantages of a dual/multiple rate system?

- Complexity – a move to dual/multiple rates will inevitably add an element of complexity which potentially increases costs and causes delay in resolving claims. However, as has been the case with all civil justice changes, we anticipate practitioners would get to grips with the changes in a

relatively short period of time. Further, our colleagues in Ireland, Hong Kong and Canada have informed us that the PIDR models in their respective jurisdictions do not currently add an additional layer of complexity, although many practitioners in these jurisdictions rely on actuarial/economist evidence.

- Disruption and increased cost – there is a risk, at least in the short term, that a move to dual/multiple rates could result in delays/and or possible disputes between parties, which in turn will lead to increased costs. We specifically highlight that in many of the jurisdictions with dual/multiple rates the parties obtain evidence from actuaries and economists.

- The potential risk of 'gaming' behaviour - especially around the switchover point.

- PPOs potentially become less attractive to claimants.

Question 10: What do you consider would be the specific effects on implementing and administering the discount rate if a dual/multiple rate is introduced?

From a practical perspective, the Ogden Tables would need to be updated, along with internal guidance for both claimant and defendant practitioners in terms of application of the new rate(s). Practitioners would also need to advise their clients on the impact of the change in rate(s). Indemnifiers will need to also take into account any change in their underwriting and reserving models.

Question 11: In addition to specific effects, do you consider there will be additional consequences as a result of implementing a dual/multiple rate?

Please give reasons with accompanying data/evidence if possible.

We are concerned that there may be potential 'gaming' as a result of a change in rate(s).

Parties will perhaps understandably seek to interpret and apply the PIDR in the perceived interests of their clients.

Question 12: If a dual/multiple PIDR were to be introduced would it be helpful to provide a lead in period to prepare processes, prepare IT changes etc. and if so, how long should this be?

Please provide reasons for your answer.

We would suggest that a three to six week period between the announcement of the rate(s) and the rate(s) coming into force would be appropriate. This reflects the approach taken when announcing and thereafter introducing the PIDR in 2019.

Question 13: What do you consider would be the effects of a dual/multiple rate on a claimant's investment behaviour and what would this mean for the design of a model investment portfolio?

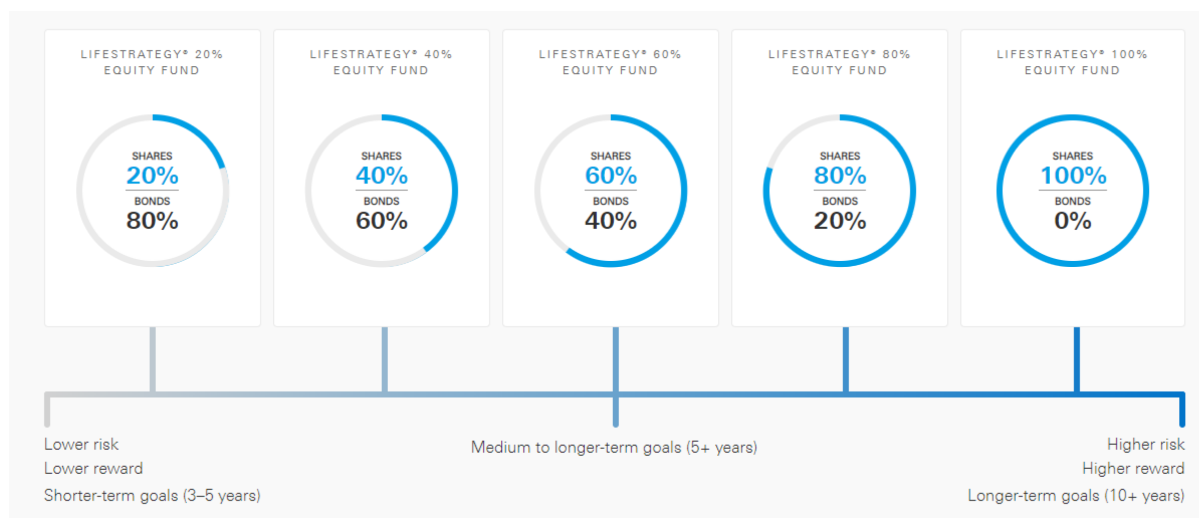
Impacts on the design of a model investment portfolio

The current legislative framework as set out in the Civil Liability Act 2018 requires the Lord Chancellor to have regard to the actual investments made by claimants and the investment return available. The Government Actuary noted in the 'Setting the Personal Injury Discount Rate' report dated 25 June 2019 that there was limited evidence of a claimant's investment portfolio and investment returns. This is an opportunity for this evidence to be obtained when reviewing the next PIDR from both claimants and their financial advisors.

In the absence of actual data the Government Actuary wrote extensively on the assumptions and model results concerning investment returns in his June 2019 report. CEBR's research has found these assumptions to be largely reasonable based on recent data on investment returns, although the returns are slightly higher than those relied on by the Government Actuary. For example, the average annual return of the Vanguard LifeStrategy 40 fund, which invests 40% in equities and 60% in bonds, was 2.7% between 2012 and 2022 after accounting for inflation. This is higher than the CPI + 2% average return assumed by the Government Actuary.

The calculations, which form the basis for the assumptions regarding portfolio returns, take into account various key elements of basic investment theory. For example, the Government Actuary considers that a suitably diversified portfolio will consist of 'growth assets' with greater risks and higher expected returns and 'matching assets' with lower risk and lower expected returns. Under the current single discount rate regime, the Government Actuary assumes that the representative claimant will invest in a relatively low risk portfolio with a growth asset allocation of around 42.5%, though allocations with 30% and 50% were also considered. This seems to be a reasonable figure based on the risk classification provided by large fund managers. See, for example, Figure *1* below.

Figure 1: Equity allocation for different portfolios and their recommended investment horizons



Source: Vanguard UK

As can be seen, a 40% equity allocation would put a portfolio towards the lower risk end of the spectrum of funds pictured.

The exact composition of the portfolio will depend not only on the claimants' risk appetite but also on their investment horizon. Indeed, the two concepts are closely linked as suggested in *Figure 1*. In line with best practices, it can be expected that financial advisors would recommend a greater allocation to growth assets for investors with a longer investment horizon and a more cautious portfolio with a lower share of growth assets for those with a shorter investment horizon. As such, the change from a single to a dual / multiple discount rate framework would require assumptions about the returns of a long- and short-term portfolio compared to the current situation where only a single assumption on the returns of an average portfolio is required. This is confirmed in the Government Actuary's report to the Lord Chancellor:

> 3.14 When considering the impact on claimants with different investment horizons, there is an argument that it is appropriate to use a different portfolio of investments for different periods of claim. This is because it is reasonable to expect that a claimant investing over longer periods may feel able to take more Risk as they have more time over which to recover from any period of poor investment returns[1]

And regarding the considerations concerning the potential implementation of a dual rate system:

> 3.15 […]I have assumed that the representative claimant with a shorter-term award invests in the cautious portfolio outlined in Chapter 6 and that the representative claimant with a longer-term award invests in the less-cautious portfolio.[2]

Accordingly, in practice, a dual rate system would likely result in a short-term rate that is lower than the current single rate and a long-term rate that is higher than the current single rate. This reflects the fact that a claimant with a shorter investment horizon is more likely to invest in a more cautious portfolio compared to the 'representative claimant' under a single rate framework, while the longer-term claimant will invest in a higher risk portfolio. A dual rate system would therefore produce outcomes which are less likely to lead to significant over- or under-compensation based on award duration.

Impacts on investment behaviour

In relation to what impact a dual/multiple rate system has on a claimants' investment behaviour, economic theory would suggest this would be zero, assuming the award is paid out as a single lump sum. As discussed above, the optimal investment strategy for a claimant will depend on risk appetite and the investment horizon. The model which produces the final set of discount rate(s) used to

[1]Setting the Personal Injury Discount Rate - Government Actuary's advice to the Lord Chancellor, June 2019

[2] Ibid.

calculate the size of the award is irrelevant from the claimant's perspective, meaning that the same investment behaviour should be assumed regardless of whether the award was calculated using a single or dual/multiple discount rate framework. While it is possible the discount rates produced by a dual/multiple rate system will lead to a change in the final award value compared to a single rate system, the choice of the optimal investment strategy remains unaffected by this.

Another way of looking at this is by considering the purpose of the discount rate, which is to convert an assumed future stream of income into a present lump sum. Once this lump sum has been determined, the decision on how to best invest this, is independent of the choice of discount rate framework.

Question 14: What do you think would be the effects of a dual/multiple rate on drawing up assumptions for tax and expenses when setting the discount rate?

Assumptions for tax drag

The Government Actuary considers costs such as investment fees, management charges, adviser fees and taxes when setting the discount rate, as these are costs a claimant realistically needs to cover. While it is acknowledged these costs will differ depending on personal circumstances as well as on the tax/fee structure in place at the time, the Government Actuary aims to give a reasonable estimate of the impact of these costs on investment returns, and therefore on the discount rate, for the 'representative claimant'.

In the sensitivity analysis of the Government Actuary's report to the Lord Chancellor, it is made clear that there are considerable uncertainties with respect to the size of tax and expense effects on the portfolio. The report contains some illustrative estimates of the tax burden under various scenarios, varying by the size of the claim, other income received by the claimant, and their investment strategy.

Figure 2: Illustrative tax drag on returns for different award amounts

		Claimant profile		
		A	B	C
Description		Small claim	Medium claim	Large claim
Award size (£)		100k	1m	3m
Other income (£ pa)		25k	10k	none
Investment Strategy / Assumed income yield	Cash	10% / 0.5% pa		
	Bonds	47.5% / 2% pa		
	Equity	42.5% / 3.5% pa		
Tax drag on return[10]		0.0% pa	0.2% pa	0.5% pa

Note: I have included an approximate allowance for capital gains tax on equities by assuming a proportion of the portfolio is sold each year and subject to capital gains tax on assumed capital growth.

Source: Setting the Personal Injury Discount Rate - Government Actuary's advice to the Lord Chancellor, June 2019

There are further variables which were not explicitly considered, including the fact tax liabilities are likely to reduce over time as the claimant regularly draws an income from the award, thereby reducing the sum of invested money. Another key variable is the tax environment and future changes to tax policy with tax reduction being a political priority. These are difficult to anticipate and therefore were not included in the modelling. Considering all of the factors, the Government Actuary comes to the conclusion that an adjustment for tax of between 0.0% and 0.5% p.a. is reasonable, with the eventual figure 'very much towards the lower end of the range'.[3]

As can be seen in Figure 2 above, the size of the claim has an impact on the estimates of tax drag, all else equal. Under a dual/multiple rate system it could therefore be appropriate to consider a higher tax drag figure for longer-term claimants, who are likely to receive a larger award, while short-term claimants would be more likely to experience lower levels of tax drag on portfolio returns.

Investment fees and other expenses

In terms of further expenses, the following types of fees can be considered:

- Financial adviser fees
- Fund management fees
- Platform fees, transaction costs, and other associated costs

The total amount of fees will not only vary depending on the specific adviser or platform chosen, but more fundamentally depending on the investment approach.

Investors can pay for their funds to be actively managed or they can pursue a passive investment approach. These approaches are summarised below:

- Under the active approach, an investment manager will look after the investment portfolio and choose the assets that are assumed to provide the best returns for a given level of risk. Securities are frequently traded in order to benefit from price fluctuations and achieve superior investment returns.

- A passive investment strategy, on the other hand, aims to build a suitable investment portfolio in line with the investment horizon and risk profile of the investor and hold securities for the long term. This is often done via index funds that aim to replicate the performance of an underlying stock market index such as the S&P 500 or the FTSE 100. Rebalancing of the portfolio occurs only to make sure that allocations between assets do not stray too far from the intended ratio, such as a 60/40 equity-bond portfolio. Meanwhile, the buy-and-hold approach means that such a portfolio requires relatively little oversight or input compared to the active investing style.

In short, an active investor tries to 'beat the market' while a passive investor is content to 'replicate the market'. Active investment managers charge substantially higher fees compared to what investors would need to pay for a passive investment approach. While the debate on whether the

[3] Setting the Personal Injury Discount Rate, 7.10

active or passive investing approach is superior is ongoing, there is ample evidence that shows that active investment managers tend to underperform the market on aggregate after accounting for fees, especially over longer periods.[4]

Given this, it seems reasonable to argue that higher fund management fees should not be factored into the decision on adjustments for the discount rate.[5] Rather, a passive investment approach, which would incur a smaller investment management cost, would seem appropriate and in line with the assumptions made by the Government Actuary.

A similar argument holds for fund management fees. As investment returns are modelled based on market returns, rather than 'market beating' returns, assuming a low-cost passive approach seems reasonable with the Government Actuary quoting fund management fees of around 0.25% to 0.5% p.a. for this.

A further argument that was raised is that platform fees are often capped based on the amount of funds invested, which implies that the relative drag on performance is larger for smaller investment sums. The Government Actuary quotes platform fees of around 0.15% p.a. of funds under management, though these "may be lower than 0.05% p.a. for much larger funds" due to the cap.[6] A dual rate system might therefore justifiably apply different platform fees for short- and long-term claimants. Nevertheless, at 0.1 percentage points based on the Government Actuary's estimates, the difference is rather small in the context of other fees and considerations.

Question 15: What do you consider would be the effects of a dual/multiple rate on analysing inflationary pressures and trends when setting the discount rate?

This question considers the appropriate way of expressing damage inflation, that is, how the costs and expenses that the award is supposed to cover will develop over time due to increases in the price and wage level among other things.

Under a single rate system, a single assumption needs to be made to reflect damage inflation in an appropriate way for the representative claimant. For the Government Actuary, the two potential options regarding the decision on how to set the adjustment for damage inflation were:

- Inflate damages at the rate of the Consumer Price Index (CPI), as this is the broadest measure of the change in the cost of living;

- Inflate damages at the rate of earnings growth, as in some cases labour intensive services such as nursing and care costs will form a substantial part of the expenses that the award will need to cover.

[4] See for example, S&P Dow Jones Indices - SPIVA Scorecard (H1 2022): "A majority of actively managed funds underperformed their respective benchmark in nearly every fund category included in our Europe scorecard."
[5] Even if active management would lead to higher fund performance, this would mean that investment return assumptions would need to be lifted as well, leading to a net neutral effect on the discount rate.
[6] Source: Setting the Personal Injury Discount Rate - Government Actuary's advice to the Lord Chancellor, June 2019, 7.32

The Government Actuary takes a blended approach between the two ideas, as "claimant's needs would include some aspects which are linked to general consumer prices (ie CPI linked) and some aspects which are linked to movements in earnings (for example care costs)".[7]

Given that earnings growth is assumed to average CPI+2% p.a., this blended approach yields a damage inflation adjustment of CPI+1%. However, as the Government Actuary concedes in the report, the assumption that earnings growth outstrips inflation is based on a long time series, which includes periods in which inflation increased at a faster rate than wages. Recent data suggest that since 2010, inflation on the CPI measure has outstripped average annual earnings growth by 0.1 percentage points per year. This suggests that an adjustment for damage inflation above and beyond CPI to account for a wage growth component is not justified based on recent data.

A dual/multiple rate system would need to make at least two or even more assumptions regarding damage inflation. For a dual rate system an assumption around short-term inflation, plus a further assumption around long-term inflation would need to be factored in. In the long term, it can be expected that inflation will converge towards the Bank of England's inflation target of 2%, as this is the mandate given to the Bank by the Government.[8] However, assumptions regarding inflation in the short term are significantly more volatile as evidenced by the current period of very high inflation levels. While under a single rate framework it can be argued that inflation will converge towards the 2% Bank of England target in the long term, this cannot necessarily be guaranteed for shorter time periods. For example, based on the latest projections presented in the Bank of England's February Monetary Policy report, policymakers expect inflation to stand at 4.3% in Q4 2023 and 2.2% in Q4 2024.[9] Inflation is therefore expected to be remain above the 2% target for an extended period beyond the initial spike in price growth.

This raises the question whether a short-term rate would require more frequent updating to reflect the current inflationary picture, while a long-term rate can likely be kept unchanged for an extended period. More frequent reviews would likely have an impact on feasibility and make implementation of such a system more complex and costly. In the absence of frequent reviews of the inflation-adjustment for the short-term rate, there is a risk that claimants, and in particular those with shorter award durations, would be over- or undercompensated. On the other hand, too frequent reviews could lead to disruption and 'gaming'. As such, there is a careful balance to be struck.

Question 16: What do you consider would be the effects on claimant outcomes of a dual/multiple rate being adopted for setting the discount rate?

As a defendant law firm that does not act for claimants, we do not have access to claimant investment data and are therefore not in a position to provide a response to this question.

We note that in 2019 the Government Actuary in his advice to the Lord Chancellor on the personal injury discount rate stated at paragraph 8.7 that: "Given that claimants have financial independence

[7] Ibid. 8.10
[8] Data from the Office for National Statistics (ONS) suggest CPI inflation averaged 2.5% between 1989 and 2022. See: https://www.ons.gov.uk/economy/inflationandpriceindices/articles/consumerpriceinflationhistoricalestimatesandrecenttrendsuk/1950to2022
[9] https://www.bankofengland.co.uk/monetary-policy-report/2023/february-2023

after their settlement and there is no data or reporting on how their needs and investments evolve, there is very little independent evidence that can be used as a cross reference".

It is hoped that this Call for Evidence and any further consultation will remedy this situation.

Question 17: If a dual/multiple rate was adopted would it be possible to return to a single rate in future reviews, or would a move be too confusing and complex and seen as irrevocable?

Please give reasons.

A change back to a single rate would, in our view, be disruptive to the indemnity market in relation to setting premiums and reserving but would not be seen as irrevocable.

In Ontario, where legislation was passed in 1999 for a dual rate with a 15 year switching point, we note that in 2020 and 2021, a sub-committee of Ontario's Civil Rules committee published reports recommending a return to a single discount rate. The 2021 report notes: "In large part, our reasons for opting for a single rate have to do with the difficulty of establishing a rate for a period that will only begin 15 years in the future." Interestingly, the report also states: "Inevitably, some individual plaintiffs would be overcompensated and some undercompensated but our objective was to maximize the chances of full compensation while removing any inherent mechanisms that would produce overcompensation."

Question 18: What do you consider the respective advantages and disadvantages of adopting multiple rates would be, when compared with either a: single rate; or a dual rate?

We refer to our response to Question 2 above. We add one of the main advantages of a single rate is simplicity and relatively easy to understand.

Question 19: If a heads of loss approach were adopted, what heads of loss should be subjected to separate rates - care and care management costs, future earnings losses, accommodation, or any other categories?

If a heads of loss approach were adopted, we consider that care and case management (which is often the largest head of loss) should be subject to separate rates.

Question 20: Introducing a dual/multiple PIDR could result in increased levels of complexity for both claimants and compensators. Do you agree with the assumption that this complexity will stabilise and ease once the sector adapts to the new process?

Please give reasons.

We believe that introducing a dual/multiple PIDR would result in increased levels of complexity. However, once practitioners have adapted to the new system, our expectation is that this would stabilise.

It is, however, likely that this additional complexity would still add additional costs to the litigation process with additional investigations and additional expert evidence being sought.

Question 21: The Government remains interested in exploring the use of PPOs in relation to high value personal injury settlements. We would therefore welcome any submissions, data and/or evidence stakeholders may have in relation to the effective use of PPOs.

For many years PPOs have been widely accepted in England, particularly in relation to NHS Resolution claims, as the preferred way of compensating claimants with significant lifetime disability, even where residual life expectancy is uncertain or reduced. It is clear from our discussions/investigations that this is not the case in other jurisdictions. The reasons may be local to those jurisdictions, however, it does need to be recognised that any alterations to the current system may affect perceptions of the relative merits of lump sum awards versus periodical payments.

It is important that modelling anticipates any potential changes in the relative merits of a lump sum compared to a PPO especially if the perceived benefits brought about by indexation to ASHE 6115 are offset by attempts to introduce a long-term discount rate which better reflects wage inflation in the care sector.

We resolve a significant number of claims at Kennedys by way of PPO. We do, however, acknowledge that cases involving claimants who are minors and those without capacity often settle by way of PPOs on the basis that their litigation friends accept it is clearly in the best interests of the claimant as a PPO ensures annual payments - usually for care and case management - for the duration of the claimant's life. Whilst this predominantly applies to NHS Resolution claims, the same considerations would also apply to those cases that settle via insurance.

Whilst insurers are also able to offer PPOs to claimants, in our view, a lump sum is often preferred by adult claimants with capacity and the ability to choose how they invest the funds.

Interestingly in Ireland where there is a dual rate, they have a statutory framework for PPOs but these have largely not been utilised as they are indexed linked to a non-earnings related index unlike in England and Wales where they are linked to ASHE 6115.

Question 22: Do you agree that using a higher PIDR to calculate the real rate of return in settlements which include a PPO element would result in a more appropriate way to adjust nominal investment returns for future inflation?

Please give reasons.

Yes, by applying a deduction in the PIDR calculation for the differential between CPI and earnings, there is a potential risk of 'double counting' which could lead to over-compensating the claimant.

When calculating the PIDR the Lord Chancellor deducts 1% for the differential between CPI and earnings related losses from the investment return (see section 8 of Government Actuary's Department report) and the table below. Claims that settle by way of PPO the annual periodical payment (usually the largest head of loss – care and case management) is index linked to an earnings related index. Accordingly, claims which settle by way of PPO benefit from: (i) a PIDR that deducts 1% across non-earnings related losses; and (ii) annual payments index linked to an earning related Index. Arguably, the 1% discount should not be applied to claims resolving by PPO.

% pa above CPI	Representative claimant
Expected gross return of investments before deductions	2.0% pa
Deduction for tax and expenses	0.75% pa
Deduction for damage inflation	1% pa
Deduction for risk of under-compensation	0.50%
Personal Injury Discount Rate	**-0.25% pa**

Of course, having a higher discount rate for claims that settle by way of PPO may potentially have the unintended consequence of more claimants opting for lump sum awards to take the benefit of the lower discount rate.

Question 23: What impact would a dual/multiple rate system have on protected characteristic groups, as defined in the Equality Act 2010?

None that we are aware of.

Contact information

Any enquiries about the response or requests for further information should be addressed, in the first instance, to Deborah Newberry, Corporate Affairs Director for Kennedys.

To find out more about our services and expertise, and key contacts, go to: kennedyslaw.com

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Request for information in Scotland and Northern Ireland - PIDR

Confidentiality Statement

The information provided in this response is confidential and is not to be circulated outside the Justice Directorate at the Scottish Government and Department of Justice in Northern Ireland without the prior written consent of Keoghs LLP. In particular it should not be released if within the scope of a request for information under the Freedom of Information Act.

Irrespective of the points made above, our position is also that the information contained in this response is provided to the Justice Directorate at the Scottish Government and Department of Justice in Northern Ireland for the purpose of, and during the course of, formulating policy, such as would fall within the exemptions under the Freedom of Information Act for at least as long as it takes for policy to be implemented, not simply formulated.

Terminology

We use the term 'claimant' throughout our response to equally apply to claimants and plaintiffs.

Introduction

The below is the response of Keoghs LLP to the joint request for views on the potential for adjustments to the range of factors taken into account when setting the personal injury discount rate ('PIDR') in Scotland and Northern Ireland, as well as the potential for adoption of a dual/multiple PIDR in these jurisdictions.

Keoghs is the only top 100 law firm to focus exclusively on handling and defending both mainstream and specialist insurance claims. We offer an end-to-end claims service to insurers, public sector bodies and self-insured companies which includes pre-litigation, litigation and costs negotiation services. Keoghs acts for eight out of the top ten UK general insurers, and with almost 1,800 dedicated staff, is a recognised leader in its field. In the last 12 months we handled approximately 90,000 cases across all classes of personal injury claim.

We have recently addressed the potential for a dual/multiple discount rate system in England and Wales in some detail. We consider that there should be consistency across the three jurisdictions with the majority of our response to the call for evidence in England and Wales being equally applicable when addressing the question of a potential dual/multiple discount rate in Scotland and Northern Ireland, we therefore attach this response as annex A.

We believe that it is important to set out some key principles and issues when addressing the option of exploring a potential dual/multiple rate system, as well as considering potential adjustments to the factors to be taken into account when setting the PIDR in Scotland and Northern Ireland.

Key Principles

100% compensation

We support and endorse a discount rate system that enables all claimants to secure full compensation.

However, in catastrophic injury claims there is a danger of becoming seduced by the idea that we are engaged in predicting the future with a high degree of certainty and that compensation for all claimants can be precisely and mathematically calculated to ensure that claimants have the very last penny needed for the duration of their lives. This is of course a fallacy and a flawed concept. The best we can do is attempt to assess a claimant's future needs, on the balance of probabilities and by reference to the available evidence, at the time the claim is settled. At that point in time both the claimant and the defendant take a risk that their view of the future (which may be 20, 30, 40, 50 or more years ahead), embodied by the settlement, is the right one. The future needs of the claimant may wax and wane over time as much as investment returns and inflation. The discount rate is but one factor in the assessment of risk.

The issue was neatly summarised by Lord Scarman in *Lim Poh Choo -v- Camden and Islington Health Authority [1980] AC 174*:

"*The course of the litigation illustrates, with devastating clarity, the insuperable problems implicit in the system of compensation for personal injuries which (unless the parties agree otherwise) can yield only a lump sum assessed by the court at the time of judgement. Sooner or later, and too often later rather than sooner, if the parties do not settle, a court (once liability is admitted or proved) has to make an award of damages. The award, which covers past, present and future injury and loss, must, under our law, be of a lump sum assessed at the conclusion of the legal process. The award is final; it is not susceptible to review as the future unfolds, substituting factor estimate. Knowledge of the future being denied to mankind, so much of the award as is to be attributed to future loss and suffering (and in many cases the major part of the award) will almost surely be wrong. There is only one certainty: the future will prove the award to be either too high or too low*".

Since 1 April 2005, some of the uncertainties referred to by Lord Scarman have been partially addressed by Section 2 of the Damages Act 1996, which had the effect of introducing periodical payment orders (PPOs). However, whether or not a PPO is awarded, the point remains that a pursuit of 'certainty' is fundamentally flawed including any attempt to do so in the setting of the personal injury discount rate.

The supposition of some measured risk in assuming investment returns is just part of the process. To ignore actual investment behaviour, as we do now, cannot be the right starting point.

The need for data

Whilst paragraph 4.5(a) of Schedule A1 of the Damages Act 1996 sets out the Lord Chancellor must "have regard to the actual returns that are available to investors" when determining a rate for England and Wales, no such requirement to consider data is contained within the legislation as related to Scotland and Northern Ireland. That is not, however, as we would contend, a reason to discount data. Indeed, it is impossible to consider, in any meaningful, evidence-backed way what the potential issues could be for any system based upon dual rate/multiple discount rates, including:

- what the potential switching point(s) should be for a potential future dual rate (if based on duration of award); and

- the form of any appropriate investment portfolios based upon short-term/long-term investment periods without any data on actual investment returns at present.

Data is needed regarding the actual investments made (and returns achieved) by claimants to show their investment behaviour. Without data of the returns claimants are securing at present (and over recent years) it is impossible to consider the appropriateness or otherwise of the current notional portfolio. The legislation applicable to these jurisdictions requires consideration of a 'hypothetical investor' who will (i) 'invest the damages'; and (ii) will 'do so as properly advised'. Accordingly, data to demonstrate how investors are, in fact, being advised to invest their damages awards (and the returns achieved on that basis) are relevant.

It is notable that in relation to the recent Call for Evidence in England and Wales the response of FOCIS contended that the data they produced from IFAs demonstrated that the percentage that had been allowed in 2019 for the combined effect of taxation and cost of investment advice (namely 0.75%) was too low[1]. The data was cited in support of an argument that there needed to be a greater percentage because of the cost of employing an IFA. It is apparent that if data can be produced on behalf of claimants to support increased charges of the involvement of an IFA then data should also be available (as required by the Civil Liability Act) as to actual investments made by claimants and returns upon the same.

The need for harmony

At present the discount rates applicable across the three jurisdictions are considerably different, with a rate of minus 0.25% in England and Wales, minus 0.75% in Scotland and minus 1.5% in Northern Ireland. Part of the reason for the difference in rates is due to them having been set at different times, however the method for setting the PIDR as set out in legislation is different across the jurisdictions – with the most notable difference being an investment period of 30 years applied in Scotland, compared to the 43 years in England and Wales and Northern Ireland.

We are reassured that the PIDR across the three jurisdictions will be next reviewed at a very similar time, which will help to ease the disparity in the rates. We consider that there should be harmony across the three jurisdictions when it comes to the method for setting the PIDR, which would minimise the current lottery of vastly differing financial outcomes for identical injuries according to the jurisdiction involved. The overarching principles should be uniform across the jurisdictions, such as the investment portfolio being based on a low-risk investor, the investment period being 43 years and the same inflation indices applying. There is logical basis for such differences in methods as there are now.

Risk of insurance premium costs rising to an unaffordable level for consumers and wider economic considerations

Competition law prohibits insurers from setting out what insurance premiums might cost if the discount rate changes (in any event, assessment of the financial impact of any change to the discount rate is extremely difficult to assess until the precise details of any such change are known, including the details of any dual rate model to be applied). However, the reality is that if the discount rate becomes more negative than it is at present in either jurisdiction (either as a single rate or as a dual rate) it will likely impact the cost of future insurance premiums, directly impacting consumers during a cost-of-living crisis.

[1]Answer to Question 14: https://img1.wsimg.com/blobby/go/be8b5965-34e8-41e9-a505-8a2285394493/230411%20-%20MOJ%20PIDR%20Call%20for%20Evidence%20-%20FOCIS%20re.PDF

This is a point which the Guernsey Policy and Resources Committee ('the Committee') was alive to during the Guernsey consultation which closed on 17 May 2022. During that consultation process, the Committee commented on the rationale when Jersey's dual discount rates were set, and the benefits (to both insurers and insured persons) of insurers being able to price across both markets, with the Committee proposing to initially adopt the rates set by Jersey (being a dual rate of 0.5%/1.8% with a 20-year switching period). The Guernsey consultation reflected the Committee's concerns that insurance could become unaffordable in Guernsey, depending on the level at which the discount rate was set.

Whilst the 100% compensation principle must always be paramount, the impact of a change in the discount rate on consumers (through higher insurance premiums/higher costs passed on by UK PLC) and on the taxpayer (through the potential impact on one of the largest compensators, the NHS) should be considered. We note that NHS Resolution's annual report for 2021/22 attributed a £42.6 billion increase in the damages provision as of 31 March 2022 to the change in the discount rate.

Difficulties comparing other jurisdictions/changes anticipated in other jurisdictions

With Jersey and Guernsey adopting a dual rate discount rate, and Ontario in Canada having operated with a dual rate discount rate for some considerable time, it might be tempting to assume that a similar dual rate discount rate can be applied in Scotland and Northern Ireland with similar considerations as in these other jurisdictions. We would counsel against this approach and caution that these other jurisdictions have crucial differences to Scotland and Northern Ireland, including being smaller and processing significantly lower claim volumes (in the case of Jersey and Guernsey) as well operating within different litigation systems.

It is worth noting that in a report prepared by the Ontario Rules Committee in April 2021 recommendations were made that the jurisdiction should:

1. return to a single rate (i.e. abandoning the dual rate completely); or alternatively
2. abandon the 0% 'floor' on the short term rate of the dual rate (thereby leaving open the potential for a negative rate for the short term period) and reduce the rate for the long-term from 2.5% to 1%.

Questions

Are adjustments merited to the range of factors to be taken into account when calculating the PIDR in Scotland and Northern Ireland?

The range of factors includes:

- the make-up of the notional portfolio
- the assumed period of investment (currently 30 years in Scotland and 43 years in Northern Ireland);
- the impact of inflation (currently allowed for by reference to the Retail Prices Index); and,
- the standard adjustments that must be made by the rate-assessor to a rate of return (currently set at 0.75% which represents the impact of taxation and the costs of investment advice and management; and 0.5% which is the further margin involved in relation to the rate of return).

The notional portfolio

This comes back to one of the fundamental issues that we highlighted in our Key Principles. Data is needed of the actual investments and returns from claimants to show their investment behaviour and the returns they are securing at present and in recent years. Without evidence of existing portfolios for those claimants currently investing their damage awards (and the rates of return in fact achieved), it is difficult to predict what portfolios should look like for any potential future dual or single rate.

No evidence has been put forward to suggest that (properly advised) claimants are, in fact, suffering a shortfall in investment returns and/or are taking on an unacceptable level of risk in terms of the investment of their damages awards.

Absent that data, any assessment of the current notional portfolio is inevitably artificial.

The legislation applicable to these jurisdictions requires consideration of a 'hypothetical investor' who will (i) 'invest the damages' and (ii) will 'do so as properly advised'. Accordingly, data to demonstrate how investors are, in fact, being advised to invest their damages awards (and the returns achieved on that basis) are relevant and real data would demonstrate what is actually happening as opposed to having to rely upon assumptions.

The assumed period of investment (currently 30 years in Scotland and 43 years in Northern Ireland)

In the Government Actuary's report to the Lord Chancellor dated 25 June 2019 on the setting of the PIDR for England and Wales, it was noted that responses to the Call for Evidence provided evidence that the average life expectancy of personal injury claimants was between 40 and 45 years and therefore a representative investment period was assumed of 43 years[2].

The setting of the PIDR cannot of course be a precise science and the reality is that some claimants will have a shorter investment period and some claimants will have a longer investment period, but in taking an average of 43 years fairness and balance can be achieved. For those claimants with very short life expectancies they may be better served by agreeing a PPO (which is available across all three jurisdictions) however the reality is that take-up of PPOs is still very low, indicating that even for those claimants with a shorter life expectancy, they still expect to achieve more favourable investment returns when investing a lump sum to meet their lifelong needs.

As discussed above, harmony across the jurisdictions is necessary to prevent a 'lottery' of claim outcomes based upon the location of the claimant. If there continues to be a considerable difference in the PIDR across the jurisdictions there is potential for satellite litigation when arguments are available for claims to be pursued in a jurisdiction which is perceived to be more beneficial.

The impact of inflation (currently allowed for by reference to the Retail Prices Index)

There are periods of time when there is little economic volatility (and investment returns and returns on investments are therefore stable) and periods of time where the economy experiences more volatility. Historically, economic cycles tend to last for around 5 years, with some lasting longer than this. The Government Actuary noted in his report to the

[2] Page 34
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/817236/Setting_the_Personal_Injury_Discount_Rate__web_.pdf

Lord Chancellor in 2019[3] that economic forecasters, such as the Office for Budget Responsibility or the Bank of England, tend to have short and medium-term projections reflecting current economic conditions and tending towards long-term trends over the next 10 to 15 years. It is important not to 'over-provide' in any system, particularly when legislation enables an earlier review of the discount rate if necessary, in the event of significant changes in the economic climate.

Inflation is just one aspect of the discount rate and it is important it is considered across the typical investment period, which was previously considered in the GAD report of 2019 to be 43 years. Any short-term volatility, as now, should be ignored. Such spikes, or indeed drops, are typically short-lived and the assessment of inflation when considering the discount rate should not be based on that small snapshot in time, but over likely inflation levels over the duration for which any damages award is expected to last.

Current inflationary pressures are unprecedented, yet the Bank of England's goal is to return inflation to 2% and to keep it at that level. The most recent OBR forecasts predict that CPI inflation will fall below 2.0% by the first quarter of 2024.

Evidence of real returns available to claimants at present would enable the issue of inflation to be put into its proper context.

As considered above we submit that there should be harmony across the three jurisdictions when it comes to the particular index applied to the PIDR (which there is not at present) and there should be no reason for different indices to apply in the future. Accordingly we consider that the PIDR should be set by reference to the consumer prices index (CPI) instead of RPI. RPI is no longer considered to be a "National Statistic" by the Office for National Statistics (ONS) and has not been since 2013. The ONS do not think RPI is a good measure of inflation and actively discourage its use. In their paper published in March 2018[4] they state "we do not view the RPI as a good measure of inflation" and that it was likely to overstate inflation.

Adjustments for taxation and cost of investment advice and 'prudence'

Taxation

In the majority of cases the impact of taxation is likely to be negligible and, as noted by the Government Actuary in their 2019 report, it will also reduce over the lifetime of a claimant's investment. The Government Actuary considered in this report that a reasonable adjustment for tax would be in the region of 0.0% to 0.5% per annum, and that taking a view towards the lower end of this range was supported by the fact that the tax adjustments they considered were based on the initial award size for a claimant, and with the size of claimants funds reducing as they make withdrawals from their funds, the tax liabilities would also reduce over time.[5]

A properly advised claimant (ie the 'hypothetical investor' as described in the legislation) will most likely invest their damages in such a way that tax liabilities are minimal or nil. Any impact of taxation should be minimal with a low-risk passive portfolio and proper investment advice.

[3] Page 25 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/817236/Setting_the_Personal_Injury_Discount_Rate__web_.pdf
[4] 1.Foreword by the National Statistician; Paragraph 3: https://www.ons.gov.uk/economy/inflationandpriceindices/articles/shortcomingsoftheretailpricesindexasameasureofinflation/2018-03-08
[5] 7.10 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/817236/Setting_the_Personal_Injury_Discount_Rate__web_.pdf

The cost of investment advice

Claimants should be supported by professionals when planning their future investments in order to ensure they are able to meet their financial needs and it is right that the costs that attach to that advice are factored into the PIDR. With the assumed risk appetite of the claimant for the purpose of setting the PIDR being that of a low risk investor, and with the makeup of the notional portfolio being set out in legislation, the management of such a portfolio should not be as 'active' and time consuming as that of a higher risk portfolio. If a claimant chooses to invest their damages in a higher risk portfolio carrying higher management charges (but therefore the prospect of higher rates of return) they are of course able to do so, however the associated higher level charges should not be factored in to the PIDR.

'Prudence'

An additional 0.5% deduction in the PIDR has been provided for in the legislation for the Scottish and Northern Irish jurisdictions however we would submit that such additional 'prudence' should not be necessary when the PIDR is already based on a low risk investor, with a passive low risk portfolio over a 43 year investment period. Any such peaks and troughs in investment experience should be considered over the passage of time. An element of risk is experienced by both the claimant and defendant at the point of settlement of a claim and any claimant with a risk appetite lower than a 'low risk' investor has the option available to them of settling their claim by way of a PPO.

Factoring in additional 'prudence' is contrary to the general principles of quantification of damages, and is at odds with the general civil burden of proof – being one of the 'balance of probabilities'. It is usual for both the claimant and the defendant to accept some level of risk at the time of agreement of a settlement.

Whether single or multiple rates should apply?

As stated above, we annex to this paper a copy of our recent response to the Call for Evidence in England and Wales on the potential for a dual/multiple rate in that jurisdiction as we consider our response equally applicable to Scotland and Northern Ireland. Below we capture a small section of our response, however this should be read in conjunction with our full Call for Evidence response.

It is impossible to state a preference definitively based on any of the examples in circulation as it depends on the precise structure and methodology proposed, in particular the level at which any short and long-term rates are set, and the length of time before any 'switching point' between those rates. In our view, it is also necessary to compare any dual/multiple rate system proposed to the single rate system currently in operation.

We have seen conflicting terminology being used in relation to the various options ('switched', 'stepped', 'blended', 'graduated') previously described by GAD in their 2019 report for England and Wales, and the attempt to sometimes fit those definitions onto discount rate regimes currently used in other jurisdictions when a direct comparison is not available (or not appropriate). It is important to ensure consistency in terminology to avoid confusion and misunderstanding. We further believe that there are different interpretations of how those options might apply in practice in other jurisdictions and therefore it is again important that when considering the various alternatives, that everyone is clear as to the precise methodology adopted.

In conclusion, out of the examples quoted, we believe that the dual rate "switched" system based on duration of damages award (referred to as the 'Ontario model' within the call for evidence) is the preferred model, and the

proposal which best encapsulates the principle of full compensation without adding undue complexity, or risking creating many adverse consequences.

Whether it is a 'fairer', better, and more practical option to the single rate currently in operation depends on the precise methodology applied when fixing the short/long-term rates, and the switching point.

There are strengths and weaknesses to the various dual/multiple rate systems, just as there are with the current single rate system. Once again, it is difficult to comment in the abstract, absent further detail on the type of dual/multiple rate system proposed and the way it would be structured.

In general terms therefore we see the main strengths and weaknesses of a dual/multiple rate system as follows:

Strengths

- The ability to deal more fairly with those claimants who have short life expectancies;
- A more 'scientific' approach with the ability to reflect and counter volatility in short-term investment returns;
- The fact that they are present in other jurisdictions and in many cases have been for several years;
- The ability to reflect different inflationary measures across different heads of loss;
- The ability to remove the need for any additional prudence when setting the rate;
- In a dual-rate system over the duration of the claim with a switching point, the greater stability of the long-term rate, which should/is likely to be higher to reflect the reality of real investment returns available.

Weaknesses

- The additional complexity in operating a system based on dual or multiple rates;
- The likely additional costs and delays involved in resolving claims under such systems;
- The greater uncertainty for litigants in accurately valuing claims;
- The increased risk of satellite litigation;
- The risk of 'gaming', especially between different heads of loss and either side of any switching point;
- The prospect of additional and costly expert evidence assessing life expectancy;
- The attempt to arrive at a more precise mathematical calculation to assess full compensation which is impossible and illusory;
- Weighting a system more in favour of the minority of claimants at the extremes of short/long life expectancies as opposed to deriving a fair system across all claimants;
- The greater uncertainty that arises in a system with potentially multiple rates, a switching point and more regular reviews.

ANNEX A

Call for Evidence response

MoJ Call for Evidence: Personal Injury Discount Rate - Exploring the option of a dual/multiple rate

Confidentiality Statement

The information provided in this response is confidential and is not to be circulated outside the Ministry of Justice, HM Treasury or the Government Actuary's Department without the prior written consent of Keoghs LLP. In particular it should not be released if within the scope of a request for information under the Freedom of Information Act.

Irrespective of the points made above, our position is also that the information contained in this response is provided to the Ministry of Justice, HM Treasury or the Government Actuary's Department for the purpose of, and during the course of, formulating policy, such as would fall within the exemptions under the Freedom of Information Act for at least as long as it takes for policy to be implemented, not simply formulated.

Introduction

The below is the response of Keoghs LLP to the MoJ Call for Evidence on the Personal Injury Discount Rate – Exploring the option of a dual/multiple rate.

Keoghs is the only top 100 law firm to focus exclusively on handling and defending both mainstream and specialist insurance claims. We offer an end-to-end claims service to insurers, public sector bodies and self-insured companies which includes pre-litigation, litigation and costs negotiation services. Keoghs acts for eight out of the top ten UK general insurers, and with almost 1,800 dedicated staff, is a recognised leader in its field. In the last 12 months we handled approximately 90,000 cases across all classes of personal injury claim.

Before answering the specific questions posed, we believe that it is important to set out some key principles and issues when addressing the option of exploring a potential dual/multiple rate system.

Key Principles

100% compensation

We support and endorse a discount rate system that enables all claimants to secure full compensation.

However, in catastrophic injury claims there is a danger of becoming seduced by the idea that we are engaged in predicting the future with a high degree of certainty and that compensation for all claimants can be precisely and mathematically calculated to ensure that claimants have the very last penny needed for the duration of their lives. This is of course a fallacy and a flawed concept. The best we can do is attempt to assess a claimant's future needs, on the

balance of probabilities and by reference to the available evidence, at the time the claim is settled. At that point in time both the claimant and the defendant take a risk that their view of the future (which may be 20, 30, 40, 50 or more years ahead), embodied by the settlement, is the right one. The future needs of the claimant may wax and wane over time as much as investment returns and inflation. The discount rate is but one factor in the assessment of risk. The supposition of some measured risk in assuming investment returns is just part of the process. To ignore actual investment behaviour, as we do now, cannot be the right starting point.

Data on actual investment returns

Paragraph 4(5)(a) of Schedule A1 of the Damages Act 1996 ('the Act') (as amended by the Civil Liability Act 2018) requires that the Lord Chancellor, when setting the reviewed discount rate, must:

- have regard to the actual returns that are available to investors;
- have regard to the actual investments made by claimants investing damages awards; and
- make appropriate allowances for taxation, inflation and investment management cost.

Quite apart from the explicit statutory requirement that regard must be had to actual investment returns and actual investment behaviours, there is a real need for this data to be made available in order to facilitate any meaningful industry input into the potential implications of a dual rate/multiple rates.

In particular, it is impossible to consider, in any meaningful, evidence-backed way what the potential issues could be for any system based upon dual rate/multiple discount rates, including:

- what the potential switching point(s) should be for a potential future dual rate (if based on duration of award; and
- the form of any appropriate investment portfolios based upon short-term / long-term investments periods

without any data on actual investment returns at present.

Difficulties calculating the perceived benefits of a dual rate

The Government Actuary's Department ('GAD') previously considered that a dual rate has the potential to more closely match the pattern of expected future investment returns, which at present time are characterised by lower short-term investment rates but higher long-term rates. The expectation, when considering any potential dual rate model, is that claimants investing over shorter periods of time can expect much lower annualised investment returns than for those investing over longer periods. A dual rate therefore has the potential benefit of making it less likely that those claimants with a shorter investment horizon are likely to experience situations where their settlement awards do not meet their needs.

If a dual rate were to be adopted in the future in England and Wales, consideration needs to be given to what a suitable notional portfolio of investments would be, with presumably a more cautious portfolio for the short-term rate and less risk-adverse portfolio for the longer-term rate. Without evidence of current portfolios for those claimants currently investing their damage awards (and the rates of return in fact achieved), it is difficult to predict what portfolios should look like for any potential future dual rate. No evidence has been put forward to suggest that (properly advised) claimants are, in fact, suffering a shortfall in investment returns and/or are taking on unacceptable level of risk in terms of the investment of their damages awards.

With the above caveats in mind, we are of the view that a 'switched' dual rate, provides the most appropriate dual rate model (should a dual rate model be preferred) out of the various models previously proposed by GAD. Such a

model would also be the easiest to administer. The benefit of such a dual rate is that while a short-term rate can be set so that investment risk to claimants with shorter life expectancies is reduced, a long-term rate can be set at a higher and more stable rate, better reflecting typical longer-term investing outcomes.

However, there are many factors involved in such a dual rate system which all need to be considered as well as the benefits of the single rate system currently in place.

Risk of insurance premium costs rising to an unaffordable level for consumers and wider economic considerations

Competition law prohibits insurers from setting out what insurance premiums will cost if the discount rate changes. (In any event, assessment of the financial impact of any change to the discount rate is extremely difficult to assess until the precise details of any such change are known, including the details of any dual rate model to be applied.) However, the reality is that if the discount rate becomes more negative than it is at present (either as a single rate or as a dual rate) it will likely impact the cost of future insurance premiums, directly impacting consumers during a cost of living crisis.

This is a point which the Guernsey Policy and Resources Committee (the Committee) was alive to during the Guernsey consultation which closed on 17 May 2022. During that consultation process, the Committee commented on the rationale when Jersey's dual discount rates were set, and the benefits (to both insurers and insured persons) of insurers being able to price across both markets, with the Committee proposing to initially adopt the rates set by Jersey (being a dual rate of 0.5%/1.8% with a 20-year switching period). The Guernsey consultation reflected the Committee's concerns that insurance could become unaffordable in Guernsey, depending on the level at which the discount rate was set.

It is evident that policy considerations concerning the price and availability of appropriate insurance cover have also been key in the setting of personal injury discount rates in Australian jurisdictions.

The Act does not limit the factors that the Lord Chancellor may consider when setting the personal injury discount rate (see Schedule A1 para 4(6)); accordingly it is open to the Lord Chancellor to take into account wider economic factors when considering the impact of a potential future dual rate/multiple rate. Whilst the 100% compensation principle must always be paramount, the impact of a change in the discount rate on consumers (through higher insurance premiums/higher costs passed on by UK PLC) and on the taxpayer (through the potential impact on one of the largest compensators, the NHS) should be considered. We note that NHS Resolution's annual report[1] for 2021/22 attributed a £42.6 billion increase in the damages provision at 31 March 2022 to the change in the discount rate.

Difficulties comparing smaller jurisdictions/changes anticipated in other jurisdictions

With Jersey and Guernsey adopting a dual rate discount rate, and Ontario in Canada having operated with a dual rate discount rate for some considerable time, it could be tempting to assume that a similar dual rate discount rate can be applied in England and Wales with similar considerations as in these other jurisdictions. We would counsel against this approach and caution that these other jurisdictions have crucial differences to England and Wales, including being much smaller, processing significantly lower claim volumes as well operating within different litigation systems.

[1] NHS Resolution continues to drive down litigation - Annual report and accounts published for 2021/22 - NHS Resolution

It is worth noting that in a report prepared by the Ontario Rules Committee in April 2021 recommendations were made that the jurisdiction should:

a) return to a single rate (i.e. abandoning the dual rate completely); or alternatively
b) that the 0% 'floor' on the short term rate of the dual rate be abandoned (thereby leaving open the potential for a negative rate for the short term period) and reduction of the rate for the long-term from 2.5% to 1%.

Further consultation and engagement

We recognise that the present call for evidence is simply an exercise to explore the option of a dual/multiple rate. However, we would stress that it is vitally important that there is further consultation and engagement with all stakeholders as matters progress.

We understand that there is a commitment to do so and that is of particular relevance with regard to the work of the expert panel in view of their important role in the process.

Questions

- *Question 1: Do you have a preferred model for a dual/multiple rate system based on any of the international examples set out in the Call for Evidence paper (or based on your or your organisation's experience of operating in other jurisdictions)?*
  Please give reasons with accompanying data and/or evidence.

  It is impossible to state a preference definitively based on any of the examples as it depends on the precise structure and methodology proposed, in particular the short and long-term rates and any switching point. In our view it is also necessary to compare any dual/multiple rate system proposed to the single rate system currently in operation.

  The minimal number of periodical payment orders ('PPOs') sought under the current discount rate, and the fact that no real data has been supplied relating to the actual rates of return on investments achieved by claimants at present – would all point to a conclusion that the current system and discount rate provides adequate compensation for claimants.

  We have seen conflicting terminology being used in relation to the various options ('switched', 'stepped', 'blended', 'graduated') previously described by GAD, and the attempt to sometimes fit those definitions onto discount rate regimes currently used in other jurisdictions when a direct comparison is not available (or not appropriate). It is important to ensure consistency in terminology to avoid confusion and misunderstanding. We further believe that there are different interpretations of how those options might apply in practice in other jurisdictions and therefore it is again important that when considering the various alternatives, that everyone is clear as to the precise methodology adopted.

  When assessing the potential benefits of a dual or multiple rate, we have considered the four options set out at paragraph 61 of the Call for Evidence and set out the strengths and weaknesses within this answer and the answer to Question 2.

a) Dual rate “switched” system based on duration (called the Ontario model) – this is in essence an approach where the short-term rate is applied to damages before the switching point and then the long-term rate takes over and is applied thereafter.

Our understanding of a switched model is as set out in the GAD report of 2019: namely, that the long term rate applies to all damages beyond the switching point (and is to be contrasted with the blended model discussed below).

This would appear to us to be the most viable dual/multiple rate option. It appears to reflect more fairly the investment cycle, recognising the greater risk to those with shorter life expectancies while also accepting that higher rates of return will be available to those claimants investing their damages awards over a longer term.

It would not, in our view, add a greater level of complexity to the current single rate model.

It should also remove the need for any additional ‘prudence factor’ to be applied, as the short and long-term rates provide sufficient additional protection to the principle of full compensation. (If suitable discount rates are based upon the assumption that damages are invested on the basis of a risk profile ‘less than would ordinarily be accepted by a prudent and properly advised individual investor’[2] then application of a further ‘prudence factor’ risks ‘double counting’ this element of protection for claimants, thus departing from the ‘100% compensation’ principle.)

When considering this model, the switching point is crucial and should not exceed 15 years. Similarly, the methodology for fixing the short and long-term rates is a vital factor. Caution should be taken when setting the short-term rate as it would not be desirable to weight the system too far in favour of a certain small class of claimants.

b) A multiple rate system (Hong Kong) – this is effectively a multi-rate “stepped” approach where the rate applied is determined by the duration of the total loss period.

This type of system simply adds unnecessary complexity, and is superfluous bearing in mind the typical investment period of 43 years as referenced in the GAD report 2019. The three rate periods applied appear to have no correlation to the typical durations of loss currently observed, nor to any particular economic cycle.

We agree with the observations made by Martin Clarke, Government Actuary in his advice to the Lord Chancellor dated 25 June 2019 when he said:

“*Whilst it is clearly feasible to set more than two rates I consider that using three rates would not lead to materially superior outcomes or improvements and I believe it is reasonable to keep the claims settlement process as simple as possible. Accordingly, I have considered only a dual rate approach.*”

That type of system is likely to create additional costs, disputes, uncertainty and “cliff edges” at the various switching points.

c) A two-tier dual rate system (Jersey) – a dual rate “stepped” approach where for loss periods before the switching point the short-term rate is applicable throughout, or for loss periods exceeding the switching point, the long-term rate is applicable throughout.

[2] See Damages Act 1996 Schedule A1 para 4(3)(d)

Similar issues arise as in b) above and we do not see any particular benefit to claimants in arriving at fair and full compensation. The 'cliff edges' still apply and implementation of a two-tier dual rate system would likely result in much more contentious expert evidence around the issue of life expectancy.

d) A dual rate system based on heads of loss (Ireland)

This would add yet more complexity and cost than b) and c) above. Furthermore there is a real risk of gaming and adverse behaviour resulting, as parties seek to tailor evidence and the claim to ensure the best possible outcome.

For example, a litigant might seek to ensure that as much of the compensation was allocated to the 'care' discount rate (if that was set at a rate that was perceived as being more favourable); rather than focussing on equipment/property adaptations/adapted vehicles etc. which might facilitate greater independence. Doing so would encourage claimants to be more dependent, not independent. Satellite litigation is another likely consequence of such a system.

In any case, in order to achieve the aim of avoiding over or under-compensation, there will still need to be a long and short-term approach to investment of damages. Having a *heads of loss* based discount rate does not avoid the problems of a claimant with a short life expectancy not being able to achieve the same kind of investment returns in relation to the care that they need because they are investing over a short period. Hence such a proposal would not meet the fundamental concern of the perceived difficulty with the current 'blunt instrument' of a single discount rate, which assumes an average investment period of 43 years, and does provide for account to be taken of the short and longer-term investment position.

Any attempt to combine systems of short and long-term discount rates, together with different rates in respect of different heads of loss, would inevitably create a complex and unworkable matrix of potential discount rates, and in turn create uncertainty in terms of being able to value and settle cases fairly. All litigants (whether claimants or defendants), and the court system itself, will benefit from an approach which provides clear and predictable valuation of claims.

Blended/graduated approach

While it is not listed as an example, we are aware of the blended/graduated system referenced in the GAD report of 2019. As far as we are aware, this model is not presently in use in any other jurisdiction(s), and so that is perhaps evidence of itself that it is an unattractive and unnecessarily complex system. Such a model does not reflect actual investment practice, and therefore results in the risk of significant over-compensation.

Summary

In conclusion, out of the examples quoted, we believe that the dual rate "switched" system based on duration of damages award (referred to as the 'Ontario model' within the call for evidence) is the preferred model, and the proposal which best encapsulates the principle of full compensation without adding undue complexity, or risking creating many adverse consequences.

Whether it is a 'fairer', better and more practical option to the single rate currently in operation depends on the precise methodology applied when fixing the short/long-term rates, and the switching point.

- *Question 2: What do you consider to be the main strengths and weaknesses of the dual/multiple rate systems found for setting the discount rate in other jurisdictions?*

  There are strengths and weaknesses to the various dual/multiple rate systems, just as there are with the current single rate system. Once again it is difficult to comment in the abstract, absent further detail on the type of dual/multiple rate system proposed and the way it would be structured.

  In general terms therefore we see the main strengths and weaknesses as follows:

  Strengths:

- The ability to deal more fairly with those claimants who have short life expectancies;
- A more 'scientific' approach with the ability to reflect and counter volatility in short-term investment returns;
- The fact that they are present in other jurisdictions and in many cases have been for several years;
- The ability to reflect different inflationary measures across different heads of loss;
- The ability to remove the need for any additional prudence when setting the rate;
- In a dual-rate system over the duration of the claim with a switching point, the greater stability of the long-term rate and the fact that is higher reflecting the reality of real investment returns available.

  Weaknesses:

- The additional complexity in operating a system based on dual or multiple rates;
- The likely additional costs and delays involved in resolving claims under such systems;
- The greater uncertainty for litigants in accurately valuing claims;
- The increased risk of satellite litigation;
- The risk of 'gaming', especially between different heads of loss and either side of any switching point;
- The prospect of additional and costly expert evidence assessing life expectancy;
- The attempt to arrive at a more precise mathematical calculation to assess full compensation which is impossible and illusory;
- Weighting a system more in favour of the minority of claimants at the extremes of short/long life expectancies as opposed to deriving a fair system across all claimants;
- The greater uncertainty that arises in a system with potentially multiple rates, a switching point and more regular reviews.

- *Question 3: What do you consider is the optimal point for the switch-over from a short to a long-term rate on a duration-based dual rate model?*
  Please give reasons with accompanying data.

  In the Government Actuary's report in June 2019 it was noted that economic cycles tend to last for around five years, though some can last longer. Also economic forecasters tend to look at trends over the next 10-15 years.

  Other jurisdictions that have switching points range from 5 to 20 years.

In the call for evidence, it is noted at paragraph 21 that the Ontario model would suggest an optimal period for a switchover to be at around 10 years.

It is to be remembered that one of the main aims of a duration-based dual rate model is to help those with shorter life expectancies (or shorter periods of loss) and previous data referred to by GAD suggests that the vast majority of cases having life expectancies in excess of 10 years (an average of 43 years).

For cases where there is a very short life expectancy because of the severity of the injury, it is very rare for life expectancy to exceed 10 years. Hence from a severity of injury perspective a switching point of 10 years might be more appropriate.

On balance, however, in light of the above typical cycles for economic trends and forecasting, while there is certainly an argument to maintain a switching point of 10 years, we consider the optimal switching point is 15 years.

We again agree with the observations of the Government Actuary Martin Clarke who in June 2019 supported a switching point of 15 years. He made the point that higher or lower switching points were possible and that adjustment by five years in either direction accompanied increasing or reducing the short-term discount rate by something in the order of 0.5% would maintain “equivalence”.

- *Question 4: What would you consider an absolute minimum and maximum point for the switch-over between two rates to be?*
  Please give reasons.

  For the reasons set out above we believe that the minimum period should be 10 years.

  The maximum point we consider should be 15 years. Such was the conclusion in the GAD report of 2019 and it is also perhaps instructive to note that Ontario has had a switching point of 15 years for the last 22 years (and for all that time the long-term rate beyond the switching point has never altered).

- *Question 5: If a dual rate system were to be introduced, would you advocate it was established on the basis of the duration of the claim with a switchover point, on duration based on length of claim or its heads of loss (or a combination of the two)?*
  Please give reasons for your choice.

  In the event that a dual rate system were to be introduced, we would advocate it was established on the basis of the duration of the claim with a switchover point, similar to the Ontario jurisdiction.

  For the reasons highlighted in our previous answers, a system based upon differing rates for different heads of loss is likely to be too complex in practice, and risks adverse behaviours and ‘gaming’, thereby resulting in increased delays and costs when dealing with claims. It also fails to deal with the fundamental concern of short life expectancies, because there would still be a need for a short-term and long-term rate for each head of claim. The matrix of discount rates would create confusion for claimants and uncertainty in valuing cases on both sides and therefore hindering settlement.

- *Question 6: In dealing with volatility of markets over the short-term is it a reasonable assumption that short-term rates in a duration-based system should be more variable and set at a lower rate; and long-term rates more stable and set at a higher rate?*
  If you agree or disagree that this assumption is reasonable, please say why.

  In principle we agree that is a reasonable assumption, but one of the key components is the definition of "short-term" and "long-term" with reference to the switching point issue as answered above. In addition, investment data and actual returns data will help to answer this question more accurately.

  A significant limitation of the last PIDR review was that the Government Actuary did not have access to data and evidence required by the Act. Hence there was a need to rely upon *Monte Carlo* computer modelling to forecast investment outcomes according to model portfolios. It is important that lessons are learned so that accurate data is obtained in good time before the review in 2024, in order that the Lord Chancellor can have regard to the factors specified by statute in Schedule A1 para 4(5)(a) and (b) of the Act.

  There have been times when market conditions are highly favourable and stable and it would be inadvisable in our view to make assumptions based upon events at a point in time where conditions may be less favourable.

  Claimants will still have the benefit of legal and financial advice and it is important therefore to ensure that any short-term rate is not so low to effectively result in no risk. The requirement in the Act is to assume that damages are to be invested at more than a 'very low risk', and that applies irrespective of whether rates are being calculated for the purposes of a single or dual-rate system.

  The long-term rates would be anticipated to be higher, to reflect the higher rates of return available to an investor selecting a portfolio of investments to generate a return over a longer period of time.

  Furthermore, in a dual rate system which is said to cater more fairly for volatility, there should be no need when setting the rates to factor in any further discount for "prudence"; this is already provided for by the statutory requirement that the Lord Chancellor must assume that damages are invested 'using an approach that involves … less risk than would ordinarily be accepted by a prudent and properly advised individual investor'. Application of different rates for short and long-term periods further removes the argument that such an additional reduction should be applied.

  There is a concern in the market that some commentators have advocated an approach of 'very low risk' analogous to a pension fund arrangement which is contrary to the clear statutory definition in the Act.

- *Question 7: If short-term rates are more volatile, should frequency of review be increased?*
  Please explain your reasoning.

  While superficially that may seem appropriate, we do not necessarily believe it to be necessary or desirable. There is already a statutory requirement to review at least every five years with discretion to review earlier. As explained in our answer to Question 6 (above), there are periods of time when there is little economic volatility (and investment returns and returns on investments are therefore stable); it is important not to 'over-provide' in any system, particularly when the Act enables the Lord Chancellor to trigger an earlier discount rate review in the event of significant changes in the economic climate.

  The main reason to avoid greater frequency of reviews is that such would create significant uncertainty for claimants and compensators. Parties benefit from certainty to ensure the smoothest, fairest and quickest resolution of claims possible. The court service already experiences significant difficulty and backlogs in listing trials, and will not be further assisted by litigants seeking to 'game the system' by attempting to expedite

and/or delay resolution of cases, in anticipation of expected favourable/unfavourable shifts in the discount rate. A five year cycle strikes a balance between ensuring regular reviews, but providing periods of relative 'stability' between reviews.

We have seen in the past that claims stall when a review is pending as parties wait to see if that review will positively or negatively impact the value of the compensation. In a system which is already under pressure due to court backlogs and where costs are high, any further delays while parties await the outcome of reviews are to be avoided as this is not in the interests of claimants.

Finally, there are then practical implications of more regular reviews, such as the resource requirements for all sides as well as the uncertainty that may result around the setting of insurance premiums which would negatively impact consumers generally.

- *Question 8: What would you regard as the advantages of a dual/multiple rate system?*

  Please see our answers to Questions 1 and 2 above.

- *Question 9: What would you regard as the disadvantages of a dual/multiple rate system?*

  Please see our answers to Questions 1 and 2 above.

- *Question 10: What do you consider would be the specific effects on implementing and administering the discount rate if a dual/multiple rate is introduced?*

  There are some immediate practical effects on implementing and administering a new system as detailed in the Call for Evidence, with which we would agree, namely:

  1. The need for new/updated actuarial tables (such as those produced by the *Ogden* working group);
  2. IT, systems and process changes for practitioners;
  3. Training for practitioners and the judiciary.

  All of those come with a financial impact. However, it would be fair to say that all involved would in due course adapt and become familiar with any changes.

  A wider concern, however, are the additional consequences which we set out in answer to Question 11 below.

- *Question 11: In addition to specific effects, do you consider there will be additional consequences as a result of implementing a dual/multiple rate?*
  Please give reasons with accompanying data/evidence if possible.

  The additional consequences that we consider could arise are:

  1. In a dual rate system with a switching point, evidence of life expectancy around that period will become crucial. These claims are already "expert heavy" which impacts upon court time and resources, as well as increasing costs. The prevailing judicial view is to avoid the need for additional

expert evidence on life expectancy unless absolutely necessary.[3] However, as the impact under a dual rate system could well be significant to both sides, it is likely to result in an increased demand for additional expert evidence. The inevitable consequence is increased costs, increased court time being required, and delay in the resolution of claims.

2. The likelihood of 'gaming' to manipulate and 'tailor' evidence to fit the claim into the most advantageous position, whether that be a particular head of loss or duration of loss.

3. Linked to the above, in a head of loss system there is the risk of adverse behaviours to seek to maximise damages. For example if there were a different, and more favourable, discount rate for future care, then it would potentially encourage "dependence" of claimants as opposed to promoting "independence" where possible. Rather than claiming for aids/equipment/treatment/therapies, the likelihood is that claims will be formulated to maximise the compensation, as opposed to what is actually required (and in a claimant's best interests) when meeting his or her reasonable needs and ensure full compensation.

4. The added complexity, in comparison to the current single rate system, will result in increased costs as practitioners will inevitably have to spend longer in giving advice on evidence, how to present and defend claims, how to calculate offers (and how to respond to such offers) and the collation of expert evidence as above.

5. The prospect of satellite litigation increases. The risk is greater if a multiple/heads of loss approach is adopted. But also, if there are different periods of loss for certain heads of loss on the evidence, how those are calculated in a dual rate with a switching point could have major ramifications for claimants and compensators. The loss of earnings claim may only be 10 years (which could fall before a notional 'switching point' of 15 years) but the other losses could be for the rest of life (which may extend beyond the same switching point). Additional evidence and costs are likely to result in dealing with such issues as well as the risk of litigation to resolve any disputes.

6. Finally, the impact generally on the process and speed of dispute resolution. The more complex the system, with more moving parts and with the potential for more frequent reviews and changes means that offers made by either side will likely be more complex. This raises the spectre of longer lifecycles for claims and with an additional risk of disputes over whether any Part 36 offers made have been "beaten".

- *Question 12: If a dual/multiple PIDR were to be introduced would it be helpful to provide a lead in period to prepare processes, prepare IT changes etc. and if so, how long should this be?*
  Please provide reasons for your answer.

  In theory yes to allow for the necessary changes highlighted in the Ogden tables, IT systems and claims handling processes.

  The call for evidence rightly highlights the risk of gaming as changes are anticipated and implemented; history has shown that, as the period approaches for a review of the discount rate, behaviours change and claims

[3] See, for example, Dodds v Arif & Anor [2019] EWHC 1512 (QB)

potentially stall while parties await (or attempt to anticipate) the outcome of the review. Any delay in the claims process should be avoided as delays in litigation are already significant.

A three to six month lead period is probably the optimum.

- *Question 13: What do you consider would be the effects of a dual/multiple rate on a claimant's investment behaviour and what would this mean for the design of a model investment portfolio?*

  This comes back to one of the fundamental issues that we highlighted at the outset of our response. Data is needed of the actual investments and returns from actual claimants to show their investment behaviour and the returns they are securing at present and in recent years, and the legislation requires that this evidence be considered by the Lord Chancellor.

  Absent that data, any assessment of a single rate or a dual/multiple rate is necessarily artificial.

  The assumed risk profile of claimants is already determined by the Act and real data would demonstrate what is actually happening as opposed to having to rely upon assumptions.

  The fact that the vast majority of claims[4] settle on a 'lump sum' basis shows that claimants are able to manage their investments appropriately and secure appropriate investment returns to meet their lifelong needs.

- *Question 14: What do you think would be the effects of a dual/multiple rate on drawing up assumptions for tax and expenses when setting the discount rate?*

  We do not believe that any different considerations should apply whether it is a single rate or a dual/multiple rate. Claimants have the benefit of professional advice (legal and financial) which will mitigate their tax liabilities.

  Investment management expenses are typically based on the level of damages and therefore the type of discount rate system should have no bearing on those charges.

  Claimants are deemed to be low risk investors pursuant to the assumptions set out in the Act and that has a bearing on the management of the long-term fund in particular.

  As we have set out at the outset, this is another area where the provision of data showing the investment charges being paid by actual claimants is crucial.

  The estimated 0.75% currently allowed for in the single rate is a more than generous provision and that remains so, irrespective of any possible change to a dual/multiple rate.

[4] Excluding clinical negligence claims where the NHS fills the role of compensator. Such claims are atypical compared to other types of personal injury claim (both in terms of the profile of claimants bringing such claims, and also in the funding model behind the compensator - with the NHS reliant on funds derived from taxes from central government, compared to a commercial insurer who is reliant upon premium income taken before the risk event).

- *Question 15: What do you consider would be the effects of a dual/multiple rate on analysing inflationary pressures and trends when setting the discount rate?*

  This issue only really comes to the fore to a significant extent if different rates are used for different heads of loss, as noted in the Call for Evidence. We have explained earlier why we do not favour such an approach. It is also a further attempt to arrive at mathematical precision in assessing final compensation which is an illusory concept. The temptation to achieve *spurious accuracy* should be avoided. It is also a further example of how greater complexity would be introduced if different rates for different heads of losses were to be adopted.

  Inflation is just one aspect of the discount rate and it is important it is considered across the typical investment period, which was previously considered in the GAD report to be 43 years. Any short term volatility, as now, should be ignored. Such spikes, or indeed drops, are typically short lived and the assessment of inflation when considering the discount rate should not be based on that small snapshot in time.

  Current events are unprecedented but yet the Bank of England's goal is to return inflation to 2% and to keep it at that level.[5]

  Evidence of real returns available to claimants at present would enable the issue of inflation to be put into its proper context.

- *Question 16: What do you consider would be the effects on claimant outcomes of a dual/multiple rate being adopted for setting the discount rate?*

  It is difficult to properly answer this question in the abstract without knowing the type of dual/multiple rate, the level of any short or long-term rates, and (if there is one) the date of any proposed switching point. Furthermore, a comparison would need to be made against the benefits or disadvantages of continuing with the existing single rate system.

  The 100% compensation principle remains, but as explained at the outset, any suggestion that it is possible to arrive at a mathematically precise calculation which will secure the last penny of compensation for every single claimant for their lifetime is a fallacy.

  It is also impossible to consider the effects on claimant outcomes, absent any information or data on the actual investments made by claimants and the actual returns available at present. Only with that data can a true assessment be made on the outcome of changing to a dual/multiple rate system from the single rate currently in force.

  We have already highlighted that those claimants with shorter life expectancies are in the minority and are typically those who avail themselves of PPOs in any event. Thus, as referenced in the Call for Evidence, there is a risk that a change to a dual/multiple rate system places too much emphasis on that small minority of claimants (with very short periods of loss) as against looking at the whole panoply of claimants bringing personal injury claims.

[5] Indeed, most recent forecasts produced by the OBR in March 2023 anticipate that inflation will '*fall sharply to 0.9 per cent in 2024 as energy and tradables prices fall further and then oscillates around zero through to mid 2026*'.

Claimants will continue to use professional advisers to ensure that their outcomes are not adversely impacted whatever the system in place.

We have indicated earlier which of the dual/multiple rate systems are most likely to result in fair outcomes.

The key is to ensure as far as is possible fair compensation for all claimants and compensators, neither under nor over-compensation while preserving the principle of full compensation, whether that be by a single rate or dual rate. It is important too to emphasise that any system should be clear, consistent and not overly complex so that claimants can fully and easily understand the outcome of their claim.

- *Question 17: If a dual/multiple rate was adopted would it be possible to return to a single rate in future reviews, or would a move be too confusing and complex and seen as irrevocable?*
  Please give reasons.

  It is correct to say that each review of the discount rate is a separate event and must be considered as such with the evidence available at the time.

  It is in our opinion perfectly possible to return to a single rate in future reviews if a dual/multiple rate was adopted. However, the uncertainty and additional complexity of moving back and forth between single and dual/multiple rates should be avoided.

- *Question 18: What do you consider the respective advantages and disadvantages of adopting multiple rates would be, when compared with either a:*
  - single rate; or
  - dual rate.

  We would refer to our previous answers and there are far more disadvantages of a multiple rate system, being:

  1. Additional complexity;
  2. Prolonging the compensation process and the taking up of more judicial time;
  3. Likely increased costs for compensators and claimants when presenting and responding to claims and when making and advising on offers;
  4. Gaming of the system and adverse behaviours, seeking to tailor evidence and claims to fit into heads of loss with a more advantageous discount rate;
  5. Satellite litigation.

- *Question 19: If a heads of loss approach were adopted, what heads of loss should be subject to separate rates – care and care management costs, future earnings losses, accommodation, or any other categories?*

  We have already indicated that we do not believe that a heads of loss approach is suitable and we would repeat our previous answers.

  While superficially it may seem an attractive proposition, practically speaking it would actually result in a far more complicated process. As identified it would not cure one of the main concerns in relation to short life

expectancy cases. There would still be a need for a short-term rate, long-term rate and switching point to address these matters hence creating an unworkable matrix of discount rates.

Furthermore, PPOs are an available mechanism for claimants with many heads of loss.

To provide multiple rates for multiple heads of loss adds unnecessary complexity and cost as well as likely introducing adverse behaviours as the parties seek to maximise or minimise the compensation by manipulating the evidence to suit a particular rate for a particular head of loss.

It is noteworthy that in those jurisdictions where a dual or multiple rate system is in operation, there are no more than two rates and furthermore those jurisdictions have a fraction of the claims going through their legal system when compared to England and Wales.

- *Question 20: Introducing a dual/multiple PIDR could result in increased levels of complexity for both claimants and compensators. Do you agree with the assumption that this complexity will stabilise and ease once the sector adapts to the new process?*
  Please give reasons.

  Introducing a dual/multiple rate PIDR will result in increased complexity. One of the advantages of the current single rate system is its relative simplicity, both in terms of operation and understanding.

  Undoubtedly claimants, compensators and their respective advisers will adapt if a new process is implemented, but that does not necessarily remove concerns over complexity.

  The more complex the PIDR, the more challenging it is for claimants and compensators to understand and advise, for example on offers made and received, resulting in a more expensive and prolonged legal process. As set out above, a more complex system is also likely to take up more judicial time, which is not ideal for an already overstretched service. Claimants who are unable to reliably predict the end valuation of their claim risk failing to beat settlement offers, and facing adverse costs orders (which will be paid out of any damages award, thus resulting in a shortfall in compensation).

  It is for theses reason among others that in our view a multiple rate system or one with different rates for different heads of loss should be avoided.

- *Question 21: The Government remains interested in exploring the use of PPOs in relation to high value personal injury settlements. We would therefore welcome any submissions, data and/or evidence stakeholders may have in relation to the effective use of PPOs.*

  The reality is that there is already in place a perfectly workable framework to enable parties to settle claims using PPOs.

  The availability of PPOs is another reason to mitigate against going down the route of different rates for different heads of loss.

  Certain cases are settled on that basis, often where the claimant lacks capacity or where there are significant uncertainties over life expectancy.

In our experience, however, the vast majority of claims settle on a lump sum basis, not because PPOs are refused, but because that is the preference of the claimant.

There are numerous reasons why settlements on a lump sum basis are preferred and while not intended to be an exhaustive some of those are:

1. With expert advice, claimants are able to invest the lump sum without risk to secure funds for the remainder of their lives in view of the current prevailing discount rate of -0.25%;
2. A lump sum gives claimants greater flexibility to manage their settlement as they see fit;
3. Many claimants wish to have no further contact with the compensator and a lump sum settlement gives them that finality;
4. The case may be subject to a liability discount and so the claimant is already having to deal with a shortfall in their compensation award.

- *Question 22: Do you agree that using a higher PIDR to calculate the real rate of return in settlements which include a PPO element would result in a more appropriate way to adjust nominal investment returns for future inflation?*
  Please give reasons.

We do not agree that is a practical or sensible way to proceed. Indeed it may not even be permissible when looking at the provisions of the Act. While different rates are permitted for different classes of case, type of loss and duration, the Act may not permit different rates based on the method of payment of compensation, whether that be by way of lump sum or PPO.

In any event, differential rate(s) in PPO cases would add a further layer of complexity into the system, which we do not believe is either beneficial or warranted. It attempts to arrive at an artificial degree of precision which we have discussed earlier. Paragraph 120 of the Call for Evidence concedes some of the obvious difficulties with this approach.

PPOs are already available for numerous heads of loss but as in Question 21, the take up is minimal, outside of clinical negligence claims against the NHS. We have highlighted various reasons as to why they are not preferred or indeed appropriate in many cases and so this would have the potential to exclude and disadvantage certain claimants. It could actually adversely impact the desire of claimants to seek a PPO knowing that as a result their lump sum element of the award would be lower.

As we have already said, the aim should be to ensure fairness across all claimants as far as possible without seeking to overly favour those small number at the extremes.

- *Question 23: What impact would a dual/multiple rate system have on protected characteristic groups, as defined in the Equality Act 2010?*

  We do not envisage any additional impact on protected characteristic groups. Claimants will have legal representation to explain any system in place. The only issue to emphasise is one highlighted in our previous answers, namely that the more complex the discount rate is the more difficult it will be for all claimants to fully understand how their compensation is calculated, with that difficulty being potentially accentuated for protected characteristic groups.

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THE LAW SOCIETY
OF NORTHERN IRELAND

Department of Justice

Consultation

THE PARAMETERS FOR THE 2024 REVIEW OF THE PERSONAL INJURY DISCOUNT RATE FOR NORTHERN IRELAND

Response of the Law Society of Northern Ireland

July 2023

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ABOUT THE LAW SOCIETY

The Law Society of Northern Ireland (the Society) is a professional body for solicitors, regulating and representing all solicitors in Northern Ireland.

The Society represents c.3000 practicing solicitors working in approximately 450 firms throughout Northern Ireland in the public sector, in business and in the community and voluntary sector. Members of the Society thus represent members of the public, small, medium and large enterprises, government bodies and charities, making the Society uniquely placed to offer constructive comment on policy and law reform proposals across a broad range of topics.

July 2023

INTRODUCTION

The Law Society of Northern Ireland (the 'Society') welcomes the opportunity to provide the views of its members in relation to the parameters for the 2024 review of the Personal Injury Discount Rate (PIDR) for Northern Ireland (NI). In preparing this response, the Society engaged with members who represent both Plaintiffs and Defendants in personal injury actions.

The current PIDR in Northern Ireland is -1.5% and was set in March 2022. Prior to this, the rate had not been reviewed since 2001 and the Society along with other bodies expressed concerns about the impact of not reviewing the rate for an extended period, particularly due to the disadvantageous consequences for Plaintiffs.[1] The Society previously set out its view that regular reviews of the rate are important and would assist in keeping the Discount Rate at an appropriate level so that those who suffered catastrophic injuries are not over or under compensated. However, it is important to note that as the current rate has only been operational for just over sixteen months, it is not possible to gather concrete evidence of its operation in such a short timeframe. Moreover, practitioners often lose touch with clients following the settlement of a case so this presents difficulties in gathering robust evidence.

Methodology and Framework

In setting the PIDR, the Society's view is that the overarching objective should be to ensure that the Plaintiffs, who have sustained life-changing injuries, receive full compensation without under-compensation or over-compensation. Additionally, the outcome should be fair to the Defendant in not requiring them to over-compensate a Plaintiff.

The NI PIDR of -1.5% is the lowest in the UK (England having a rate of -0.25% and Scotland applying a rate of -0.75%). The view of Defence practitioners acting for defence organisations and insurers across the UK is that the lack of alignment across the UK results in them having to apply different rates to different books and markets, which over complicates matters. On the other hand, it is important to note that the jurisdictional differences:

1. In relation to the NI market, the population is considerably smaller.
2. There are a limited number of insurers in NI and;

[1] http://www.niassembly.gov.uk/globalassets/documents/committees/2017-2022/justice/primary-legislation/damages-bill/written-subs/law-society-ni---30-april-2021.pdf

3. Less access to financial services in comparison to Great Britain (GB).

Regardless of these differences, Plaintiffs involved in life-changing injury cases have similar investment decisions to make as those in neighbouring jurisdictions.

In relation to those affected by the PIDR, Plaintiff practitioners note that there is a small percentage of cases of this nature in NI, and they involve the most catastrophically injured people, who are the least likely to take risks given their circumstances and overriding objective to preserve the value of their investment. It is also important to note that most catastrophic cases are taken against Government Agencies, and in particular Health Trusts. On certain occasions, the discount rate is taken out of the equation, particularly for future losses as these are often made the subject of a Periodical Payment Order (PPO).

Defence practitioners noted that the PIDR has real life consequences, for example in relation to professional indemnity cover for doctors and dentists. Plaintiff practitioners would argue that the cost would ultimately fall to the taxpayer in any event because if an individual is under-compensated, costs associated with care and treatment will fall back to the state. This emphasises the importance of the point highlighted above regarding achieving fairness for all.

In relation to the make-up of the notional portfolio, set out in Schedule C1 to the Damages Act 1996, the view of Defence practitioners is that most investors would describe it as a 'conservative' portfolio.

On the assumed period of investment (currently 43 years), the view from Plaintiff practitioners is that this is a sensible period and helps to smooth out any instability in the markets. The majority of Defence practitioners suggest that the 43-year assumed period of investment is more realistic in comparison to the model adopted in Scotland of 30 years.

Regarding the impact of inflation, it is important to note the current economic climate in the context of this review. Additionally, one must consider current interest rates and the impact this may have on the PIDR. It is the view of Plaintiff practitioners that the PIDR in NI should be reduced even further. In terms of the stability of damages over the past year since the current rate was introduced, the situation has not improved for Plaintiff clients. This has been coupled with the deteriorating financial state in the UK over the last number of months

with Retail Price Index (RPI), Consumer Price Index (CPI) and other measurements increasing at unfavourably higher rates compared to elsewhere.

In respect of the standard adjustments that must be made by the rate-assessor to a rate of return, members approached this as a standard tool used by auditors and investors to calculate anticipated return in a fair manner to be reflective of the degree of risk required to be taken by an investor. The view from Defendant practitioners is that the offsets including the 0.75% adjustment and the further margin of 0.5% are designed to protect the claimant and therefore suggest that as there is already a conservative portfolio, this is effectively double counting. Defendant practitioners believe that the further margin of 0.5% relating to the rate of return should not be added in as this may result in overcompensation. On the other hand, Plaintiff practitioners have pointed out that apart from arrangement fees increasing, the margin of these standard adjustments has been set statutorily and are not presently part of the debate. The standard adjustments are not unfair to the compensator and represent standard industry practice and are not double compensation. Currently they do not take account of the dramatic increase in earnings and nursing home fees in the last number of years which cannot be ignored as to do so could foreseeably result in a Plaintiff being at a loss.

Single v Multiple Rates

In reaching a view on whether a single or multiple rates should apply, practitioners considered whether it would be fairer for claimants to bear different levels of investment risk for different heads of damages by splitting earnings related future costs (care and loss of earnings) on the one hand and price based future costs for fixed assets (eg a wheelchair or OT aids) on the other. There is an argument that multiple rates would reduce the risk of over or under compensation and, consequently, could lead to an argument that the further 0.5% could be considered superfluous. However, the view was that the downside of adopting a multiple rate would be that it could result in creating delay, uncertainty, and additional costs for both plaintiffs and defendants. These possible unintended consequences were not acceptable to our members.

The view from practitioners was that the single rate approach provides practical advantages for both plaintiffs and defendants:

1. It is relatively straightforward.
2. It is easy to calculate and apply.
3. It provides a degree of certainty in the level of damages.
4. It allows for less complicated negotiations.

On the whole the Society therefore supports the retention of a single rate.

CONCLUSION

The Society welcomes the opportunity to submit a response in respect of the Consultation on the parameters for the 2024 review of the Personal Injury Discount Rate for Northern Ireland.

We trust our contribution is constructive and we are happy to meet with officials to discuss any of the issues raised in our response.

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By email

10 July 2023

Dear Martin,

PERSONAL INJURY DISCOUNT RATE

Thank you for your letter of 31 May 2023 regarding the Personal Injury Discount Rate (PIDR). I am responding on behalf of MDDUS. We are pleased to provide our views on the factors to be taken into account when calculating the PIDR in Northern Ireland.

MDDUS has over 1,700 members in Northern Ireland spread across GPs, dentists, hospital doctors and other healthcare providers. We provide our members with indemnity as well as with regulatory support and advice.

I will make a few general points and then pick up some points of detail.

Wider impacts of any change

The consultation is deliberately framed as an opportunity to make technical adjustments to detailed parameters used in award calculations. The questions asked are all relevant ones in that context. However, the actual decision is one that raises far wider issues of public policy in terms of, for example, the impact of the decision on NHS expenditure at the aggregate level and choices that may need to be forgone in that arena were more expensive changes to be made. Likewise, the impact on insurance and indemnity premia is a relevant factor to be considered given the current personal inflationary context and the risk that sharp increases may tempt some individuals to under-insure or may even contribute to workforce retention issues, in what is already a challenging environment. We would expect decision documents to show how these difficult trade-offs between individual and wider public goods have been evaluated and resolved in practice, particularly in relation to the retention or removal of the additional adjustment (see below).

Greater harmonisation across UK jurisdictions

As we provide indemnity across the whole of the UK, we find it unhelpful to have different PIDRs in different jurisdictions. We expect the same is true for other similar organisations. Therefore, we would encourage greater alignment of the timing, approaches and assumptions. The methodologies used in Northern Ireland and Scotland are broadly the same although there are

differences in assumptions. The approach taken in England and Wales differs both in methodology and assumptions.

The timings of the next set of changes to the PIDR look as if they will be fairly close and this ought to remove one of the causes of differences between PIDRs. Further alignment on other aspects of the calculation of PIDRs would be appreciated. As the Northern Ireland Assembly and the Scottish Government are consulting on the parameters to use, the approaches in practice are not totally dissimilar to that of England and Wales. We consider that a more formal process of setting up an advisory panel involving the Government Actuary would be possible under the current legislative framework in Northern Ireland and would provide greater consistency of outcomes across all of the UK jurisdictions.

Dual or multiple rates

A further area where the different jurisdictions could adopt different approaches is with respect to introducing, or not, a dual or multiple rate system. We would strongly encourage Northern Ireland, Scotland, England and Wales to take a consistent approach to this. We responded to the recent Ministry of Justice consultation on a dual rate and we include our response along with this paper. In summary:

- A dual rate system with a short-term and a long-term rate has merit, as it may reduce the risk of under-compensating claimants
- As the risk of under-compensation should reduce with the move to a dual rate system, the additional margin of 0.5% included within the current calculation of the PIDR should be removed
- A dual rate system will be more complicated to set up and administer so the expected benefits need to clearly justify the additional effort required.

If you decide to introduce a dual rate system then all of the parameters used to calculate the rates will need to be reviewed taking account of whether they are being used for the short term or long term rate.

Possible adjustments to factors

Make up of the notional portfolio

As we only work with defendants, we have no direct experience of how successful claimants invest lump sum awards. We encourage you to undertake further research into how claimants actually invest their awards and how their investment decisions compare to the current notional portfolio. The period of investment and the needs of the claimant should be taken into account when reviewing investment profiles. As we have commented previously, however, we are aware of claimant law firms putting in place strategies through their investment management arms clearly seeking to achieve far higher returns than those derived from the current negative rates.

Investment markets have been very volatile in the last year or two and this may continue. Part of this is due to the impact of the higher inflationary environment. It is possible that this higher level of volatility may continue and that inflation could remain higher than expected for some time to come. We appreciate that this will make setting an appropriate notional portfolio extremely challenging. We would though comment that assuming a large allocation to fixed interest investments in a high inflation environment would not be realistic. Therefore we would encourage you to increase the proportion of equities in the notional portfolio.

The assumed period of investment

The assumed period of investment relates to the life expectancy of the claimant and potentially to the profile of their cash requirements.

We have looked at the claimant life expectancy data available from schedules of loss for claims against our Northern Ireland based members. There is, however, insufficient data on which to base any conclusions. We are aware that the ABI have gathered data which shows that the 43 year assumption that you are currently using is reasonable.

Impact of inflation

It is going to be very difficult to determine how future investment returns will relate to inflation, however measured. This is also complicated by care costs inflation differing from the economy-

wide general inflation rate measured by RPI or CPI. It would be worth considering if there is justification for using the Northern Ireland inflation rates produced by the Office for National Statistics.

It will be important that the Government Actuary, as the Official Rate Assessor, provides detailed and transparent analysis of the approach taken to allowing for inflation when reporting to Northern Ireland Ministers.

We encourage you to use a consistent basis for inflation along with the other jurisdictions as currently Northern Ireland and Scotland use RPI while England and Wales use CPI. Given that the UK government will stop using RPI in 2030, we consider that it would be appropriate to move to a CPI basis.

You will need to avoid compounding the impact of recent high inflation by assuming that high inflation will persist over the whole of the investment period. The Bank of England expects to be able to bring inflation back down to its target of 2% within a few years.

Standard adjustments

We are not able to comment on the appropriateness or otherwise of the adjustment of 0.75% made for tax and cost of investment advice. We therefore encourage you to undertake further research into the impact of tax and the cost of investment advice on the investment returns to claimants.

As we mentioned above when commenting on the possibility of the introduction of a dual rate system, the additional adjustment of 0.5% should be removed if Northern Ireland ministers decide to move to a dual rate system. We remain unaware of any evidence that systematic under compensation exists at all, never mind whether this rate is appropriate to counter it. Even if such evidence existed, the way to tackle it would be through changes to the main formula to reflect the categories of cost that were not being properly identified or covered, rather than via this random figure. An adjustment in the opposite direction to reflect asserted fraud or over generous assessment would, quite rightly, be laughed out of court for its unevidenced basis. So should the current adjustment.

We hope you find these comments helpful. We would be very happy to discuss further.

Your sincerely

Dermot Grenham FIA

Company Actuary

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Response from the Medical and Dental Defence Union of Scotland to the call for evidence from the Ministry of Justice on the option of a dual/multiple personal injury discount rate for England and Wales

Introduction

The MDDUS are pleased to be able to respond to the Ministry of Justice's call for evidence to justify the possible introduction of a dual/multiple personal injury discount rate (PIDR). We are keen that whatever, if any, changes are introduced as a result of this call for evidence that they improve the working of the PIDR system for both defendants and claimants.

MDDUS is a mutual defence organisation founded by and for healthcare professionals, with an expert staff of doctors, dentists, lawyers and risk advisers who are leaders in the medico-legal and dento-legal fields. All benefits of membership of MDDUS are discretionary as set out in our Articles of Association. MDDUS is not an insurance company.

MDDUS supports and protects over 56,000 healthcare professionals across the UK. Changes in the PIDR of the type described in this call for evidence could affect us financially as a result of the clinical negligence claims we deal with on behalf of our members, particularly dentists and private doctors and GPs doing private work, in England and Wales. This would lead us to have to review our subscription rates to meet any increase in costs, something that would be particularly unwelcome by members in the current economic environment. Such changes could also have a significant impact on the public purse through the increased compensation payments made by the NHS. There is therefore a balance to be struck between providing appropriate compensation to those patients affected by clinical negligence and the amounts that healthcare professionals are required to pay for indemnity.

Changes introduced in England and Wales could also influence decisions taken in other parts of the UK something that we would also need to consider when setting subscription rates.

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Question 1: Do you have a preferred model for a dual/multiple rate system based on any of the international examples set out in the Call for Evidence paper (or based on your or your organisations experience of operating in other jurisdictions)?

Please give reasons with accompanying data and/or evidence.

We agree with the disadvantages set out in paragraph 80 of the consultation paper regarding the disadvantages of a dual or multiple rate system, in particular the greater complexity of a dual/multiple rate system and consequent impact this would have on legal time and cost.

However, if the decision is made to change to a dual or multiple rate then the new approach should:

a) ensure that there is no cliff edge in the discount rate used on crossing the dual rate switch-over point;

b) require the review of the short-term rate relatively frequently, especially in times of heightened investment volatility. To avoid the review process becoming overly onerous, a clear methodology and basis for revising the short-term rate could be set;

c) reduce the risk of investment volatility for very short-term awards as there is less chance of recovering from an investment shock over a period of say 5 years than over a period of 15 years or more; and

d) take into account, when setting the assumption for the average length of long-term awards, that short-term awards can be excluded from consideration. The creation of a dual rate system necessarily involves resetting both rates, rather than starting from the present single rate as a given.

Question 2: What do you consider to be the main strengths and weaknesses of the dual/multiple rate systems found for setting the discount rate in other jurisdictions?

It would appear that the Hong Kong and Jersey models both have a cliff edge at the switch-over point, which could mean that in certain situations, claimants with a longer payment period could get a lower lump sum than claimants with a shorter payment period. This could increase legal arguments about the payment period to use which would increase cost and delay the making of payments to claimants. We consider that the risk of negative impacts of a cliff-edge ought to be avoided and, if a dual rate is introduced, that a blended approach, as in Ontario, is used to move from the short-term to the long-term rate.

We consider that a switch-over point of 15 to 20 years for a short-term rate could be too long, especially given the heightened volatility currently being experienced in investment markets. The blended approach with a shorter switch-over point could be one way of partially dealing with this or an additional very short-term rate could be introduced.

Another weakness of a dual or multiple rate system is the increase in costs associated with more frequent reviews required to combat the dual or multiple rate systems having inequitable results.

It is not clear to us that the greater cost and complexity of the various dual or multiple rate systems in place in other jurisdictions have demonstrably led to better outcomes for either claimants or defendants. It would be helpful to see evidence to justify any change to a dual or multiple rate system, otherwise any change would be based on theoretical arguments.

Question 3: What do you consider is the optimal point for the switch-over from a short to a long-term rate on a duration-based dual rate model?

Please give reasons with accompanying data.

MDDUS is not in possession of data which would enable us to identify an optimal switch-over point. It is possible that, even if an optimal point actually exists, it may vary with investment and broader economic conditions such as the level of inflation.

The decision about the optimal point for the switch-over from a short- to a long-term rate will depend on what the dual rate is designed to do. It may also depend on the structure of the dual rate, for example, whether it is two separate rates or whether the short-term rate blends into the long-term rate after the switch-over point.

Question 4: What would you consider an absolute minimum and maximum point for the switch-over between two rates to be?

Please give reasons.

As the switch-over point is the time when the short-term rate will either change to the long-term rate or at least start to be blended into the long-term rate, we think that the minimum ought to be relatively low. This would be a short period over which a claimant would generally wish to invest very cautiously as there would be limited time to make good any negative movement in the value of their investments. We therefore consider that the minimum period should be around 5

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years and the maximum period around 10 years. If the investment horizon is longer than 10 years, claimants may already start investing in more risky assets.

Question 5: If a dual rate system were to be introduced, would you advocate it was established on the basis of the duration of the claim with a switchover point, on duration based on length of claim or its heads of loss (or a combination of the two)?

Please give reasons for your choice.

We appreciate that there can be situations where having rates that vary by duration and head of loss could be advantageous to either claimant or defendant. However, we are not sure that this flexibility would outweigh the greater complexity and associated higher legal costs that would be incurred.

Varying the PIDR by both duration and head of loss would seem to make the task of setting the various rates harder and more expensive.

We would therefore have a preference, if a dual or multiple rate system is to be introduced, for a dual rate system where the rates do not vary by head of loss.

Question 6: In dealing with volatility of markets over the short-term is it a reasonable assumption that short-term rates in a duration-based system should be more variable and set at a lower rate; and long-term rates more stable and set at a higher rate?

If you agree or disagree that this assumption is reasonable, please say why.

If a dual rate system is to be introduced then we generally agree with the proposition set out in the question. Claimants who have a longer investment horizon can, in general, take greater investment risk and therefore the PIDR for those claimants could be set at a higher rate.

While the long-term rate may not need to be reviewed as frequently as the short-term rate, it should still be reviewed regularly. As well as investment returns, the PIDR also requires assumptions about inflation, tax, investment expenses to be reviewed even if expected long-term investment returns are not changing.

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Question 7: If short-term rates are more volatile, should frequency of review be increased?

Please explain your reasoning.

It would seem reasonable that if a short-term rate is introduced that it is reviewed more frequently than a single rate or the associated long-term rate would be. This may reduce the attractiveness of the dual rate system as more frequent changes in the short-term rate could affect the behaviour of lawyers in trying to speed up or slow down the resolution of cases. Frequent changes in the short-term rate would affect all cases where a blended approach to transitioning from the short-term to the long-term rate is used.

The short-term rate would also need to be reviewed more frequently to cater for changes in inflation, especially during periods where inflation is not stable.

Having frequent reviews would increase the cost of carrying out these reviews to all who take part in the process, such as the MDDUS, as well as government departments and the Government Actuary's Department.

Question 8: What would you regard as the advantages of a dual/multiple rate system?

We generally agree with the advantages set out in paragraph 79 of the consultation paper although we think that the benefits are not easily measurable and could be marginal. It may therefore not be worth the effort of introducing a dual rate system. The consultation paper itself states that a dual or multiple rate system would provide only be "a little more flexible…"

Question 9: What would you regard as the disadvantages of a dual/multiple rate system?

We generally agree with the disadvantages set out in paragraph 80 of the consultation paper. We agree that there would be additional burdens on practitioners especially in the first 1-2 years following implementation of any dual rate regime and whenever rates change in future, especially if this happens frequently. Frequent changes could add delay and cost to the litigation process. Such delays will be to the detriment of legitimate claimants, rather than simply a cause of administrative problems for defendants and their indemnifiers.

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Question 10: What do you consider would be the specific effects on implementing and administering the discount rate if a dual/multiple rate is introduced?

We would expect to have to spend additional resources on training staff to be able to deal with claims based on a dual/multiple rate. We would also expect to have to instruct expert actuaries or forensic accountants in addition to training our own staff. This will increase costs for both claimants and defendants in expert evidence.

We envisage that a dual or multiple rate system will require more regular revaluations by claims handlers, probably greater uncertainty about settlements in the short-term at least and therefore the potential for increased costs and charges for defendants and for the public purse in terms of NHS liabilities.

Question 11: In addition to specific effects, do you consider there will be additional consequences as a result of implementing a dual/multiple rate?

Please give reasons with accompanying data/evidence if possible.

Some additional consequences will be the need for insurance companies and indemnifiers to reassess their actuarial provisions for existing and incurred but not reported claims. Depending on the proportion of liabilities which would vary with changes in PIDR rates, this could cause increased volatility in their financial results, capital requirements and prices.

Question 12: If a dual/multiple PIDR were to be introduced would it be helpful to provide a lead in period to prepare processes, prepare IT changes etc. and if so, how long should this be?

Please provide reasons for your answer.

While establishing the precise timetable would depend on knowing what the changes are going to be, adding a requirement that will be making additional demands on IT resources in a period when such resources are in short supply could be potentially problematic. It would therefore be sensible to allow at least a full year, if not longer, for implementation to be planned.

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Question 13: What do you consider would be the effects of a dual/multiple rate on a claimant's investment behaviour and what would this mean for the design of a model investment portfolio?

As we do not advise claimants we don't have access to any evidence to enable us to respond to this question.

We would expect that Financial Advisers working for claimants ought to be able to provide evidence.

In theory, claimants with a short-term investment horizon ought to be advised to invest more cautiously, which would justify the use of a higher PIDR than if they had a long-term investment horizon. It would be essential to monitor actual behaviour over time, both to correct the current structural weakness of a lack of evidence on investor behaviour in setting the rate, but more particularly because of the possible need for more frequent reviews of one or both components of settlements in a dual system.

Question 14: What do you think would be the effects of a dual/multiple rate on drawing up assumptions for tax and expenses when setting the discount rate?

The estimated tax and investment costs of 0.75% was a broad average and therefore it may be introducing spurious accuracy to try to determine different estimates for the equivalent adjustments to the short-term and long-term rates or for rates for different heads of damage.

Although long-term claimants may start off with a larger pot their pot will reduce over time and investment management fees may increase as a % of the fund.

Tax rates may be very specific to the individual claimant and therefore it would seem to us to be very difficult to estimate a specific tax adjustment based on duration.

Question 15: What do you consider would be the effects of a dual/multiple rate on analysing inflationary pressures and trends when setting the discount rate?

If a dual or multiple rate is introduced then, to be consistent, the appropriate inflation rate ought to be analysed either by duration or the heads of loss. When inflation is expected to be low and fairly constant as it had been until just a couple of years ago, then this may not be that difficult. However, in economic

environments such as the one we are currently experiencing, setting assumptions about future inflation rates is more challenging.

Question 16: What do you consider would be the effects on claimant outcomes of a dual/multiple rate being adopted for setting the discount rate?

Claimant outcomes will very much depend on how they invest, which will depend in turn on how they are advised. It is not clear to us that their investment decisions, and hence their outcomes, reflect the assumptions that are made in setting the discount rates. Therefore it may be the case that, in spite of the best endeavours to improve claimant outcomes, no significant change happens, apart from increasing the cost and complexity of the system.

Question 17: If a dual/multiple rate was adopted would it be possible to return to a single rate in future reviews, or would a move be too confusing and complex and seen as irrevocable?

Please give reasons.

We think that, once we have moved to a dual or multiple rate system, it would be very difficult to move back, unless there is a significant change in the economic or investment environment which would justify moving back to a single rate system in spite of the reasons given to make the change to a dual rate in the first place.

On the other hand, there could be situations where the short-term and long-term rates coincidentally turn out to be the same so that, at least temporarily, we are in a de facto single rate system.

Question 18: What do you consider the respective advantages and disadvantages of adopting multiple rates would be, when compared with either a:

- **single rate; or**
- **dual rate.**

While we understand the reasons put forward for considering the introduction of multiple rates, we don't think that the effort required and the other disadvantages mentioned in paragraph 103 of the consultation paper, justify making this change. We consider that trying to set different rates based on

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different heads of damage would lead to additional legal arguments about the apportionment of costs between the heads of damage.

It would also require additional effort and cost at each review of the PIDR especially given how uncertain the relationship is between the various measures of inflation that apply to the different heads of loss.

Question 19: If a heads of loss approach were adopted, what heads of loss should be subject to separate rates – care and care management costs, future earnings losses, accommodation, or any other categories?

We do not think that the effort involved in setting different rates for different heads of loss would be worthwhile and could lead to additional legal costs. Splitting the heads of loss into many categories each with their own PIDR could cause confusion and be trying to attain a level of perfection that, in practice, is not achievable.

Question 20: Introducing a dual/multiple PIDR could result in increased levels of complexity for both claimants and compensators. Do you agree with the assumption that this complexity will stabilise and ease once the sector adapts to the new process?

Please give reasons.

While some of the additional complexity and cost will be incurred at the implementation of any new regime we think that on going costs, including for government at the time of each review, will continue. These ongoing costs will include those that arise from the need to instruct specialist advisers for every case which could add logistical delay as well as costs.

Question 21: The Government remains interested in exploring the use of PPOs in relation to high value personal injury settlements. We would therefore welcome any submissions, data and/or evidence stakeholders may have in relation to the effective use of PPOs.

We cannot recall recently having been asked by claimants or their legal representatives to provide compensation by means of a PPO so we have no evidence on the effective use of PPOs. All we can say is that they are currently not the claimants' preferred way of being compensated.

Question 22: Do you agree that using a higher PIDR to calculate the real rate of return in settlements which include a PPO element would result in a more appropriate way to adjust nominal investment returns for future inflation?

Please give reasons.

See our response to question 21.

Question 23: What impact would a dual/multiple rate system have on protected characteristic groups, as defined in the Equality Act 2010?

We are not aware of any impacts other than those commented on in the consultation paper.

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<table>
<tr><td colspan="2">Full name</td><td>Dermot Grenham FIA</td></tr>
<tr><td colspan="2">Job title or capacity in which you are responding to this Call for Evidence exercise (e.g. member of the public etc.)</td><td>Company Actuary</td></tr>
<tr><td colspan="2">Date</td><td>6 April 2023</td></tr>
<tr><td colspan="2">Company name/organisation (if applicable):</td><td>Medical and Dental Defence Union of Scotland (MDDUS)</td></tr>
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Please quote our reference in your reply

Our ref: PIDR/DJNI/100723TCJR
Your ref:
Date: 10-07-23

Dear Mr Moore,

Call for Evidence: Personal Injury Discount Rate

Thank you for inviting the Medical Defence Union (MDU) to make a submission to the joint evidence gathering exercise being undertaken by the Northern Ireland Department of Justice and the Scottish Government, on the Personal Injury Discount Rate (PIDR).

The Damages (Return on Investment) Act (Northern Ireland) 2022 and the Damages Act (Scotland) 1996 require the *Government Actuary* to begin reviews of the respective PIDR's on 1 July 2024. The MDU is pleased to have this opportunity to make brief observations at the outset of the preparatory work for these reviews.

I note that both reviews have a specific interest in the option for dual/multiple rates. The MDU has long encouraged governments across the United Kingdom and the Republic of Ireland to consider the merits of a dual or multiple rate approach to the PIDR, and we welcome the pro-active consideration being shown to this via this evidence gathering exercise.

In principle, we support the concept of dual/multiple rates. However, the time for determining whether multiple rates are needed, is at the time of the formal Discount Rate Review for both Northern Ireland and Scotland – not now. While I make some brief observations on various international models open to the governments of Northern Ireland and Scotland to consider, the MDU does not express a

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preference for any of them. Neither do we express a preference for any of the three principal ways dual/multiple rates could work: stepped, switched or blended. These observations are made in the spirit of open deliberation as sought by this consultation exercise.

The MDU continues to be concerned about the rate setting methodologies at the heart of both the 2022 Act and 1996 Act. Any dual/multiple rate model and its workings will only be as good as the policy decisions taken by Ministers and the quality of the evidence on which those decisions are based. Our concerns about the process for setting the PIDR(s) are manifested in the evidence base on which ministers make their decisions. Neither the Northern Ireland Executive or the Scottish Government seemingly have access to any robust evidence on how claimants are advised to invest their money in a real-world setting, nor what they ultimately do in practice, nor what returns those invested funds achieve. If the rate setting process is to be robust, with an accurate rate or dual/multiple rates set, it is essential the government obtains this evidence. In particular, it should look beyond those cases that tragically involve catastrophically injured claimants. Less significantly injured claimants might adopt very different investment strategies than a claimant who needs to ensure continued funding for vital care needs. Without this evidence, hypotheses cannot be tested – and we are concerned this underpins a policy bias towards overcompensation.

When setting a PIDR, Ministers in Northern Ireland and Scotland are obliged to consider what is the most appropriate rate to ensure a successful claimant is fully compensated. Full compensation is precisely that: no less, and no more. In 2019, the *Government Actuary's Department's* (GAD) formal advice to the Lord Chancellor was a PIDR in England of 0.25%, because this provided the best chance of a patient being fully compensated. However, the then Lord Chancellor – David Gauke – set the rate at -0.25% The stated rationale for this was to the effect that such a rate provided *an additional margin of prudence* to help ensure claimants were protected.

In Northern Ireland and Scotland, this goes further and is actually embedded within the methodology itself. An additional margin in relation to the rate of return is set at 0.5% ('the further margin') in both jurisdictions. The implication of this is a quasi-acceptance of overcompensation and a proactive move away from achieving full compensation. The financial impact on compensators – such as *Health and Social Care NI* and *NHS Scotland* – can be immense. Both governments must abandon this further margin in the upcoming and all subsequent reviews. Failure to do so renders discussions about certain dual/multiple rate models even more of an academic exercise.

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Reflecting now on the current economic climate – particularly in respect of inflation rates. In all likelihood, the economic environment in which next years PIDR reviews will take place in Northern Ireland and Scotland will be dominated by continuingly high inflation. UK rates of inflation have been at historic highs in recent months. While some signs of abatement are evident, the recovery will still likely be firmly in progress when these PIDR reviews take place. It is, therefore, vitally important that the *Government Actuary* does not attach a disproportionate focus to recent inflationary trends, but rather a focus on long-term rates and predictions for a more settled future picture.

Finally, I now turn to the approach taken to setting comparable rates in other jurisdictions, and the MDU makes the following brief observations on some of the dual/multiple rates that operate around the world.

The dual rate system used in the Canadian province of Ontario is of particular interest. In theory, there is clearly merit in exploring a dual rate approach whereby shorter-term economic factors can be addressed in a short-term rate, with a longer-term rating being activated at an appropriate time point. We note that in the 22 years this model has been in place in Ontario, the long-term rate has remained unchanged, but the short-term rate has changed 16 times.

We are aware that many proponents of the status-quo and a single PIDR, advance an argument that dual/multiple rates are complex and harder for the public to understand. In response, the MDU is respectfully saying to all these reviews that the PIDR and the rate setting mechanism are by their very nature immensely technical and complex. Hence, were there to be any further complication added to the system - providing that it leads to a more accurate rate(s) with the aim of full-compensation more achievable - it should not be beyond those involved in the PIDR to bare it.

The Hong-Kong method is not one we would endorse. We do not see any case for a middle period between the prescribed short and long-term losses. Turning to Jersey, the 'cliff edge' at 20-21 years appears impractical. A claim with a 20 year loss period results in more compensation than an identical claim with a 21 year loss period. The inevitability of legal dispute as to whether a case is a 20 or 21 year claim, is patent.

While these international models are often cited as principal examples in these discount rate discussions, there is nothing preventing a hybrid model of one or more being adopted in either/or Northern Ireland/Scotland. Indeed, it is not possible to simply transfer a model between jurisdictions, as the legal system will inevitably prompt variations.

The MDU is grateful to have had this opportunity to provide its initial views. We look forward to further engagement with the formal review of the PIDR in both Northern Ireland and Scotland.

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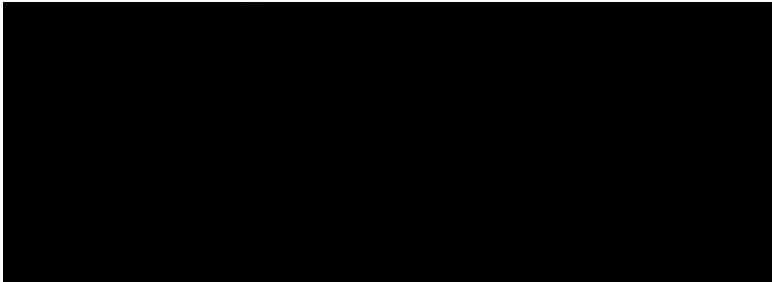
Should you require any further information from the MDU at this stage, please do not hesitate to contact me.

Yours sincerely,



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Cc.

Gearoid Cassidy, Head of Primary Care – Department of Health, Northern Ireland

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MPS

Scottish Government:

Personal Injury Discount Rate

June 2023

Medical Protection response to the Scottish Government review of the Personal Injury Discount Rate (PIDR)

Opening remarks

The Medical Protection Society (MPS) welcomes the opportunity to make a submission to the Scottish Government review of the Personal Injury Discount Rate. Our ambition is that the legislation leads to a fairer and more predictable framework for setting the discount rate.

MPS is the world's leading protection organisation for doctors, dentists and healthcare professionals with more than 300,000 members around the world, with over 6,600 healthcare professionals in Scotland.

This review is particularly relevant to us since membership to MPS provides members with the right to request indemnity for claims arising from professional practice. Changes to the PIDR have profound consequences on the cost of clinical negligence and this in turn has a significant impact on healthcare professionals. As a responsible and well-managed defence organisation, we have an obligation to reflect the rising costs of clinical negligence in membership subscription fees so we can be in a position to defend members' interests long into the future. Changes to the PIDR also lead to significant changes in the costs for the state in terms of the cost of claims against NHS.

Our claims handling philosophy aims to provide an expert, supportive and efficient claims handling service to members who are faced with claims. Where there is no defence and it is clear that a claim will be pursued, MPS will try to effect settlement on fair terms as early as possible. Where there is a good defence to a claim, MPS is robust in pursuing it. Many claims do not withstand detailed legal scrutiny and are successfully rebutted, and MPS successfully defends a significant proportion of claims.

It is important that there is reasonable compensation for patients who are harmed due to clinical negligence, but this must be balanced against society's ability to pay. We have long highlighted that if the cost of claims rises too high then the balance could tip too far, and the cost will become significantly greater for the Government, for healthcare professionals and for society.

Response

As a Medical Defence Organisation, MPS does not represent claimants or hold data on claimant investment behaviour. We are however aware of the evidence provided by the Association of British Insurers (ABI) to the 2017 Ministry of Justice and Scottish Government consultation[1] after obtaining information from Pannells Financial Planning a firm of independent financial advisers. They stated that the notional portfolio is not deemed to be accurate as there is a larger proportion of fixed investments and a lower proportion in equity investments. Using the current model, there is the potential for over compensation due to the notional portfolio being of lower risk than that which a claimant is typically likely to be recommended by a financial planning professional.

We believe claimants are reported to maintain an overall low level of risk, they are not in practice following a very low risk investment approach as we think this is the most appropriate assumption given the research compiled for the UK Ministry of Justice in 2013[2].This research found that claimants who sought independent financial advice following settlement would typically invest in a mixed portfolio (including fixed-interest accounts, property, equities, commodities, hedge funds, gilts, and notional savings) rather than investing solely in ILGS , Therefore, whilst claimants are reported to maintain an overall low level of risk, it seems they are not in practice following a very low risk investment approach.

With reference to whether to adopt a single or multiple rate, MPS is of the view that setting the discount rate should provide accuracy, transparency and stability in the assessment of damages for personal injury. There are both advantages and disadvantages to a single and a dual rate and both systems can reflect the 100% compensation principle, which is our main concern.

The main strength of the dual rate -if the one used is the Ontario model- is that it could provide compensation which more accurately reflects investment markets and claimant investment behaviour, thus making the compensation fairer. The main weakness would be that a dual/multiple rate system would add complexity and would require significant time to assess and implement.

If the Government is minded to introduce a dual/multiple rate system, MPS would advocate for the dual rate used in Ontario as this system uses a blending model which prevents from over or under compensation. We understand that the lower rate for the first 15 years of loss is based on the 12 month average rate on long term Government of Canada bonds, which like ILGS, have until recently had a low or nil rate of return. We further understand that compensators in Ontario perceive the lower rate to be an unfair burden, as like the position in Scotland, it is likely that claimants invest in a mixed portfolio of investments, and compensators are seeking dialogue with the Province to open a debate about the dual rate approach. However, we recognise that these concerns must be put in the context of the economic and litigation environment in Canada. In the context of Scotland we feel that this approach may warrant further consideration if the lower rate is subject to frequent, transparent review, to mitigate against swings in the rate, and that the longer term discount rate is fixed, ideally by statute, to provide for stability and predictability. This is why in our view while the Ontario model is an appropriate model, if applied to Scotland the review of the short term rate should not take place annually but every 3 years. This is to reduce volatility and uncertainty in the short-term rate which could lead to settlement delays associated with claims.

One of the main concerns for us is uncertainty as without knowing what the PIDR will be and what system the government is minded to introduce, it is difficult to carry out the necessary analysis to

[1] https://consult.justice.gov.uk/digital-communications/personal-injury-discount-rate/

[2] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/254856/personal-injury-discount-rate-research.pdf

determine what subscription rates and membership funds should be, which is already unsettling for us and for our members. This is the reason why we would request that if the Scottish Government is gong to introduce a dual/multiple rate, they should give a notice period of at least 24 months before installing a dual/multiple PIDR.

About MPS

Medical Protection is part of MPS, the world's leading protection organisation for doctors, dentists and healthcare professionals with more than 300,000 members around the world.

Our in-house experts assist with the wide range of legal and ethical problems that arise from professional practice. This can include clinical negligence claims, complaints, medical and dental council inquiries, legal and ethical dilemmas, disciplinary procedures, inquests and fatal accident inquiries.

MPS is not an insurance company. We are a mutual non-for-profit organisation and the benefits of membership of MPS are discretionary as set out in the Memorandum of Articles of Association.

Contact

We would be very happy to provide evidence to the inquiry. Should you require further information about any aspects of our submission, please do not hesitate to contact Patricia Canedo, Policy and Public Affairs Manager, patricia.canedo@medicalprotection.org.

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NFU Mutual Response to Scottish Government and Northern Ireland Department of Justice – Discount Rate reviews

July 2023

The National Farmers Union Mutual Insurance Society Limited
Tiddington Road
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About NFU Mutual Insurance Society Ltd

The National Farmers Union Mutual Insurance Society Ltd (NFU Mutual) is a composite insurer providing insurance, pension and investment products. We are a member of the Association of British Insurers (ABI).

NFU Mutual is a mutual company, founded in 1910. We do not have any shareholders and we therefore do not pay dividends. Our Policyholders are members of the company.
We have a gross premium income for general insurance in excess of £1.8 billion.

Consideration 1: Should the range of factors to be taken into account when calculating the PIDR in Scotland and Northern Ireland be adjusted?

Make-up of the notional portfolio

Evidence demonstrating how claimants invest their lump sum damages is not readily available however previous reports obtained by ABI and shared with the Ministry of Justice in considering the PIDR in England & Wales indicate that claimants tend to invest in a mixed portfolio of a low risk. This was accepted by the Government Actuary Department in their 2019 report to the Lord Chancellor. Within the GAD report it was outlined that the low risk, moderately cautious, mixed portfolio would contain 32.5% equities, and this was accepted and used by the Lord Chancellor in assessing an appropriate PIDR in England & Wales, however this is not reflected in the Scottish & Northern Ireland notional portfolio which assumes a 20% investment in equities.

NFUM would propose that a review of the notional portfolio in Scotland and Northern Ireland is carried out to reflect a more realistic investment portfolio as otherwise the approach is too cautious and will result in a less favourable PIDR leading to overcompensation.

NFUM fully endorse the need to ensure 100% compensation for injured claimants, however any real risk of significant overcompensation should be avoided where possible.

Assumed period of investment

Discount rates should aim to reflect returns on investment based on a low-risk investor investing over an average period of 43 years, as is the period utilised by England & Wales and Northern however Scotland has relied upon a 30-year period.

The 30-year investment period adopted by Scotland is not reflective of reality and not evidence based, NFUM would propose this should be changed to 43 years to ensure the PIDR more accurately represents the reflected realistic returns on investment.

The investment period of 43 years has been accepted by the GAD following evidence supplied by ABI in the 2019 call for evidence to support a PIDR review in England & Wales. The duration is taken from the average life expectancy for personal injury claims to which the PIDR applies, the evidence provided a breakdown of the average life expectancies for various damages values and clearly shows 30 years is too short a period with at least 75% of injured parties having a life expectancy of over 42 years and a period of 30 years assumed would more than likely result in overcompensation, especially in the £1m+ brackets.

Value Band	Life Expectancy (average)	Life expectancy >30 years (%)
£250k - £500k	42	75%
£500k - £1m	43	80%
£1m - £3m	47	80%
£3m+	50	88%

Impact of inflation (currently allowed for by reference to the retail prices index)

NFUM do not disagree that it is prudent to consider inflationary factors when setting the PDR, however caution should be exercised not to be too reactive to the circumstances and assess inflationary pressure over a longer term, ideally 43 years to reflect the average period of loss. The Bank of England strive to return inflation to 2% annually and this goal is expected to be achieved within the next few years with the aim to retain a 2% trend longer term, therefore the longer-term consideration of inflation ought to reflect this projection.

This should apply whether a single rate or multiple rate PIDR applies, it is not expected that any shorter term PIDR would be under 5 years and therefore will not be impacted by sudden spikes in inflation.

The current means of assessing inflationary factors in Scotland and Northern Ireland with reference to the RPI is recommended to be reconsidered as it is no longer regarded as an appropriate index due to its failures to meet international standards and tendency to over inflate.

In 2019, the Lord Chancellor set out within the terms of reference for GAD in the review of the PIDR in England & Wales that the PIDR (as an extension on returns of investments) should be expressed relative to CPI. NFUM support this as a more appropriate measure and recommend the use of forecasts and not historic data to calculate an appropriate adjustment factor to avoid the risk of overcompensation.

Standard adjustments that must be made by the rate-assessor to a rate of return

The current rate of adjustment applied in Scotland and Northern Ireland for the impact of taxation and the costs of investment advice and management is set at 0.75% with a further adjustment of 0.5% for the rate of return.

The impact of tax over a longer-term investment should be minimal for any appropriately advised claimant by the use of various tax wrappers to mitigate income and capital gains tax risks. These low-risk investment portfolios will require little by way of management and therefore fees can be kept to a minimum.

Given the propensity for recipients of personal injury damages to invest in low-risk investments (without the need for the active investment approaches which would attract higher taxes and management fees), the current method for calculating the PIDR in Scotland and Northern Ireland accounts for too much of these expenses and the adjustment should be reviewed downwards.
In a financial memorandum in 2018, the Scottish Government noted that under the current minus 0.75% PIDR in Scotland, ‘Awards currently average 120% to 125% even after management costs and tax’, which indicates significant over-compensation rather than under-compensation. NFUM would

propose that a rate of 0.5% should be applied in both Scotland and Northern Ireland, instead of the 0.75% currently in place in both jurisdictions.

The additional adjustment of 0.5% provides a further layer of caution and removes the PIDR further away from providing full compensation to providing overcompensation.

The impact of the lower discount rates currently in place in Scotland and Northern Ireland add to the cost of personal injury claims for both the defendant Insurers and the public purse. In addition to local authority claims experiences, the NHS has faced substantial increases in the cost of claims for clinical negligence damages awards.

In a time of austerity and uncertainty both the consumer and business are facing challenges with the cost of Insurance and the providers of Insurance in some areas has reduced creating a harder market which sustains higher premiums for policyholders.

Neither Scotland nor Northern Ireland currently have a low value claims portal process with fixed legal fees which creates disproportionate damages compared to legal costs on small to medium injury claims.

In Northern Ireland, in addition to having the lowest PIDR in the world, the average damages for personal injuries are also higher with the Green Book value bandings for injuries of a nature likely to be impacted by the PIDR on average 50-100% higher than a comparative bracket in the JC Guidelines used in Scotland and England & Wales.

The below table shows a comparison for the three UK Jurisdictions for 25-year-old suffering injuries rendering them tetraplegic, with an assumed pre-accident earnings of a modest £25,000. The examples do not take account for additional accommodation needs and are restricted solely to the average care package required in such cases and future loss of earnings.

Head of Loss	England & Wales (-0.25%)	Scotland (-0.75%)	Northern Ireland (-1.5%)
PSLA	£400,000	£370,000	£700,000
Loss of Earnings (future)	£653,000	£705,000	£794,000
Care (future)	£10,632,000	£12,214,000	£15,248,000

Consideration 2: Should a single or multiple discount rate apply and if so which model?

The question of introducing a dual rate has been raised by the recent MOJ call for evidence in England & Wales, NFUM response and considerations to this is attached for reference (Appendix A).

It would seem that a collective approach should be taken in relation to this issue across all UK jurisdictions, if possible, for the benefits of all impacted parties. In particular to make the compensation process less complicated for injured parties and avoid any costs burden for defendant Insurers having to manage alterative outcomes being passed onto to the premium paying public.

NFUM recently responded to the MOJ call for evidence in relation to the consideration for dual/multiple discount rates (see appendix A). Our view is that a "stepped", "blended" or "heads of loss" are not appropriate for introduction in Scotland or Northern Ireland as they are impractical and complex and would result in negative unintended consequences. There is a real risk of overcompensation for long term awards in the "blended" model which should also be avoided.
As outlined within that response we feel that the only approach that should be considered if a dual discount rate is deemed appropriate is a "switched" rate as it balances fairness and complexity to administer.

Within the appendix consideration points have been made in relation to the application of the various dual rate approaches, the key points are:

- Ease of application. The approach should not be overly complex for compensators or claimants.
- Clarity of how to apply the appropriate rates would be essential to avoid ambiguity and disputes on how to apply this in practice. Failure to do this would lead to confusion, added complexity and delays, and ultimately additional expense
- The date of loss should trigger the discount rate used.
- A switching point of between 10-15 years.
- The short-term rate is not factored into the losses beyond any switching point.
- The long-term rate properly reflects the returns on long term investments.
- Short term volatility is not taken into account when setting the longer-term rate.

- The long-term rate is set on the basis that it is unlikely to change (outside of the statutory 5 year review cycle)

Without the knowledge of the model to be used or the PIDR applicable it is difficult to make a recommendation as to whether a single or a dual discount rate is most suitable. NFUM's opinion is that the single rate poses a risk of over or under compensation depending on the rate being utilised, we would be in favour of the "switched" rate as the most suitable solution and method of using a dual rate to ensure 100% compensation in the fairest and least complex model, with a switch point of 15 years (as supported by the GAD modelling in the 2019 report). What must be the prevailing consideration is the correct approach to avoid significant overcompensation and complexity for fairness to those in receipt of compensation, those paying the compensation (insurers, local Government, NHS, Self-insured enterprises), the public purse and insurance premium paying consumers and businesses.

As highlighted above the lower discount rate currently applicable in Scotland and Northern Ireland, in addition to significantly higher damages awards for pain, suffering & loss of amenity in Northern Ireland together with no low value claims portal process in either jurisdiction result in a more costly and lengthy compensation process in these jurisdictions which creates negative outcomes for all stakeholders.

It is hoped a review of the approach to the discount rate may seek to achieve a greater balance, which is achievable without the risk of under compensation.

NFU Mutual Response to Ministry of Justice Call for Evidence

April 2023

The National Farmers Union Mutual Insurance Society Limited
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Question 1:

Do you have a preferred model for a dual/multiple rate system based on any of the international examples set out in the Call for Evidence paper (or based on your or your organisations experience of operating in other jurisdictions)?

Please give reasons with accompanying data and/or evidence.

There is difficulty in specifying a preference as an important factor, the rates to be used in whatever system chosen, is still unknown and thus we do not have all of the information to provide a fully informed preference. However, we will consider the merits of each option.

Dual rate 'stepped' system (Jersey) is on the face of it the most straightforward and easy to understand. All losses with a period up to the switching point are at the short term discount rate and all losses with a period over the switching point are at the long term discount rate. Due to the cliff edge encountered this creates unfairness for a claimant with a loss period just over the switching point, where they could end up with less than a claimant who's loss is just under the switching point (depending of course upon the short and long term discount rates adopted). We therefore do not think this is a preferred model.

Dual rate 'switched' system (Ontario) is in our opinion the most viable option. All losses up to the switching point are discounted and the short term rate with losses after this applying the long term rate. This avoids the unfairness caused by the cliff edge for losses with a period just in excess of the switching point. This should reduce the need for an additional prudence factor as all claimants benefit from the short term rate for their losses under the switching point.

Dual rate 'blended' is an unknown and untested option and appears to be complex. We therefore do not think this is a preferred model.

Heads of loss dual rate approach (Ireland) we consider does not fix the fundamental issue that the dual rate is intended to resolve as it is based on loss type not loss period. Therefore, short term loss claimants would be no better off under this system. PPOs can be used, and are used, by claimants who want certain heads of loss to fall outside of the lump sum payment, this is usually care and case management and therefore we do not consider a head of loss approach is needed given PPOs can already cater for this situation. We consider this approach may still require a dual rate thus adding too much complexity. We are also concerned that this could lead to gaming of the process or protracted and lengthy disputes for certain heads of loss (for example care) to be maximised over other heads (for example aids and equipment) if the former attracts a more favourable discount rate. In Ireland the two rates are very close so the risk of gaming for a more favourable rate has less impact. We wholly support a system that enables the claimant to secure full compensation, but a large part of the process is helping the claimant to achieve the best recovery they can and our concern is that the heads of loss approach may run contrary to this.

It is therefore our view that if a dual rate system is adopted the switched rate is the better option as it balances fairness and complexity to administer.

Question 2:

What do you consider to be the main strengths and weaknesses of the dual/multiple rate systems found for setting the discount rate in other jurisdictions?

This is set out in our answer to question 1.

Question 3:

What do you consider is the optimal point for the switch-over from a short to a long-term rate on a duration-based dual rate model?

Please give reasons with accompanying data.

We would agree with the conclusions from the GAD modelling in the 2019 report that the switching point should be 15 years.

The purpose of the dual rate is to ensure claimants with a shorter life expectancy are not under compensated. We therefore consider 15 years to be the optimal point as claimants with an expected loss longer that this, if the switched model is accepted, will have losses up to this period at the short-term rate and PPOs are in place and can be used for claimants with very short life expectancies. This means all claimants benefit from the better discount rate to ensure their short-term needs can be met.

Question 4:

What would you consider an absolute minimum and maximum point for the switch-over between two rates to be?

Please give reasons.

Minimum 10 years and maximum 15 years for the reasons started above. As per the 2019 GAD report a period over 15 years leads to a significant risk of over-compensation year on year.

Question 5:

If a dual rate system were to be introduced, would you advocate it was established on the basis of the duration of the claim with a switchover point, on duration based on length of claim or its heads of loss (or a combination of the two)?

Please give reasons for your choice.

We advocate a dual rate approach based on the duration of the claim with a switchover point. We consider this to be the most straightforward approach which addresses the issue of potential under-compensation for claimants with a short period of loss.

Heads of loss doesn't solve fundamental issue regarding short life expectancy claimants and could lead to gaming as stated in our answer to question 1. Personal injury claims are complex and damages are awarded for multiple heads of loss, which are not straightforward to categorise into groups by means of assessing which rate of inflation should apply to them A heads of loss approach would lead to disputes over which inflationary measure should apply which is likely to lead to the need for further expert evidence, and the associated costs of that, in an areas which is already expert heavy and where costs are significant. This would lead to increased expense, further delay and more disputes which will impact our Court system which already has significant backlogs.

A heads of loss approach, on its own, also does not deal with the issue of potential under compensation for claimants with a short period of loss.

If a combination approach were selected there would be multiple discount rates on each and every claim. As stated above there is already significant expert evidence and costs in personal injury claims and a combination approach would add to this significantly. We do not consider a combination approach could work.

Question 6:

In dealing with volatility of markets over the short-term is it a reasonable assumption that short-term rates in a duration-based system should be more variable and set at a lower rate; and long-term rates more stable and set at a higher rate?

If you agree or disagree that this assumption is reasonable, please say why.

Agree short term rate should be lower but linked to switching point. The later the switching point the higher the rate should be.

Question 7:

If short-term rates are more volatile, should frequency of review be increased?

Please explain your reasoning

There is a statutory requirement to review the discount rate every five years and we do not think there is a need to review the short-term rate more frequently.

More frequent reviews would create significant uncertainty for claimants and compensators. Under the current legislation there is already a mechanism for an earlier review which could be used in the event of exceptional market volatility.

We have seen in the past that claims stall when a review is pending as parties wait to see if that review will positively or negatively impact the value of the compensation. In a system which is already under pressure due to court backlogs and where costs are high, any further delays while parties await the outcome of reviews are to be avoided in our opinion.

Finally, there are practical implications of more regular reviews, such as the resource requirements for all sides as well as the uncertainty that may result around the setting of insurance premiums which would negatively impact consumers generally.

Question 8:

What would you regard as the advantages of a dual/multiple rate system?

The advantage of a dual rate system is there is less chance of short-term loss claimants being under compensated, and thus a better chance of achieving 100% compensation for all claimants. A separate rate for long term claimants will be better able to reflect investment return prospects over the longer term. This should reduce overall levels of compensation and benefit consumers in the insurance market

We also consider that the introduction of a dual rate would negate the need for the current methodology of reducing the single discount rate by -0.5% to counter the risk of under-compensation. The risk of under-compensation was greater for claimants with a short-

term loss and the introduction of a dual rate would mean this risk is already addressed and therefore no longer a need for additional prudence.

Question 9:

What would you regard as the disadvantages of a dual/multiple rate system?

This will depend in part on the system adopted. We consider the disadvantages are the increased complexity for all parties involved (new and more complex Actuarial tables); greater risk of legal challenge (leading to increased expert evidence / increased costs / potential delays / more litigation); challenges around new processes and IT systems to accommodate the changes.

This is why we would advocate, if a dual rate is adopted, it should be a switched dual date as this is the fairest with a review every 5 years which would provide certainty to claimants and compensators, efficacy and confidence.

Question 10:

What do you consider would be the specific effects on implementing and administering the discount rate if a dual/multiple rate is introduced?

We consider the effects would be increased complexity and therefore a need to ensure compensators, solicitors and the judiciary understand the new system. There would need to be system changes for practitioners to ensure the new calculations could be done for the purposes of reserving and creating schedules and counter-schedules. New Ogden Tables will be needed.

If a dual rate is adopted the methodology for this would need to be set out clearly to avoid ambiguity and disputes on how to apply this in practice. Failure to do this would lead to confusion, added complexity and delays, and ultimately additional expense.

Question 11:

In addition to specific effects, do you consider there will be additional consequences as a result of implementing a dual/multiple rate?

Please give reasons with accompanying data/evidence if possible.

Depending upon which system is chosen life expectancy could become a more contentious issue, particularly if this is borderline with the switching point. This could lead to additional expert evidence being required, increased costs and more delays.

Question 12:

If a dual/multiple PIDR were to be introduced would it be helpful to provide a lead in period to prepare processes, prepare IT changes etc. and if so, how long should this be?

Please provide reasons for your answer.

This may depend upon which option is chosen as some may be more complex than others. There will be a need to update systems and train staff which will take time however a long lead in time may lead to a delay in settlements, which we should aim to avoid. We therefore consider a 3 to 6 months lead in time to be appropriate.

We would encourage the sharing of the methodology of the dual / multiple rate at the earliest possible time to enable processes and IT changes to begin before the rates are shared.

Question 13:

What do you consider would be the effects of a dual/multiple rate on a claimant's investment behaviour and what would this mean for the design of a model investment portfolio?

There is a lack of evidence about claimants' investment behaviour available and therefore we are not able to comment on whether we think this would be affected by a dual/multiple rate system.

Question 14:

What do you think would be the effects of a dual/multiple rate on drawing up assumptions for tax and expenses when setting the discount rate?

Given the lack of evidence about claimants' investment behaviours we do not see a need to change the assumptions from those made by GAD in the 2019 report. Until evidence is provided on the actual tax and expenses incurred this should remain at -0.75%.

Question 15:

What do you consider would be the effects of a dual/multiple rate on analysing inflationary pressures and trends when setting the discount rate?

The majority of claimants have a long term loss and thus we need to avoid allowing short term inflationary events, which by their nature are volatile and hard to predict, to influence the setting of the discount rate. We consider the long term view should be taken for the assessment of the value of inflation

Question 16:

What do you consider would be the effects on claimant outcomes of a dual/multiple rate being adopted for setting the discount rate?

We consider a dual rate switched approach will produce fairer outcomes to all claimants.

Question 17:

If a dual/multiple rate was adopted would it be possible to return to a single rate in future reviews, or would a move be too confusing and complex and seen as irrevocable?

Please give reasons.

We see no reason why a return to a single rate would be too confusing or complex.

However, given the system changes needed to deal with a dual rate we would want to avoid a regular switch between single and dual rate as this would lead to uncertainty for reserving and planning and could also lead to increased costs associated with the changing of systems.

Question 18:

What do you consider the respective advantages and disadvantages of adopting multiple rates would be, when compared with either a:

- single rate; or
- dual rate

We feel there needs to be a balance between the aim to achieve 100% compensation and the complexity involved in this. The principle of 100% compensation is artificial as it is an attempt to financially compensate for future losses using expert evidence to guide this, but it is inevitably fraught with uncertainty.

We consider multiple rates cause too much complexity without materially improving outcomes for claimants. Similar to our answer on heads of loss approach, a multiple rate system will lead to increased costs and expert evidence as there would be multiple discount rates on each and every claim. There is already significant expert evidence and costs in personal injury claims and a combination approach would add to this significantly.

We therefore consider a single rate or switched dual rate would be preferential to multiple rates.

Question 19:

If a heads of loss approach were adopted, what heads of loss should be subject to separate rates – care and care management costs, future earnings losses, accommodation, or any other categories?

We do not consider a head of loss approach should be adopted for the reasons stated in answer to questions 1, 2 and 5.

PPOs already exist to enable a claimant to remove certain heads of loss from the lump sum settlement.

Question 20:

Introducing a dual/multiple PIDR could result in increased levels of complexity for both claimants and compensators. Do you agree with the assumption that this complexity will stabilise and ease once the sector adapts to the new process?

Please give reasons.

Complexity for compensators and claimant representatives is likely to stabilise and ease but for claimants it will always be complex as this is likely to be the one and only time they will have to be involved in a large claim, hence for them it will always be novel and we therefore need a system which is easy to explain and for a claimant to understand and make sense of. The more complex the method chosen the more difficult it will be for all claimants, practitioners and the judiciary to understand.

We therefore consider the switched dual rate to be the most appropriate as this has the right balance of fairness and ease of understanding.

Question 21:

The Government remains interested in exploring the use of PPOs in relation to high value personal injury settlements. We would therefore welcome any submissions, data and/or evidence stakeholders may have in relation to the effective use of PPOs.

> We have 13 active PPOs in the last 10 years and 12 of these are on-going. There are no trends with our PPOs in terms of claimant life expectancy and in our view the appetite for a PPO is particular to an individual claimant's circumstances.

Question 22:

Do you agree that using a higher PIDR to calculate the real rate of return in settlements which include a PPO element would result in a more appropriate way to adjust nominal investment returns for future inflation?

Please give reasons.

> We do not agree that further complexity is needed.

Question 23:

What impact would a dual/multiple rate system have on protected characteristic groups, as defined in the Equality Act 2010?

> Whilst claimants are legally represented and are provided with advice we consider the system needs to be easily explainable to and understood by claimants. Therefore we would advocate against a system which is overly complex.

Response to NI/Scottish call for evidence June 2023

General

It is difficult to comment on the factors associated with the calculation of the PIDR without understanding and commenting on the basic model. Accordingly, following is a brief description of the current PIDR model as I see it, designed (i) to highlight the differences between the old and the new regimes, and (ii) to compare and contrast the E&W approach with that in Scotland and Northern Ireland (NI). There are significant differences between them and the models were calibrated at different dates. The upshot is three quite different PIDRs, viz., -0.25%, -0.75% and -1.5% when one might have expected a more uniform result.

No other country produces single PIDRs with anything approaching this degree of variability, indeed, for the most part, they have discount rates that have remained unchanged for decades. The UK, by contrast, has handed responsibility in large measure to the Government Actuary who is using a model prevalent in the insurance and pensions world where it is used to internally model technical reserves and respond to credit rating agency queries, as distinct from real world, i.e., PIDR, projections. The use of Economic Scenario Generators (ESGs) in the UK is, therefore, both unique and problematic.

UK discount rate summary

	From	To	Period years	Gross time return (RPI)	Tax % pts	Tax Rate						Unrounded PIDRs	Rounded PIDRs
UK	Pre-Wells		NA	6.00%	-1.50%	(25%)						4.50%	4.50%
	16/07/98	27/06/01	3.0	3.28%	-0.49%	(15%)						2.79%	3.00%
	28/06/01	20/03/17	15.7	2.46%	-0.37%	(15%)						2.09%	2.50%
	21/03/17	04/08/19	2.4	-0.83%	0.00%	(0%)						-0.83%	-0.75%
	NEW REGIME			Gross time return (RPI)			Switch to CPI	Wages	Tax & fees	Impact of withdrawals	Prudent margin	Unrounded PIDRs	Rounded PIDRs
	05/08/19			1.60%			+1.0%	-1.0%	-0.75%	-0.7%	-0.5%	-0.35%	-0.25%
Scot	08/02/02	27/03/17	15.1	2.46%	-0.37%	(15%)						2.09%	2.50%
	28/03/17	30/09/19	2.5	-0.83%	0.00%	(0%)						-0.83%	-0.75%
	01/10/19			1.20%					-0.75%	-0.7%	-0.5%	-0.75%	-0.75%
NI	28/06/01	30/05/21	19.9	2.46%	-0.37%	(15%)						2.09%	2.50%
	31/05/21	21/03/22	0.8	-1.78%	0.00%	(0%)						-1.78%	-1.75%
	22/03/22			0.50%					-0.75%	-0.7%	-0.5%	-1.45%	-1.50%

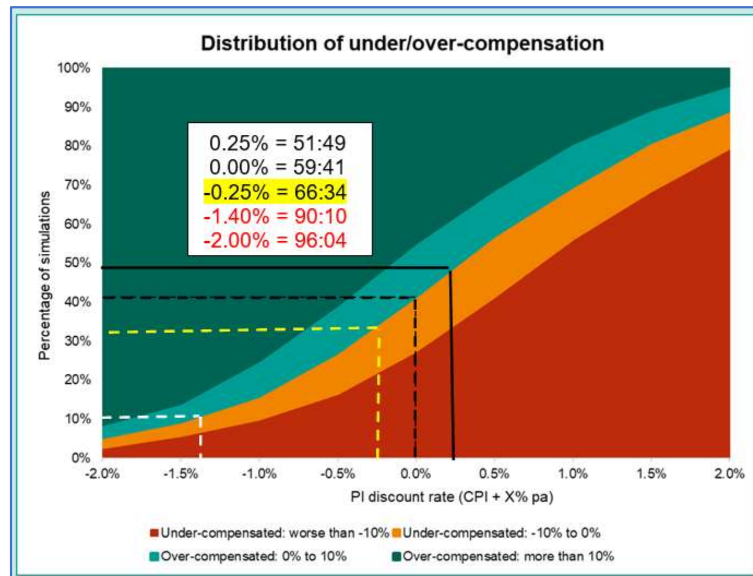
NB: blue/green shading = PIDR based on ILGS yields; orange/red = low-risk mixed basket PIDR based on simulated porfolio returns. Impact of withdrawals reflects the switch from a time return to a money return. Sources: UK MOJ, GAD, NI DOJ and author.

A summary of the components of the various UK PIDRs is set out in the Table. The switch to the new calculation methodology produced a negative PIDR of -0.25% for England & Wales which endures pending the first five-year review in 2024.[1] It was accompanied by several innovations highlighted in orange:

1. *The RPI was replaced by the CPI, this added 1% to the PIDR;*
2. *A new damages/wage inflation allowance of 1% was introduced – this conveniently offset the switch to the CPI. In practice, the GA calculated a 2% real wage differential but applied only half of this without explaining why – it appears he made a crude assumption that wage-related items accounted for half of a typical lump-sum claim and applied an average 1%. As it happens, a real wage assumption of 1% was broadly appropriate, however, as the 1% adjustment was applied across the board, i.e., there was no differentiation between wage-related and non-wage-related claims, it followed that non-wage claims were overcompensated by 1%.*
3. *A new tax and fees allowance of 0.75% was introduced in place of the 15% tax deduction in Wells (subsequently reduced to zero by Lord Chancellor Truss for E&W and by the Ministry for NI). This was needed because of the higher taxes and expenses associated with investing in a mixed basket.*
4. *An allowance for the impact of capital withdrawals, i.e., there was a switch from a time-weighted to a money-weighted averaging approach, which lowered the PIDR by 0.7%.*
5. *A new and controversial "margin of prudence" was introduced which reduced the rate by 0.5% based on obscure, Monte Carlo, random modelling exercises, conducted by the UK*

[1] *This was another disappointment to defenders as the Government had, on 7 September 2017, announced to the Stock Exchange that "Based on the evidence currently available the Government would expect that if a single rate were set today under the new approach the real rate might fall within the range of 0% to 1%." The discrepancy reflected the impact of unanticipated innovations such as the 0.5% "prudent margin".*

Government Actuary (GA).[2] The idea is that if the average portfolio return is, say, 2.5%, this is the median return and there is an infinity of other possible returns above and below the 2.5%.[3] One half of the investors will, therefore, be overcompensated while the other half will be undercompensated. No other country has sought to allow for this and few outside the actuarial profession would countenance it. The 0.5% prudent margin is designed to increase the proportion "overcompensated" from half to two-thirds, i.e., still leaving one-third "undercompensated", a further reflection of the questionable nature of the exercise. Finally, as the curve is asymptotic to the axis, it is impossible to achieve 100% compensation no matter how low the PIDR is set – see chart below produced by the GA which shows that a minus 2% PIDR would still leave 4% of claimants "undercompensated".[4]



6. *Strangely, the GA ignored life expectancy where one could make a similar point, viz., that the expected remaining lifespan is no more than the mid-point of a range of possibilities, i.e., half of claimants will be overcompensated because they will die sooner, and the other half will be undercompensated because they will live longer. This is why one occasionally sees people like Chris Daykin, the former UK GA, suggesting that a second 0.5% "margin of prudence" should be deducted to reflect this. This further underlines the surreal nature of the "prudent margin" exercise.*

The new UK PIDR system suffers from several defects, some of them major:

(i) *It is completely opaque – other countries, e.g., Ontario, by contrast, strive to ensure that their regimes are so transparent that the calculations can be replicated without difficulty. In contrast to the previous, ILGS regime, it is not possible for anyone outside the GAD to replicate the calculations underlying current UK PIDRs.[5]*

(ii) *The results are subject to erratic short-term influences – see difference between the Scottish and NI PIDRs in the Table above. The main reason for the difference appears to be an unusually high inflation assumption which, in turn, indicates that short-term market movements have an undue influence. This is a far cry from Wells where it was held to be*

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[2] *A book published in March 2020 by John Kay, well known economist, and Mervyn King, former Governor of the Bank of England, strongly criticized the notion that risk is as readily quantifiable as Monte Carlo and other statistical analysis tools assume.*

[3] *The GA initially modelled 1,000 simulations, then doubled that to 2,000 – others go as high as 10,000.*

[4] *"The then Lord Chancellor justified his decision to add an additional margin of prudence to the PIDR by arguing that claimants would need an additional safety net against under-compensation. This is not a convincing argument. … For future reviews, we will work very hard indeed to make a very strong case against the – in our opinion – unlawful additional margin that the Lord Chancellor added to the rate. This additional margin is a fundamental shift away from the 100% compensation principle that Parliament agreed was an important principle in setting the rate and means that claimants are now more likely to be over- rather than under-compensated." Huw Evans, former DG of ABI, Gibraltar, 20 Nov 2019.*

[5] *The GAD refuses to release details of the Economic Scenario Generator (ESG) models used or their detailed results on the somewhat questionable grounds of confidentiality as they are hired proprietary models.*

important that the calculations should be simple as well as accurate and should not change too often.

(iii) *The 1% allowance for higher wages means that non-wage-related claims are overcompensated by 1%,*

(iv) *The prudent margin results in overcompensation of 0.5%.*

The Scottish and NI models are similar, save that they continue to be based on the RPI and no allowance is made for (higher) wage inflation – two factors that are assumed to be equal and offsetting.

In his modelling, the GA makes extensive use of the spectacularly mistitled Economic Scenario Generators (ESGs) – in reality they are statistical scenario generators which are devoid of economic content. The origins of ESGs can be traced to 1986 when D Wilkie produced a new type of model that used stochastic (random) regression techniques within a cascade (layered) model structure to generate simulations of economic variables (interest and inflation rates) and capital market returns (stocks and bonds).

> *"The purpose of this paper is to present to the actuarial profession a stochastic investment model which can be used for simulations of "possible futures" extending for many years ahead… The model described in this paper is for the use of the actuary, and I do not pretend that it competes with other methods, either statistical or economic, of obtaining short term forecasts".* [6]

Nowadays, two common applications drive the increased use of ESGs:

1. **Market-consistent valuation work for pricing complex financial derivatives and insurance contracts with embedded options ("market-consistent" models).** This application is mostly concerned with mathematical relationships within and among financial instruments and less concerned with forward-looking expectations of economic variables.

2. **Real-world models for risk management work in calculating regulatory capital and rating agency requirements.** These applications are concerned with forward-looking potential paths of economic variables and their potential influence on capital and solvency.

In practice, we are concerned with the latter.

According to the Society of Actuaries:

> *"The purpose of an ESG is thus to provide a reasonable representation of the full range of future dynamics and distributions of economic and capital market variables, so that risk can be appropriately assessed and risk mitigation strategies can be evaluated. Therefore, ESG models are not intended to be predictive, and there is no requirement that the models provide any insight about why the economy works the way it does. The primary objective of an ESG is to produce a set of scenarios that represent the type of economic conditions that may occur in the future." (emphasis added)*

This indicates that while ESGs can be used to produce thousands of simulations/forecasts for economic variables such as interest and inflation rates, the primary objective is to use them as inputs to simulate possible but unlikely, impacts on insurance company capital or pension funding sensitivities, i.e., simulations, not predictions. It seems to me that, in the present instance, ESGs are being used to predict interest rates and inflation, something they were not intended to do. The various GA reports state that they are cross referenced to a variety of other forecasts and house views, however, it is not possible to verify this due to the paucity of information provided by the GAD.

The GA methodology is convenient, not least because it would be difficult to produce an alternative solution. However, this should not be excluded. New Zealand has long been an innovator at the forefront of public finance. The NZ Treasury produces a real discount rate curve five times a year – the accompanying chart shows the end June evolution over recent years.

In contrast to the GA, they set out clearly their modelling framework and parameters – see Appendix A. In general, their approach shows greater stability even though it is also used for valuing insurance liabilities. Since 2019, their Ultimate Forward Rate (UFR) or long-term discount rate, has remained unchanged at 2.3%. Like the GA, they use bond yields to determine the shorter end of the curve which they then bridge to the UFR. The NZ bond yield curve extends out to about 30 years following which

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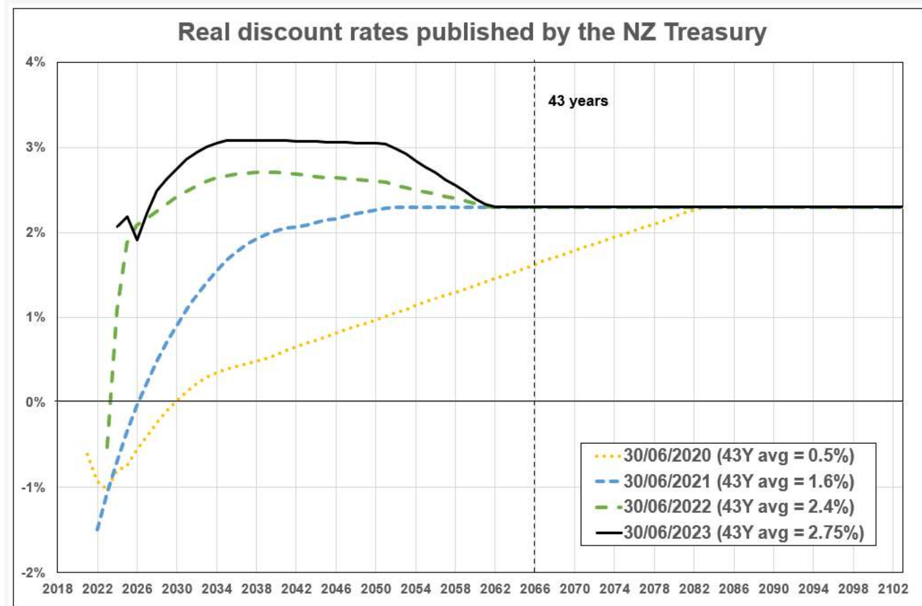
[6] *A stochastic investment model for Actuarial use, Wilkie, A.D., Transactions of the Faculty of Actuaries 39 (1984-86) 341 – 403.*

they use a bridging period of 10 years, i.e., by 2060 market-based discount rates have converged on the UFR.[7] It would be interesting to know how long a bridging period the GA uses and whether this contributes to the volatility observed in his results. As the GA modelled an average 43-year period, I have shown the average NZ discount rates over that term – leaving aside 2020, they range from 1.6% to 2.75%. These figures would compare with the GA's E&W, Scottish and NI gross time return figures of 0.5%, 1.2% and 1.6%, respectively, in the table above (more realistically, 1.5%, 2.2% and 2.6%, if one substitutes CPI for RPI). Viewed from this perspective, the GA's figures do not appear unreasonable though it is unsatisfactory that he adopts a "black box" approach and is not more transparent.



Average life expectancy

It is undesirable and confusing to have different PIDRs for different parts of the UK which has a single financial market and should, therefore, have a single PIDR. It follows that the portfolios and their assumed duration should be identical. This applies in particular to the unusually short 30-year period incorporated in the Scottish legislation. This compares with an average of 43 years used in England, Wales and NI. Even the 43 years may be too short as it was merely the average of a 40 to 45-year range cited by various respondents to MOJ consultations and calls for evidence, and the life expectancy for a one-year-old child is now 88 and 91 years for males and females, respectively, per the Office for National Statistics (ONS), and many of the most severe claims relate to damages at birth. Accordingly, I recommend a close look at the average life expectancy which I would expect to be closer to 45.

The only evidence for this type of thing comes from interrogation of real-life cases, something which the vast bulk of the respondents, the writer included, to whom this call for evidence is addressed cannot do. In large measure, this explains why repeated consultations and calls for evidence by the UK MOJ have been so unproductive (with exceptions in 2000 and 2017). It is astonishing that the only proper survey of damages and how they are invested, dates from the Law Commission Report No. 224 of September 1994.

RPI

The RPI is now an anachronism and it is strange that it is used in Scotland and NI but not in the UK. The opportunity to correct this anomaly should be taken. I realise that this poses practical difficulties. However, the E&W solution, i.e., offset CPI with a 1% real wage allowance, while surprising at first sight, has something to recommend it.

Wage inflation

In his 2019 Report, the GA said:

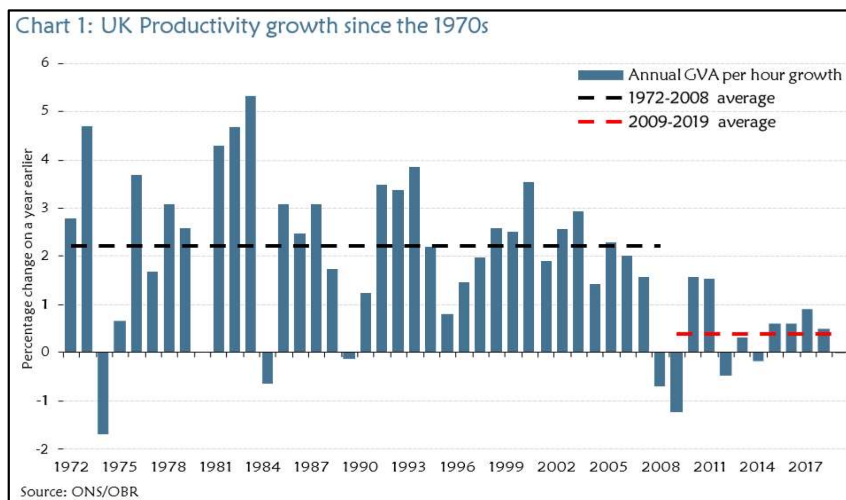
[7] 2020 was an exception when they lost their nerve and briefly used a 30-year bridging period.

"There was no evidence or clear consensus from the Call for Evidence as to the varying levels of inflation that apply to different award components or in what proportions. It is fair to say therefore that the assumed level of inflation remains open to judgement but that some aspects are likely to be linked to general consumer prices (i.e., CPI linked) and some aspects linked to movements in earnings.

In the absence of any firm evidence, I therefore believe it reasonable to assume that claimant's damages inflate at CPI+1% pa and have accordingly included this in my analysis."

The GA determined that the gap between wage and consumer inflation was 2% but then proceeded to arbitrarily halve it to a 1% allowance. The GA did not explain how he derived the 2% but included a table of simulations out to 50 years showing a 2.2% differential which he rounded to 2% before then halving it. It is likely that the 2.2% was based on a long-term average. However, use of such averages is highly contentious. The GA sometimes determines his own wage assumptions and sometimes defers to the Office for Budget Responsibility (OBR).

The OBR's Fiscal Sustainability report sets out long-term economic forecasts, including for productivity and wage growth, which it uses to project the budgetary aggregates and assess whether they imply a sustainable path for public sector debt. Its forecasts are sometimes cited by the UK GA as forecasting is not something that actuaries are well suited to as they are statisticians rather than economists.[8]



The OBR's March 2020 Economic and Fiscal Outlook contained a material downward revision of their long-term productivity and wage growth assumptions.[9] Between 2008 and 2019, UK output per hour (which determines real wages) grew by an average of just 0.3 per cent a year, compared to a little over 2% over the preceding four decades – see Chart 1 produced by the OBR – the period covered in the chart is approximately 50 years. Their overall conclusion was:

> *"… the continuation of the weakness seen since the financial crisis has led us to revisit our assumption that productivity growth will ultimately recover to around its pre-crisis trend rate. Consequently, in this year's FSR, we will assume that it returns to a steady state of 1.5 per cent a year by 2036-37".*

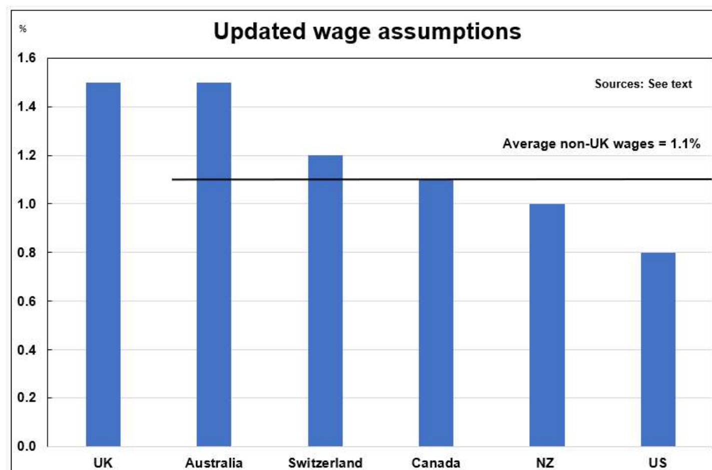
The OBR also looked at other long-term forecasts in the UK and elsewhere. They found that their 2.0% assumption was out of step as a range of UK forecasters had lowered their productivity assumptions to about 1.5%, as had the US, Australia and New Zealand. This reinforced their doubts, prompting them to jettison their 2% assumption in favour of 1.5%.

While the OBR have not changed their 1.5% assumption in the meantime, the other countries cited by them have moved on and, outside of the UK, the average real wage assumption is now 1% - see chart below. In my view, 1% is a more appropriate assumption for real wage growth at the present time. What is needed is a simple rule of thumb that is reviewed every five years. In normal circumstances, the

[8] *In Simon v Helmot [2012] UKPC 5, Chris Daykin's attempt to convince the Court that actuaries were also economists was rebuffed and only the economist, Roger Bootle, was allowed give evidence on the real wage differential and a similar approach was adopted in Thomson [2015] SC (Bda) 37 Civ (22 June 2015).*

[9] *https://obr.uk/publications/economic-and-fiscal-outlook-march-2020/*

OBR (and similar economic forecasters) are best placed to provide this.



Therefore, a 1% allowance for real wages growth remains appropriate even if the experience of recent decades is for zero or negative real wage growth.

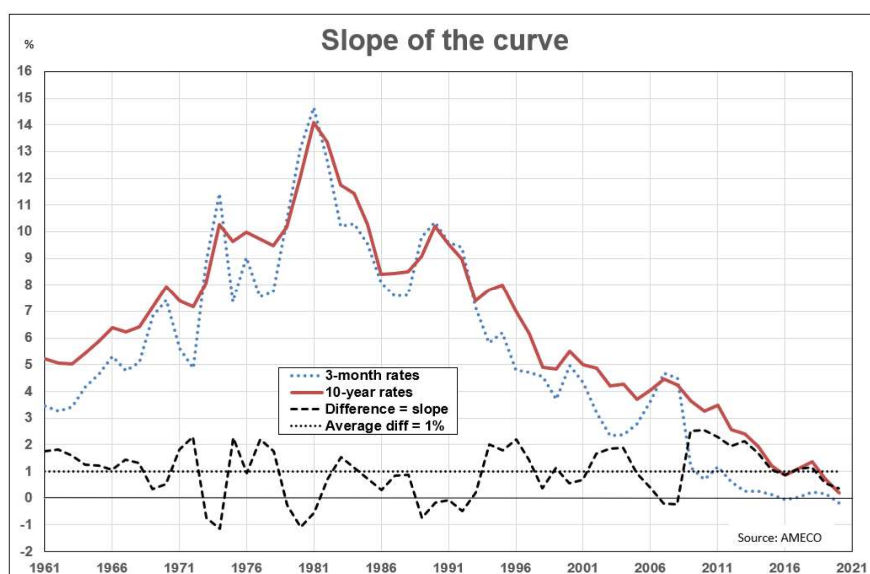
Margin of prudence

See comments above and Appendix B attached.

Multiple PIDRs

The only way to properly and accurately compensate claimants is to have dual rates by claim type, one for wages and another for non-wage claims. While UK commentators, notably the legal profession, consistently oppose this, they have no experience of how it would operate in practice, and it seems to operate without difficulty in ROI, Ontario and Hong Kong. Moreover, E&W has already taken a step towards dual rates by head of claim without following through to the logical conclusion. There should be no need for further evidence on this and it is unlikely that any will be forthcoming.

The case for dual PIDRs by time has already been made by the GA in his 2019 report. There is usually a big difference between short and long-term rates i.e., the yield curve slopes upwards reflecting the higher returns and risk that are a feature of investment for longer periods. This, in turn, means that a single PIDR will inevitably overcompensate long awardees as the expense of those in receipt of lump sums designed to last for shorter periods.



The chart above shows short and long-term average rates for seven countries - Belgium, Germany, France, Italy, Neths, UK and US - used by the European Insurance and Occupational Pensions

Authority (EIOPA) to calculate their Ultimate Forward Rate (UFR), or risk-free long-term discount rate. Every now and then, the yield curve inverts, i.e., short-term rates exceed long-term ones. In fact, this occurred about 20% of the time between 1961 and 2020. However, most of the time, long rates exceed short ones, i.e., the yield curve is normal or upward sloping and, in the example below, the difference between short rates, as represented by three-month money, and long rates, in this case 10-year yields, is about 1% on average. The gap between money market rates and longer-term bonds (20Y+) would be even greater.

In his 2019 review of the PIDR, prepared for the Lord Chancellor, the UK GA said:

> *"Currently, it is a feature for expected investment returns to be low in the short term but to increase to more normal levels over the longer term. This means that the expected outcomes for a claimant investing over the next 10 years are markedly different to a claimant investing over 50 years".*

He explained that this was because, in the short term:

- *expected returns were lower,*
- *there was limited time over which to recover from any poor investment returns, and*
- *there was also limited time over which to build up excess funds from good investment returns.*

As a result, claimants with a shorter investment horizon were proportionately more likely to experience under-compensation. Effectively, this meant that a single rate system discriminated against those with shorter awards.

Real portfolio money weighted returns			
	10Y	43Y	50Y
Cautious portfolio: 30% allocation to growth assets	0.70%	1.50%	1.70%
Central portfolio: 42.5% allocation to growth assets	1.20%	1.90%	2.10%
Less-cautious portfolio: 55% allocation to growth assets	1.60%	2.30%	2.50%

Accordingly, the GA modelled a time-based, dual rate, structure with a 15-year switching point. For this, he assumed that a claimant with a shorter 10-year award invested in the more cautious low-risk portfolio while the longer, 50-year, award was invested in the less-cautious portfolio. He also assumed that claimants investing over longer periods invested in longer-dated bonds and vice versa. The results are shown in the Table above.

The short 10-year investment produced a return of 0.7% while the 50-year investment yielded 2.5%, a difference of almost 2% - this would have reflected cautious assumptions and the typical difference between long and short rates on investment portfolios is usually greater. By comparison with the 43-year representative portfolio, the longer investor gained 0.6% (2.5% - 1.9%) but the short-term investor lost 1.2% (1.9% - 0.7%). A single PIDR based on the 1.9% central return overcompensated the long investor who could afford to boost his returns by taking more risk but seriously undercompensated the short investor.

The short-term investor was at a disadvantage and this held true even if they threw caution to the winds and invested in either the central or the less-cautious portfolios. The assumption of additional risk boosted their returns to 1.2% and 1.6%, respectively, but both were still below the 1.9% on which the standard award was based. On all three scenarios, an investor with a 10-year lifespan/investment horizon was undercompensated and the under-compensation was greatest when the most appropriate (cautious) portfolio was adopted. The long investor, by contrast, could choose either the central or riskier portfolios and still comfortably beat the 1.9% single PIDR. The dice was well and truly loaded.

Summary Table	Dual Short	Single Standard	Dual Long
Portfolio money returns	0.70%	2.00%	2.50%
Tax & charges	(-0.75%)	-0.75%	(-0.5%)
Damages inflation	(-1.00%)	-1.00%	(-0.00%)
GA rates pre 'prudent margin'	**-0.75%**	**0.25%**	**1.50%**
Prudent margin deduction	(-0.50%)	-0.50%	**
Lord Chancellor's PIDR +		-0.25%	
Implied dual rates	**-1.25%**		**1.50%**
** The GA said there was no need for a prudent margin deduction			

The various deductions and allowances modelled by the GA, varied with the structure, and are set out in the Summary Table above. While there was full transparency as regards the components underlying

the derivation of the single PIDR, the position regarding the deductions in the case of the long and short rates was less clear and the figures quoted did not add up. The areas of uncertainty are indicated by the pink shading in the Table. However, the GA's final position was clear – before allowing for a prudent margin, the dual rates he calculated were minus 0.75% (short) and plus 1.5% (long). As the GA stopped short of recommending a dual regime (and the Lord Chancellor opted for a single rate pending further study), the Lord Chancellor's final dual regime figures were never definitively outlined. However, they are relatively easy to deduce and allowing for the prudent margin, the short PIDR would have been -1.25% and the long PIDR, 1.5%. We are, of course, unclear as to how the 1.5% was derived. In principle, a short PIDR should apply for claims up to a 10-year duration and be recalculated yearly, much as is done in Ontario. A long PIDR could be calculated by the GA but it would be best if this was done in a transparent manner, preferably without the use of ESGs.

In the 2017 UK public consultation, an array of different interests including (ex-GA) Daykin, the Association of British Insurers (ABI), NHS Resolution, Scottish actuaries, the Association of Personal Injury Lawyers (APIL), and some financial advisers, all favoured dual time-based rates. In evidence to the UK Scrutiny Committee on the Civil Liability Act 2018, the ABI stated that the industry favoured a dual or "stepped" rate option. The NHS made a detailed submission containing simulation exercises before concluding:

> *"The Ontario system appeared to better balance the interests of both claimants and defendants by avoiding the "grossly excessive lump sums that were currently applicable on cases with a long-life expectancy" at the same time as protecting a claimant in the initial years".*[10]

Thus, the two major UK defendants, the NHS and the ABI, as well as the leading claimant representative, APIL, were all in favour of a time-based dual-rate system. It is unlikely that the current Call for Evidence can add much to this. Short and long-term PIDRs have to be blended which poses issues – see Appendix C.

In short, this means having four PIDRs, two for wage-related claims, one short and one long, and two for non-wage claims, one short and one long.

Pat McArdle

Economist

11 July 2023

[10] *NHS Resolution's reply to the Ministry of Justice Consultation on The Personal Injury Discount Rate: How it should be set in future, May 2017 obtained under FOI.*

Appendix A

The New Zealand approach

Table 1: Eight step framework for determining the Treasury risk-free discount rates and CPI assumptions

Period	Step	Proposed process
Short to medium-term assumptions Short-term: up to four years Medium-term: five to 29 years (until 15 May 2051, the latest maturity date of a Government nominal bond)	1	Determine risk-free discount rates for the first month from the yield on one month Overnight Index Swaps (OIS). Use OIS rates as additional data points in the first year.
	2	Determine any adjustments required to the nominal Government bond yields to give short to medium-term risk-free discount rates.
	3	Determine the smoothed market forward rate curve with reference to OIS and nominal Government bond yields
	4	Determine short to medium-term CPI inflation assumptions.
Long-term assumptions Long-term: greater than 39 years (or later if maximum slope applies)	5	Determine the long-term real risk-free discount rate.
	6	Determine the long-term nominal risk-free discount rate.
	7	Determine the long-term CPI inflation from the above, cross-checked against available market and historical data.
Assumptions for bridging the short to medium and long-term	8	Determine the method of blending short to medium-term and long-term rates.

	Modelling parameter	Proposed/current value
5	Inflation risk premium adjustment to breakeven inflation	-0.30%
6	Weighting given to inflation forecasts: weighting given to breakeven inflation	50:50
7	Long-term real return	2.30% pa (compound 2.25%)
8	Long-term CPI inflation	2.0% pa
9	Long-term nominal discount rate (forward rate)	4.30% pa
10	End of market observations (nominal discount rates and CPI inflation)	End of nominal yield curve (currently 15 May 2051)
11	Start of long-term assumptions	Greater of end of nominal yield curve plus 10 years (currently 15 May 2061) or as determined by the maximum slope of the bridging assumption
12	Bridging assumption – nominal discount rates	Linear between the end of market and the start of long-term with a maximum slope of 0.05% per year of duration
13	Bridging assumption – inflation	Linear between six months prior to the maturity date of the last inflation-indexed government bond and the end of the bridging period for nominal rates

Appendix B
The Prudent Margin

Introduction

ESGs are random because they rely on Monte Carlo simulation, a process identified during the second World War. There is little doubt that it works, albeit in certain well-defined situations. The problem with the GA's approach is that these situations do not include financial market returns. For example, if you toss a coin, you know with certainty that the outcome will be either a head or a tail. In financial markets, by contrast, you have no idea what the outcome will be and 2022 was a good example, with UK gilts and index-linked bonds recording the worst returns in the 123-year history of the Barclays Equity Gilt Study, viz., -34% and -34.6%, respectively.[11] While equities fared better in 2022, their history includes a fall of 58% in 1974, followed by a rise of 100% in 1975. It is not easy, in my opinion impossible, to find a model that can cope with these outcomes. However, that is precisely what the GA is attempting and, moreover, using it not just to "predict" future investment returns, but also to produce the probability distributions used to calculate the prudent margin. Whatever about the former, the latter is particularly egregious.

FIGURE 1. **Real investment returns by asset class (% pa)**

	2022	10 years	20 years	50 years	123 years*	Max	Min
Equities	-11.5	2.6	3.8	4.5	4.8	99.6 (1975)	-58.1 (1974)
Gilts	-34.0	-3.3	0.0	2.4	0.9	57.5 (1921)	-34.0 (2022)
Index-Linked	-34.6	-1.8	0.8			18.9 (1993)	-34.6 (2022)
Cash	-10.9	-3.3	-1.8	0.7	0.5	41.5 (1921)	-16.6 (1915)

Note: * Entire sample.
Source: FTSE, Bloomberg, Refinitiv Eikon, Barclays Research

The word 'scenarios' refers to randomly generated simulations using a Monte Carlo driven model which produces (thousands of) scenarios and should not be confused with the more traditional use of the term whereby a central macroeconomic forecast is provided sometimes with a few possible alternative scenarios. Monte Carlo is a statistical rather than an economics process and one of the issues with the 2019 UK review of the PIDR is that it was controlled by actuaries apparently with little or no economic input.

Monte Carlo Simulation

Monte Carlo simulation is used in numerous fields, (science, engineering, and supply chain management) as well as finance. The technique was first developed by Stanislaw Ulam, a mathematician who worked on the Manhattan Project during the second world war. While recovering from (brain) surgery in 1946, he entertained himself by playing countless games of solitaire. He became interested in plotting the outcome of each of these games in order to observe their distribution and determine the probability of winning. While individual events were random, he found that multiple repetitions had non-random characteristics. Ulam frequently spoke of his uncle who had a gambling habit and would borrow money from relatives because he "just had to go to Monte Carlo", hence the name. The method was first

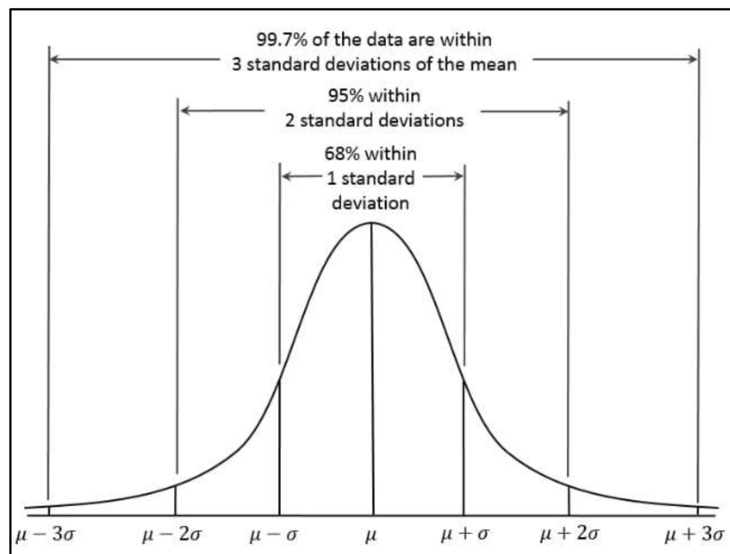
[11] The figures in the Barclays Study are understated by about 1% because the deflator is RPI which overstates inflation. On the other hand, they do not allow for a money-based approach that would reduce then by about 0.75%. Overall, therefore, they are a reasonable approximation of the returns available to claimants on a portfolio with regular withdrawals.

used in development of the Hydrogen Bomb and subsequently expanded to a wide array of fields including finance. [12]

A Monte Carlo simulation takes an uncertain variable and assigns it a random value. The model is then run and a result obtained. This process is repeated again and again while assigning the variable in question with many different, computer-generated, random values. Once the simulation is complete, the results are averaged together to get an estimate. By generating an arbitrary but high number of simulations, it is possible to assess the probability that a variable will follow a given trajectory. These random simulations take the form of a bell curve or normal distribution – see chart below.

The Monte Carlo simulation method is complex, difficult to understand, and requires lots of (costly) data – some applications compute up to 10,000 scenarios whereas the GA initially proposed 1,000 then doubled up to 2,000 which still looks low. It is only possible because of advances in computer power and microchip technology. Crucially, Monte Carlo simulations ignore everything that is not built into the price movement (macroeconomic trends, company leadership, hype, cyclical factors, etc., etc.); in other words, they assume perfectly efficient markets.

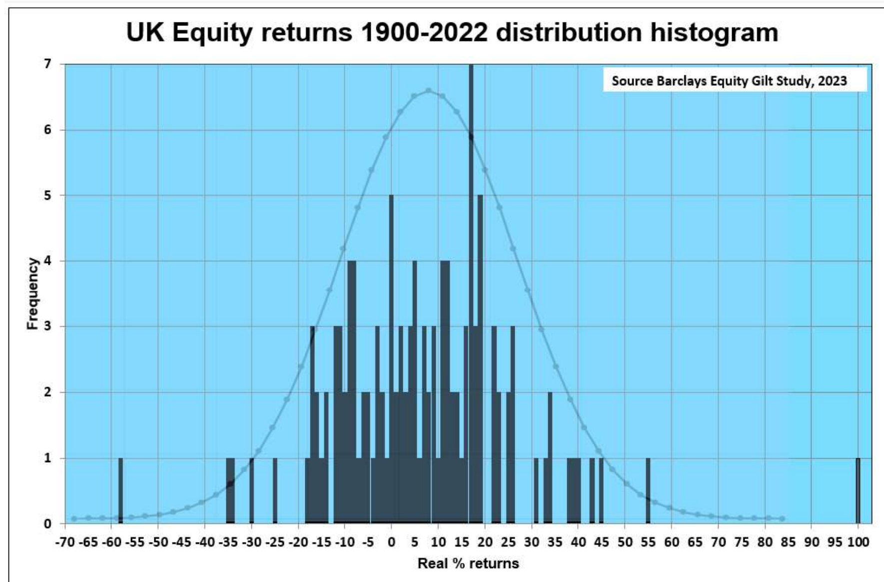
Standard deviation is a measure of the dispersion, or deviation, of returns around a central expected value. By virtue of the attributes of a normal curve, the probability that the actual return will be within one standard deviation, + or -, of the most probable ("expected") rate is 68%; that it will be within two standard deviations is 95%, and that it will be within three standard deviations is 99.7% - see chart below. Still, there is no guarantee that the most expected outcome will occur, or that actual movements, albeit rare, will not exceed the wildest projections – 2022 being a case in point. A normal distribution has a bell shape and the vast majority of occurrences fall close to the mean. The further out you go, the fewer occurrences there are. Human height is a good example of a normally distributed statistic, i.e., for everyone who is taller than average there is someone who is shorter, but the vast majority are around average height.



We next look at the underlying data to assess whether or not it conforms to a normal distribution. If it does, then the frequency histogram should be similar to that in the chart above. The chart below shows the frequency distribution of UK real equity returns over the past 123 years. It is immediately obvious that the equity distribution does not resemble the normal or bell curve which is superimposed on the chart. In a normal curve, the mean or average, median

[12] *Its use in finance (insurance) was boosted by the requirement under the EU Solvency 2 post 2008 crash regulations to calculate one in 200 events which implied use of distributions, though these involved internal simulations where the regulator wanted to impose extreme levels of caution, rather than future predictions.*

(middle data point) and mode (the most frequent result) are identical with the mean providing the greatest number of observations or frequency, i.e., it should be the apex of the curve with an equal number of observations on either side. In the case in point, the mean is 4.8, the median 6. However, the mode is 17 which appears 7 times whereas the mean and the median have frequencies of only four and three, respectively. Tail, or unexpected events, usually pose challenges and it can be seen that there are instances of equity returns of +100%, +55%, -35% and -58% that lie well outside the curve – theoretically, each of these should be close to zero.[13] If the returns were a normal distribution, the observations would all lie on or near the bell curve outline. This, alone, should cause one to pause and reflect on whether randomly generated future returns that assume a normal distribution are a useful way of assessing the probability of over or under compensation in a real-life scenario.



A book published in March 2020 by John Kay, well known economist, and Mervyn King, former Governor of the Bank of England, strongly criticised the notion that risk is as readily quantifiable as Monte Carlo and other statistical analysis tools assume. The authors' bugbear is the standard approach to uncertainty in economics and related disciplines, which requires a comprehensive list of possible outcomes with well-defined numerical probabilities attached, precisely what the GA did. In their view, this is an impoverished and, at times even fraudulent, approach to decision-making. Apart from stable and repeated situations, they explain at great length that probabilities do not exist; or they and their possible outcomes are unknowable; or all the above at once.

> *"Some uncertainties are resolvable. The insurance industry's actuarial tables and the gambler's roulette wheel both yield to the tools of probability theory. Most situations in life, however, involve a deeper kind of uncertainty, a radical uncertainty for which historical data provide no useful guidance to future outcomes. Radical uncertainty concerns events whose determinants are insufficiently understood for probabilities to be known or forecasting possible. Before President Barack Obama made the fateful decision to send in the Navy Seals, his advisers offered him wildly divergent estimates of the odds that Osama bin Laden would be in the Abbottabad compound. In 2000, no one - not least Steve Jobs - knew what a smartphone was; how could anyone have predicted how many would be sold in 2020? And financial advisers who confidently provide the information required in the standard retirement*

[13] *The situation regarding gilt returns is similar.* Over the years, *several alternative approaches have been proposed to try to cope with this issue.*

planning package – what will interest rates, the cost of living, and your state of health be in 2050? - demonstrate only that their advice is worthless.

The limits of certainty demonstrate the power of human judgment over artificial intelligence. In most critical decisions there can be no forecasts or probability distributions on which we might sensibly rely. Instead of inventing numbers to fill the gaps in our knowledge, we should adopt business, political, and personal strategies that will be robust to alternative futures and resilient to unpredictable events".[14] (emphasis added)

One does not need to be a former Bank of England Governor to realise that the prudent margin is problematical. In June 2019, the GA's advice to the Lord Chancelor was that a +0.25% PIDR was consistent with the traditional approach to the determination of PIDRs, i.e., absent the Prudent Margin, the PIDR would have been towards the bottom of the 0% to 1% range that the MOJ had earlier notified to the Stock Exchange as likely. The GA did not formally recommend any particular Prudent Margin, however, he tended towards 0.25%. Subsequently, the Lord Chancellor used the distribution data provided by the GA to introduce a Prudent Margin which lowered the PIDR by 0.5% to -0.25%. This was deemed to "overcompensate" 66% while still "undercompensating" 34%. Logically, however, if he accepted the GA's approach and believed that the distribution he supplied was meaningful, the Lord Chancellor should have opted for as near to 100% "compensation" as possible, viz., a PIDR of -2% or lower – see chart from the GA's 2019 Report in the main body of this document. There is clearly something wrong with an approach that holds that the only way to adequately compensate the final 1% is to "overcompensate" the other 99%.[15] If adopted, it would imply that the old common law 100% "full compensation" rule routinely referred to in *Wells* and elsewhere, is in need of revision. "1% full restitution and 99% overcompensation" does not trip off the tongue but it does demonstrate that the actuarial advice as regards the Prudent Margin, if pursued to its logical limit, produces nonsensical results.

In short:

(i) *ESGs are not supposed to be used as predictors but actuaries, including the GA, regularly ignore this, and*

(ii) *The Prudent Margin hinges on a probability distribution which, to quote Kay and King, is based on numbers that are "invented" and "worthless".*

[14] *Radical Uncertainty: Decision-making for an unknowable future, Mervyn King and John Kay, ISBN: 9780349143996.*

[15] *By the same token, if the GA's approach were to be adopted as regards life expectancy, all awards would have to assume the longest expected life span which again would mean that 99% of recipients would receive an award based on a lifespan greater, in many cases significantly greater, than they would experience in reality.*

Appendix C

Blending of dual time-based rates is necessary to avoid cliff edges and injustices. Hong Kong and Jersey have the most straightforward systems. If the claimant's needs are for periods shorter than the switchover point, the short rate is used; otherwise, the longer rate applies. This means that there can be a big difference in awards that fall close to but on either side of the switching point.

In his 2019 Report, the UK GA summarised the situation as follows:

> *"In terms of the way in which dual PI discount rates are applied, there are a number of approaches that could be made:*
>
> - *the PI discount rate to be used may simply depend on the total period of damages being met. In this instance, if the total period stretched beyond the switching point, then all damages would be discounted at the long-term rate. Otherwise, all the damages would be discounted at the short-term rate.*
> - *alternatively, all cashflows prior to the switching point could be discounted at the short-term PI discount rate and all cashflows after the switching point could be discounted at the long-term rate…. the claimant with a 16-year award would have the first 15 years of their damages discounted at the short-term rate and then the cashflow in the final year discounted at the long-term rate.*
> - *finally, all periods before the switching point could be discounted at the short-term PI discount rate and any cashflows beyond this discounted further at the long-term rate, for each year after the switching point. For example, the claimant with a 16-year award would have the first 15 years of their damages discounted at the short-term rate and then the cashflow in the final year 16 discounted for 15 years at the short-term rate and one year at the long-term rate".*[16]

The Hong Kong and Jersey systems are modelled on Method 1 while Ontario uses Method 3 and the GA also proposed this Method in his dual rate modelling. The GA said he believed that this approach was the most appropriate as it reduced "cliff edges" without further elaboration.

Initially, Ontario used Method one, same as Jersey and Hong Kong. However, this was challenged in *Slaght.*[17] The Defence said they understood the existing Court Rule to mean that the discount factor to be applied to the payment in year 16 should be based on the 2.5% discount rate in each of the 16 years, viz., Method one. The Plaintiff argued that this discriminated against her and, to demonstrate this, her expert witness produced an example using the then prescribed short, and long rates of 0.75% and 2.50%, respectively:

- *Scenario 1: Assume that $1,000,000.00 was payable at the end of 15 years from today (discounted at 0.75%).*
- *Scenario 2: Assume that the same $1,000,000.00 was payable 15 years plus a day from today (discounted at 2.5%).*
- *For Scenario 1, today's present value would be approximately $894,000 whereas for Scenario 2, it would be $690,500.00.*

The Judge, not unreasonably, held that it was not logical that a one-day difference in the due date of a $1,000,000 payment could yield a difference of $203,500 or 23% less, and ruled in favour of the Plaintiff,

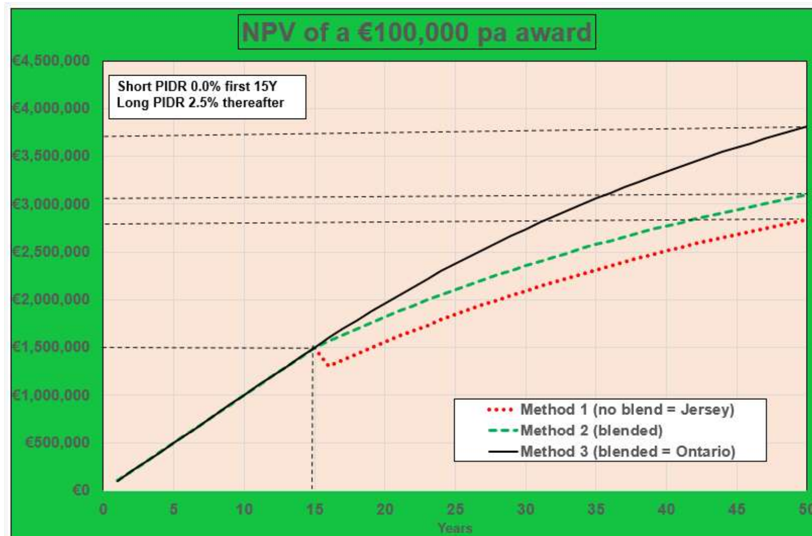
However, the Plaintiff's arguments were not rebutted by expert evidence and it appears that the Ontario Court jumped from Method one to Method three without any consideration of the in-between and less costly Method two. The consequences of this oversight are depicted in the chart below which models the results of the three methods using a 2022 example of a €100,000 award with short and long PIDRs of 0% and 2.5%, respectively.

In all three cases the PIDR for the first 15 years is 0% and the cumulative payout by year 15 is €1.5 million (100,000 x 15). Method 1 is depicted by the dotted red line and the downward kink in year 16 is obvious. Method 2, the dashed green line, removes the kink at a once-off cost of €300k. Method 3 – the solid black line – also removes the kink but does so in a manner that sees the cost escalate over time. By year 50, the cumulative costs are €2.8m, €3.1m and €3.8m, for Methods 1, 2 and 3,

[16] *Setting the Personal Injury Discount Rate Government Actuary's advice to the Lord Chancellor, 25 June 2019.*

[17] *Slaght v. Phillips and Wicaartz, 2010 ONSC 6464 (CanLII).*

respectively. The failure to use Method 2 has caused the plaintiff to be over-compensated by €0.7m or 23%. It appears that the UK GA erred by not opting for Method two which also removes the kink and produces a smooth outcome but does so in a manner that avoids significant overcompensation.



The use of Method three in Ontario means that reference to a 2.5% long rate is quite misleading as, in practice, a smoothed or blended long PIDR is calculated which results in a de facto variable PIDR that never reaches 2.5%.

The long and short Ontario rates specified for 2022 are set out in the Table below. For the first 15 years, i.e., for periods up to 2036, the 2022 PIDR was 0% in each year. However, the long and the short rates were then blended to avoid abrupt changes. This resulting year 16 rate is 0.15% instead of the expected 2.5% and it increments only gradually thereafter. By 2122, i.e., in 100 years' time, the long rate is still only 2.1% and the overall average much lower. For a claimant with a 50-year remaining lifespan, the rate for the first 15 years is 0% and for the next 35 years the blending methodology produced an average long PIDR of 1.3%, instead of the expected 2.5%. The result was an average 0.86% PIDR for the whole 50-year period. Method one would have produced a 1.75% average for the 50 years while Method two would be in between but much closer to Method one.

It is not clear whether or not the GA allowed for blending in determining the long PIDR but it appears that he did not. If so, then his 2.5% is not a good reflection of the actual, post blending, long PIDR or, indeed, of the cost of compensation when blending is included.

Ontario 2022 prescribed rates					
	Prescribed	Blended		Prescribed	Blended
2022	0.00%	0.00%	2022	0.00%	0.00%
2023	0.00%	0.00%	2032	0.00%	0.00%
2024	0.00%	0.00%	2042	2.50%	0.71%
2025	0.00%	0.00%	2052	2.50%	1.28%
2026	0.00%	0.00%	2062	2.50%	1.58%
2027	0.00%	0.00%	2072	2.50%	1.76%
2028	0.00%	0.00%	2082	2.50%	1.88%
2029	0.00%	0.00%	2092	2.50%	1.97%
2030	0.00%	0.00%	2102	2.50%	2.03%
2031	0.00%	0.00%	2112	2.50%	2.08%
2032	0.00%	0.00%	2122	2.50%	2.12%
2033	0.00%	0.00%	Centuries		
2034	0.00%	0.00%	2222	2.50%	2.31%
2035	0.00%	0.00%	2322	2.50%	2.37%
2036	0.00%	0.00%	2422	2.50%	2.41%
2037	2.50%	0.15%	Average rates		
2038	2.50%	0.29%	43Y period		0.72%
2039	2.50%	0.41%	50Y period		0.86%
2040	2.50%	0.52%	100Y period		1.42%
2041	2.50%	0.62%	200Y period		1.83%

Northern Ireland PIDR consultation response

Written evidence submitted by: Mr Richard Cropper, PFP Ltd (richard@pfp.co.uk) and Professor Victoria Wass, Cardiff University (Wass@cardiff.ac.uk)

Date: 10th July 2023

We are independent experts who have provided assistance to the courts in the jurisdictions of the UK in valuing claims for personal injury. We have both made submissions to consultations on the PIDR in England and Wales, Scotland, Ireland and Guernsey (Wass 2017, Wass 2018, Wass 2019, Wass et al 2020a, Wass and Cropper 2022). We made a joint submission to the PIDR consultation in Northern Ireland in August 2020 (Wass et al 2020b).

Richard Cropper is an independent financial adviser who has specialised in providing financial advice to recipients of personal injury damages for over 25 years. He was retained by the Lord Chancellor in 2015 to provide advice in respect of the personal injury discount rate (PIDR) (Cox et al 2015). He is a member of the Ogden Working Party.

Victoria Wass holds an Emeritus Chair at Cardiff University following over thirty years' employment there as a labour economist. She continues working as a labour economist in private practice advising on the PIDR, indexation of periodical payments and the application of Ogden Reduction Factors in the assessment of claims for loss of future earnings. She is a member of the Ogden Working Party. She was an expert reviewer for the research undertaken for the UK Ministry of Justice (MoJ) on claimants' investment behaviour (MoJ 2013).

Based on our knowledge and experience, our submission responds to the issues raised by Martin Moore in his letter of 31st May 2023 and are presented in the order in which they are raised. We add commentary on Economic Scenario Generators (ESG) in the determination of the PIDR which we believe is an important and overlooked component of the calculation.

In our responses to 1 to 6, we reflect on the existing parameters within the PIDR calculation, including a discussion of the role and impact of ESGs. At 7 we discuss the proposal to change the methodology to adopt a split PIDR with the intention to better match the characteristics and circumstances of the claimant.

1. Investment portfolio

We consider the portfolio prescribed for the Northern Ireland PIDR calculation in March 2022 at 35% in risky assets as more appropriate than the one prescribed for the portfolio in England & Wales in 2019 at 42.5%. However, a portfolio with 35% invested in risky assets is not, in our view, a low-risk portfolio.

In her submission to the England and Wales PIDR consultation in January 2019 (Wass 2019), Victoria Wass likened the position of the Ministry of Justice (MoJ) and the Lord Chancellor in selecting the portfolio mix in the PIDR to that of the professional Trustee in a defined benefit pension scheme. The Trustee is expected to act in a cautious and prudent manner to ensure that the fund can meet the future liabilities to its members on retirement. In this role the Trustee is provided with guidance by the pensions regulator (tPR). The primary role of tPR is to safeguard the government-backed pension protection fund (PPF). The text of her submission, reproduced in Appendix 1, is based on guidance and statistics published in the Pension Protection Fund (2018). Statistics for 2022 are published in Pension Protection Fund (2022) with relevant tables on asset allocation reproduced at Appendix 2. In summary, there has been a clear movement away from scheme investment in equities towards low-risk liability-matched investments. In 2006, schemes were invested in equities at around 61%. This was reduced to 27% in 2018 and 20% in 2022 (Table 7.2). For a mature pension scheme, which most closely matches the position of the claimant, schemes are invested in 7% equities (Table 7.9). The PPF itself is invested in 7% equities.

The pension Trustee is better placed to manage the risks that the fund will meet future liabilities than is the claimant because it is, or is advised by, financial services professionals and it has access to sophisticated financial instruments. The risks to the fund are also lower than those facing the claimant because the scheme is able to spread risk across members (and life expectancies) and expenditures. The claimant is seeking to meet a single liability, his or her care costs over his/her expected life-time. On this basis, the claimant's exposure to risky assets should be less than that of the average defined pension scheme (19.5%) and the PPF (7%), and not more.

We think the current inconsistency between the HMT's requirement that pension fund trustees invest cautiously and the MoJ's requirement that claimants invest more aggressively requires justification and reconciliation. It is not acceptable that Government requirements should differ so widely in circumstances which are essentially the same, without explanation.

2. Duration of compensation

We have not seen any population-representative evidence on duration of claim to indicate the average length of a claim. In the absence of such evidence, our recommendation is that the rate-setter should err on the side of a lower duration rather than a higher duration. The 30 year duration adopted in Scotland is preferable to the 43 year duration adopted in Northern Ireland but itself might be too high.

3. Inflation

The PIDR is set in real terms, i.e. at a level which is net of inflation. The reference rate of inflation in Northern Ireland and in Scotland is the RPI and in England and Wales it is CPI + 1 percentage point. From the period from 2019, the two measures have been broadly comparable. The purpose of the 1 percentage point uplift on CPI inflation in England and Wales is to capture real wage growth in the claimant's damages. The Department of Justice will need to make equivalent provision for real wage growth from 2030, either in a single PIDR or in a split PIDR (see 7 below).

Appendix 3 reproduces a Note prepared for APIL by Richard Cropper in respect of the impact of the methodological change in the RPI from 2030.

4. Taxation and costs of fund management

Taxation and the costs of fund management are combined in a 0.75 percentage point allowance with the understanding that provision for taxation is a small proportion of this. It is not clear to us that the evidence on which taxation provision is based is the right evidence. It appears to have been based on responses on taxation costs under the pre-2019 damages methodology based on notional investment in ILGS where the growth in maturity values from inflation is not taxed. Under the post-2019 methodology, investment is in corporate bonds and equities where higher income streams will attract higher tax rates and where growth in value is subject to capital gains tax. The tax position ought to be reviewed in this respect and any error corrected.

In addition, future demographic trends (at least 70 years ahead) are likely to raise rates and/or impact of taxation, including on taxation of assets. The proportion of working-age people is and will continue to contract while the proportion of retired people increases. The fiscal impact is to increase spending on public services, especially health and social care, and to decrease the tax base from which revenue for this additional spending is raised. Increased rates of taxation are the most likely response to these population pressures. This is evidenced by the freezing of allowances in recent years and the recent reviews into Capital Gains Tax.[1] Given that population ageing is certain, and its effects almost certain, provision for future increases in tax rates ought to be factored into the PIDR.

[1] https://www.gov.uk/government/publications/ots-capital-gains-tax-review-simplifying-practical-technical-and-administrative-issues#:~:text=The%20OTS%20recommends%20that%20the%20government%20consider%20whether%20Capital%20Gains,preserving%20eligibility%20to%20existing%20reliefs

Investment advice and management expenses were assumed to be the larger proportion of the combined allowance of 0.75 percentage points. This was at the lower end of the evidence submitted to the England and Wales consultation. It presumes that a claimant will buy tracker funds that replicate the asset allocation and rebalance the portfolio annually, back in line with the model (regardless of taxation implications), rather than take any advice. It is not reasonable to assume that an investor with no previous experience will have the ability to do this without advice.

In the light of the type and level of ongoing investment advice needed to manage a mixed portfolio, this is probably too low and ought to be raised.

5. Adjustment for the margin of prudence

At section 2 of its report (GAD 2019) the GAD sets out the justification and calculation of the PIDR adjustment of 0.5 percentage point as a margin of prudence. The purpose is to reduce the impact of investment risk that the claimant bears under the new 'risk-sharing'/'best estimate' PIDR methodology that the Civil Liability Act [2018] introduced. It shifts the curves in Figure 1 to the left, the graph in Figure 2 downwards and the box plots in Figure 3 to the left. This shift reflects the change in the probability of compensation adequacy from a ratio of 50:50 to a 67:33. As stated at paragraph 2.12 (GAD 2019), this acknowledges the additional investment risk that the claimant faces post-injury, but it does not acknowledge, or compensate for, other risks that the claimant now faces. These include life expectancy risk, inflation risk, taxation risk (that taxes increase over time), need risk (that the claimant's needs do not present as expected) and sequencing risk. The justification given is that in accepting a lump sum over a periodical payment, the claimant is accepting the life expectancy risk and feels compensated for bearing it by the benefits of early-receipt of funds. This ignores the pressure on some claimants to accept a lump sum in the litigation process and also the need for a degree of financial flexibility to manage risks elsewhere.

The combined effect of post-injury risks, even after accounting for the benefits of early receipt, very likely exceed the provision of a 0.5 percentage point margin of prudence so that the chances of achieving full compensation for 67% of claimants is exaggerated.

6. Economic Scenario Generator (ESG)

ESGs are used to predict future investment returns. This is an important component of the PIDR calculation. The chosen prediction has a very marked impact on the PIDR. It is less favourable investment forecasts that is largely responsible for the progressive reduction in the PIDR from England and Wales in July 2019, to Scotland in September 2019 and to Northern Ireland in March 2022. Given the potential impact of ESGs, it should form a key focus in any review.

Appendix 4 reproduces research undertaken by Richard Cropper in respect of the England and Wales portfolio that considers how the portfolio has performed since the GAD report was published in 2019. One can see that poor investment returns and high inflation means that a claim would be around minus 18% in real terms after less than four years. This has lasting implications on the future real rate of return required to avoid under-compensation. This illustrates the limitations of ESGs to predict future returns and the vulnerability of the claimant when the predications turn out to be wrong.

There are secondary issues of transparency and complexity in relation to the use of ESGs. There currently is no transparency in the economic modelling used in the determination of the PIDR in any of the jurisdictions. The models are protected by commercial sensitivity. As a result, there is no discussion or scrutiny over the predictions and they cannot be replicated. It is our view that this lack of transparency can and should be avoided.

It is possible to use much simpler models. It is not clear that model performance would be impacted by a simpler model. Experts will often try to improve the accuracy of their models by increasing the number of variables that are considered. There is evidence that adding more variables does not improve accuracy, "complexity may work in the odd case, but more often than not it reduces validity. Simple combinations of features are better." (Kahneman 2011,224). These simple models should be published.

7. Single or multiple discount rates

The proposal to introduce a dual rate system with two different PIDRs is considered here: (i) a system differentiating the PIDR according to different heads of damage which escalate over time at different rates of inflation and (ii) a system differentiating the PIDR by duration of claim with different short-term and long-term rates. This represents a methodological change and we make some preliminary comments in this respect before considering each type of split in more detail.

Changing the method of setting the PIDR is different from changing the PIDR itself. Changing the methodology creates more uncertainty and an expectation of further changes and uncertainty ahead. For this reason, we favour an underlying presumption towards stability in the methodology for setting the PIDR at the first review unless there is clear evidence of a net benefit to any proposed change. Consideration of a change in the methodology is appropriately undertaken using a cost benefit approach. The key benefit of a split PIDR is the potential gain in accuracy of match to the characteristics and circumstances of each claim. There are a number of costs to set against the potential gain in accuracy.

Methodological change creates uncertainty which is costly. The other key disadvantage is the increased complication of calculation and application and thus a loss of simplicity and efficiency. These are the hallmarks of the Ogden approach. It is simplicity which creates a degree of certainty within the valuation of claims and allows lawyers to value claims without recourse to expert financial advice. Added complexity falls as a burden on the parties and their advisers, the courts and those advising them on the PIDR (experts) and those providing guidance on its application (the Ogden Working Party). The main cost of either split is the added complication. The UK approach uses a simple formula (multiplier x multiplicand) which is applied by lawyers with the purpose of avoiding the cost of expert advice. The multiplier is determined by lawyers using standard tables which they have learned to apply. Costs of complexity would lead to greater delay in settling claims under a new PIDR determination where changes are more complicated and/or more frequent.

(i) split by heads of damages

A dual rate by heads of damages offers potential for greater accuracy through a closer match to the inflation rate associated with different heads of damages. This is a benefit to both claimants and defendants. A split by prices and earnings inflation is the most important inflation rate distinction. Having a separate PIDR for earnings-related heads, primarily the costs of care and case management, would avoid the uncertainty and inaccuracy introduced into the setting of a single rate by the need to cover different inflation rates and the decision of how much weight to give to prices-based expenditures and how much to earnings-based expenditures. These weights will be different for each claim depending on the proportion of total damages accounted for by care and case management. Few claims will split 50:50 on this basis. Moreover, under the current single rate, claimants can benefit from taking their earnings-based damages as a periodical payment and their prices-based damages as a lump sum. A split PIDR based on prices and earnings inflation would eliminate this benefit.

The costs are administrative. The greatest of these is grouping heads in the Schedule of Loss according to their inflation rates: prices or earnings and in large part these are already incurred. For clarity, and to save costs and argument, which heads of loss are assigned to which inflation group should be undertaken by the rate-setter. There is the added complication for the rate-setter and his/her advisors to determine an appropriate rate for long-term real earnings growth. A straight-forward approach to this would be to use the Office for Budget responsibility (OBR) long-term assumption for real wage growth which is published every two years in the Fiscal Risks and Sustainability Report (last report July 2022).

The fact that there are examples of dual rates by heads of damages where underlying inflation rates differ (Ireland, US, Guernsey and Bermuda) suggests that some jurisdictions have found that the benefits of greater accuracy outweigh the costs of greater complication. Ireland has operated a split PIDR according to care-related costs and non-care costs since 2014. Victoria Wass is familiar with PI in claims in the USA. The methodology for determining the PIDR, or sometimes the PIDR itself, is set at the state level. In states without a pre-determined state-wide PIDR, the PIDR is often determined uniquely in each claim and is determined on the basis of advice from forensic economists. This expert-led approach normally involves a separate PIDR for different heads of damages, according to separate inflation rates.

Overall, we consider a dual PIDR based on prices and earnings as warranting further investigation on the basis that it offers significant benefits in terms of accuracy of match to the target expenditures. On the face of it, this benefit appears to outweigh the rather modest increase in costs involved in its administration. The costs involved in a split rate by heads of damages are modest, manageable and one-off.

(ii) split by duration of claim

The overall benefits of greater accuracy offered by a dual rate by duration are uncertain to us. To the extent that the net effect is to raise the PIDR, it represents and further transfers the risk (and its associated costs) from the defendant to the claimant. On the cost side, a split rate by duration would demand more, and more complicated, tables.

The costs of a split rate by duration are higher and workability is uncertain. These are summarised below.

- Gaming system from anticipated frequent PIDR change;
- Need to account for higher tax rates for higher investment returns;
- Need to account for higher fees for more active fund management;
- More frequent reviews, PIDR-setting and revisions to tables;
- More recourse to experts;
- Need for an additional contingency fund to cover bad-timing of any collapse in market values in long-term funds; and
- An expectation of methodology changes at future reviews generates additional uncertainty.

As a whole these costs are significant and there is a need to be sure that there are clear benefits which will more than offset them.

We are not aware of different rates determined on the basis of duration of claim in the USA. For states adopting a risk-free investment assumption, where the PIDR is based on US government bond yields (TIPS), a split rate by duration is not needed. For those states that require the claimant to invest in risk-seeking assets, as in the UK, a split rate is possible, but we have not seen one used. In our view, the absence of duration-based rates in the USA is a significant indication against any proposition to introduce one in the UK. Given a dual rate based on duration in its close neighbour, Ontario, it will have been considered for application in those US states where it might apply. It appears to have been rejected.

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Appendix 1 Extract from Wass January 2019 Submission to England and Wales PIDR consultation Q 12(a)

It has been recognised by the courts that the claimant is not a hypothetical investor seeking the best returns. Rather the claimant's lump sum is more like a hypothetical closed/mature pension scheme meeting inflation-linked known liabilities from a finite fund. This analogy was first proposed by the House of Lords in Wells v Wells [1999]: "What the prudent plaintiff needs is an investment which will bring him the income he requires without the risks inherent in the equity market: which brings us back to ILGS" (Lord Lloyd para. 367). "Others like them with fixed outgoings at stated intervals take the same view as to prudent investment policy. So, the plaintiffs are not alone" (Lord Lloyd para. 368). "The general practice for a closed pension fund is to invest in ILGS so as to be sure of being able to meet their liabilities as they fall due" (Lord Lloyd para. 368). "Similarly, when the only liabilities of a pension fund are to pay index-linked pensions, the pension fund will invest entirely in index-linked government securities. Plainly insurers and pension fund managers, in so investing, are acting prudently (Lord Steyn). They are also required to act in accordance with the Pension Act (1995) and to comply with the investment guidance provided by tPR (2018).

I extend the analogy of the claimant's lump sum to that of a pension fund and suggest that in the context of the former the Lord Chancellor stands in the shoes of the professional Trustee of the pension fund. The Lord Chancellor (advised by GAD, HM Treasury and the expert panel) is charged with determining the portfolio mix which underlies the discount rate and this accords with the role of that of the professional Trustee. The professional Trustee is advised by the scheme Actuary. The GAD could provide a similar service to the Lord Chancellor. The requirement on both the Lord Chancellor and the Trustee is to invest assets backing the fund's liabilities "in a way that's appropriate to the nature, timing and duration of the expected future retirement benefits payable under your scheme." (The Pension Regulator (tPR) 2018 p. 52). While not a perfect analogy (the pension scheme has access to financial instruments, pooling possibilities, especially over life expectancy risks, and professional financial advice unavailable to the claimant for example), the role of the Trustee is sufficiently close to that of the role of the Lord Chancellor (advised by GAD) to be informative here. It is helpful that data are available both at the individual and collective level on pension scheme portfolios and on the Pension Protection Fund itself. The Purple Book published by the PPF reports the aggregate profile of pension scheme portfolios (see Figure 7.2 PPF 2018). There is a clear trend away from equity-based portfolios so that in 2018 they accounted for 27% of the fund. This is less than in each of the three portfolios proposed by the GAD. The PPF investment strategy is less risky than the portfolios proposed by the GAD even though it has the advantages of a 91% probability of meeting its funding target, can raise funds through a levy on DB pension funds and has access to range of complex financial instruments. The claimant's lump sum is very much more vulnerable to downside investment risks than is the average pension fund of the pension protection fund and therefore ought to have less exposure to investment risk, not more.

The investment portfolio of a pension scheme is regulated by primary legislation in the form of the Pension Act 1995 and by the Pension Regulator (tPR). I have selected three themes and an example from the Investment Guidance published by tPR (2018) which I consider pertinent

to the task before the Lord Chancellor and his advisor on actuarial matters, the GAD. The Pension Regulator advocates the use of robust risk management and risk-mitigation strategies. These will differ according to the circumstances of the scheme and the risks faced. The circumstances which most closely match the position of the claimant's lump sum is example 11 which is a mature underfunded scheme with a weak covenant. Such a fund is described as particularly vulnerable to investment under-performance and the guidance points strongly to a liability-driven investments (LDI) strategy in high-quality, low-yield corporate and government bonds as a means to manage and mitigate liability valuation risk. Liability valuation risk arises where values of assets and liabilities do not respond in the same way to changing market conditions.

1. matching assets (tPR 2018 p. 52)

The guidance notes advocate holding 'matching assets' in order to manage investment risk relative to the liabilities: "when setting your investment strategy you need to consider the scheme's asset, liability valuation and cash flow risks." (tPR 2018 p. 40) and focus on mitigating liability valuation risk. The primary route to do this is through an LDI strategy, changing the allocation towards assets that respond to changes in interest rates and inflation in the same way as liability values. This is normally a shift away from higher to lower risk investments which reduces the fund's vulnerability to investment under-performance. There is clear evidence that pension funds have been using this LDI strategy to de-risk their portfolios since 2006 (PPF 2018 Figure 7.2).

2. employer covenant (tPR 2018 p. 26)

Any flexibility to depart from the matched assets approach depends on the employer covenant. In a mature pension scheme this is the dominant aspect. The employer covenant is the obligation on and ability of the sponsoring employer to support downside investment risk in the fund now and in the future. A strong covenant allows the scheme to invest more heavily in risk-seeking assets. The claimant of course is without an employer sponsor to provide a covenant and is therefore in the very weakest position to invest in risk-seeking assets. In tPR terms, the lump sum cannot support any downside risk.

3. scenario and sensitivity analysis (tPR 2018 pp. 42-43).

Trustees are advised to model the impact of a shock to assets on the value of assets and liabilities both in the medium and long-term (scenario analysis). The models used to do this are sensitive to assumptions and there needs to be consideration of what happens to the outputs if the assumptions change (sensitivity analysis). It is the recommendation of tPR that these kinds of scenario and sensitivity analyses are a MINIMUM REQUIREMENT (tPR, p 46, author's emphasis). They ought to be part of the deliberations of the Lord Chancellor, GAD and eventually the expert panel. It does not appear that they are. If they are, they have not been published. As stated in my response to Q8, the GAD uses forecasts of real wage growth in the region of 0.5 to 0.7% pa over the next five and fifty years. Since the medium forecasts used by GAD are inconsistent with other forecasts, including official forecasts undertaken by the OBR and Bank of England, the requirement for sensitivity testing is acute. How would the GAD

advice change if official forecasts of real wage growth (1.2%, 2.0%) were assumed instead of forecasts at around a third of these rates? Of course, a 50 year inflation forecast has a large error margin and requiries scenario and sensitivity checks.

4. example 11 (tPR 2018 p.44)

Example 11 is a mature scheme with a weak covenant. It is underfunded and therefore sensitive to volatility in the equity market. The guidance is to favour 'matching over return seeking assets' (tPR 2018 p. 45). The Trustees are advised to hedge against the greatest risks facing the fund of low interest rates and high inflation through LDI. This essentially matches assets to liabilities with various degrees of leverage, the leverage depending on the strength of the employer covenant.

If the Lord Chancellor and his advisors in the GAD were to treat the portfolio as if it were regulated by the tPR, it is my view that it would be forced on the basis of 1 to 3 above to recommend a very low-risk low-return portfolio comprising largely of corporate and government bonds. The model portfolios proposed at para 45 of the Call for Evidence would not satisfy the regulator in terms of exposure to investment risk. The Lord Chancellor and/or the GAD needs to explain why these portfolio selections are so markedly different from those that would be selected by the professional actuaries which advise on pension schemes and from the actuarial guidance provided by tPR.

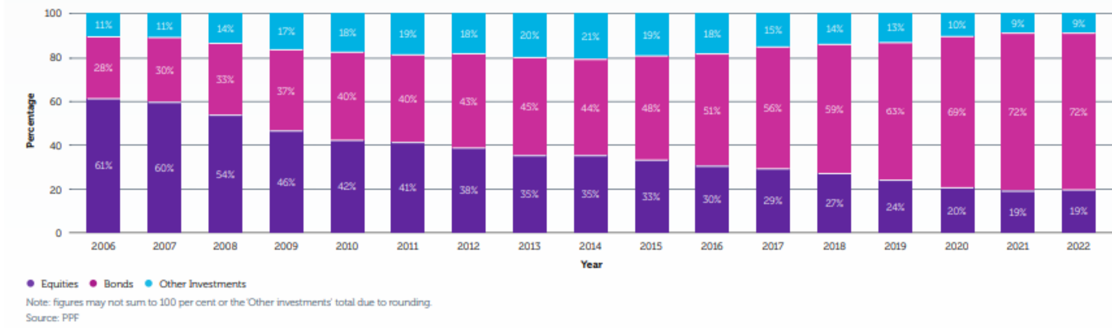
In view of the similarity between the role of the pension fund Trustee and the Lord Chancellor (advised by GAD) in determining an investment portfolio matched to the fund's liabilities, I propose that advice is also sought now from an independent actuary sensitivity an with experience as a pension fund Trustee and that this person goes on to join the expert panel when it is formed.

The Government's response to this consultation needs to explain why one arm of Government, in the form of the Lord Chancellor and the GAD, are proposing that a claimant who is in the very worst position to manage the risks associated with the equity market because his/her fund is underfunded (see (i) to (vi) of Q4) and without an alternative source of income (no sponsoring employer) be required to increase his/her exposure to equity risk when another arm of government, in the form of tPR, requires pension funds (substantially less vulnerable than the claimant's lump sum) to contain exposure to risk-bearing investments.

Appendix 2 Extract from Pension Protection Fund (2022) Purple Book Asset Allocation

Figure 7.2 | Weighted average asset allocation in total assets

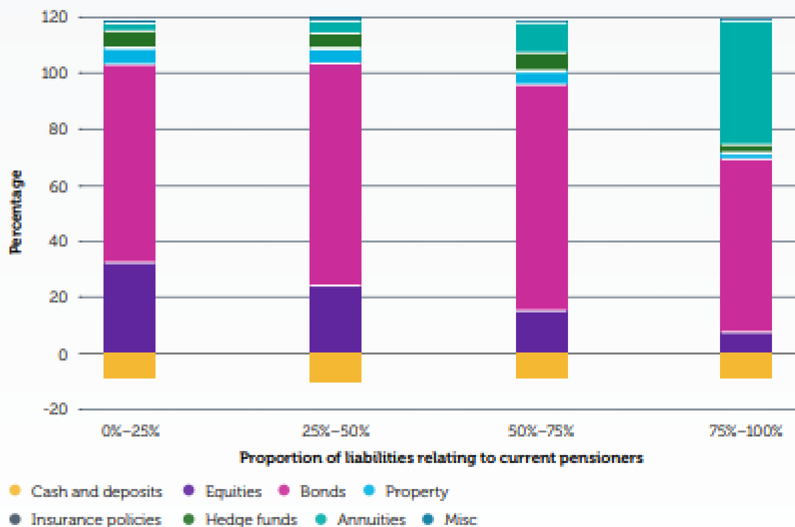
The proportions of assets invested in equities and bonds have been broadly stable since 31 March 2020.



Note: figures may not sum to 100 per cent or the 'Other investments' total due to rounding.
Source: PPF

Figure 7.9 | Weighted average asset allocation of schemes by scheme maturity

As scheme maturity increases, the proportion of equities falls.



Source: PPF

Note: the heavy concentration in 'Annuities' for mature schemes is explained by one large scheme with a heavy concentration in annuity policies.

Appendix 3 Note on PIDR for Scotland for APIL Richard Cropper January 2023

The PIDR in Scotland and the RPI

12th January 2023

The Government Actuary's report entitled "The Personal Injury Discount Rate, Review and determination of the rate in Scotland by the Government Actuary", dated 27th September 2019 states (at paragraphs 3.4 to 3.6):

> Future of RPI
>
> *As outlined in Table 2, the Act prescribes that I determine the real return on the notional portfolio, relative to RPI inflation. On 4 September 2019, the Chancellor responded4 to both the UK Statistics Authority's (UKSA) proposed reforms to RPI and the Lords Economic Affairs Committee report 'Measuring Inflation', which outlined the potential for future changes to the way in which RPI is measured.*
>
> *In his response to the UKSA, the Chancellor recognised that there are flaws in the way that RPI is measured. However, he did not give consent for UKSA to stop publishing RPI or to change its methodology to bring RPI in line with CPIH, as the UKSA had proposed. The Chancellor stated that the government will begin consultation in January 2020 to decide if changes, based on proposals by UKSA, should take place between 2025 and 2030. After 2030, the UKSA will no longer need the Chancellor's consent to make changes to RPI.*
>
> *Ahead of the consultation, it is not possible to know what changes might be made to RPI and when such changes might be introduced. Given the uncertainty, I have not made any allowance for the outcome of this consultation in my advice. Instead I would recommend that the appropriateness of the PI discount rate is reviewed when the consultation is concluded and there is more clarity on potential changes to RPI.*

The Government Actuary's report entitled "The Personal Injury Discount Rate, Review and determination of the rate in Northern Ireland by the Government Actuary", dated 15th March 2022 states (at paragraphs 3.4 to 3.10):

> *RPI Inflation 3.4 As outlined in Table 2, the Act prescribes that I determine the real return on the notional portfolio, relative to RPI inflation. For this purpose, it is relevant to note the policy changes that may affect the RPI from 2030 onwards.*

On 25 November 2020, the UK Statistics Authority (UKSA) and the UK Government issued a response to their joint consultation on aligning the methodology of RPI more closely with the methodology of 'the Consumer Prices Index including owner occupiers' housing costs' (CPIH). Their response confirmed the following:

- *The UKSA confirmed its policy to implement the change at the earliest possible time it could.*
- *The Government does not consent to the alignment of RPI with CPIH before 2030.*

It is my understanding that the UKSA's policy intent is to make the change to the formula used to calculate RPI in February 2030 (at which point it does not need the Government's permission).

I estimate that the likely effect of this change will be to reduce RPI inflation by about 0.9% pa on average from 2030, given the parameters for the change in methodology for RPI set out by the UKSA. This is solely driven by a change in the way in which RPI is to be calculated and does not reflect a change in the actual prices of the underlying goods in the index. In other words, a representative consumer of the basket of goods in the index will not see any change in their real cost of living, as a result of the change to the definition of the index.

The decision to change the way that RPI will be calculated from 2030 is the subject of an ongoing Judicial Review. The case, which is expected to be heard later this year, therefore casts some uncertainty over the proposed changes described above.

To allow for the fact that investment returns will be offset by increases in claimant damages costs, as set out in Table 2, the Act requires that I assess real returns relative to RPI inflation over a 43-year period. In view of the legal challenge to the proposed intention to change the methodology of RPI to be more in alignment with the methodology of CPIH from 2030, and which may affect the policy or the way it was accomplished, I consider there to be sufficient uncertainty of the change in definition of RPI from 2030 onwards, to continue to allow for RPI in its current form in my assessment.

Other things being equal, were I instead to take into account the proposed change in methodology of RPI from 2030 onwards to be more aligned with CPIH, this would increase the required rate set out in this report by around 0.5% pa.

It seems to me from the above that:

- The Government Actuary was aware of the potential change to the methodology of the RPI from 2030 when setting the discount rate in Scotland;
- No allowance was made due to the uncertainty surrounding the potential change;

- The Government Actuary recommended that once the consultation had concluded the PIDR in Scotland should be reviewed;
- The Government Actuary was aware of the proposed changes to the methodology of the RPI from 2030 when setting the discount rate in Northern Ireland, but was also aware of the Judicial Review; and
- The Government Actuary ignored the change when setting the PIDR in Northern Ireland due to the Judicial Review but acknowledged that the change would reduce the PIDR in Northern Ireland (i.e. over a duration of 43 years from 2030) by 0.5%.

The Judgment in the relevant Judicial Review in the matter of *The Queen (on the application of (1) BT Pensions Scheme Trustees Limited (2) Marks and Spencer Pension Trust Limited (3) Ford Pension Scheme for Senior Staff Trustees Limited (4) Ford Salaried Pension Fund Trustees Limited (5) Ford Pension Fund Trustees Limited v (1) UK Statistics Authority (2) Chancellor of the Exchequer* [2022] EWHC 2265 (Admin) and the Summary are enclosed.

The Court rejected all grounds.

The Government Actuary has not set out what the impact would be in Scotland and the 0.5% change in Northern Ireland can only be considered as indicative, as the duration the PIDR is modelled over in Scotland is 30 whereas in Northern Ireland the duration is 43 years.

The change in seven years means that the new methodology will apply for 83.72% of the modelled duration in Northern Ireland (that being 36 divided by 43), but only 76.67% in Scotland (23 as a proportion of 30).

However, taking account of this change can only lead to a reduction in the PIDR in both Scotland and Northern Ireland.

Now that both the consultation and the Judicial Review have concluded, I consider the "… *appropriateness of the PI discount rate is reviewed …"* in Scotland, as recommended by the Government Actuary in his report.

Richard Cropper
Consultant

Appendix 4 Discount Rate Portfolio Assumption Analysis Richard Cropper January 2023

Objective: To analyse the returns achieved by the low-risk portfolios as described in the 'Setting the Personal Injury Discount Rate Government Actuary's Advice to the Lord Chancellor' dated 25th June 2019, to understand the impact to real world investors.

The portfolios provided in the above guidance are defined as follows[1]

Allocation	Cautious	Central	Less-Cautious
Cash	12.50%	10.00%	7.50%
Gilts	35.00%	30.00%	22.50%
Corporate Bonds	22.50%	17.50%	15.00%
Equities	22.50%	32.50%	42.50%
Alternatives	7.50%	10.00%	12.50%

The element invested in Gilts and Equities appears to be further split into nominal gilts, index-linked gilts, UK Equities and Overseas Equities[2], however no specific breakdown between these sub-asset classes has been provided. The make-up of the Alternatives sector has also not been defined.

For each of the above portfolios I have considered the following to be appropriate:

1) Splitting the allocation to Gilts into Nominal and Index-linked Gilts:
   a) 2/3rds Nominal to 1/3rd Index-linked.
   b) An even split between both Nominal and Index-linked.
   c) 1/3rd Nominal to 2/3rds Index-linked.

[1] Setting the Personal Injury Discount Rate Government Actuary's Advice to the Lord Chancellor; page 43

[2] Setting the Personal Injury Discount Rate Government Actuary's Advice to the Lord Chancellor; page 73

2) Splitting the allocation to Equities into UK Equities and Overseas Equities (excluding UK):
   a) 2/3rds UK to 1/3rd Overseas (excluding UK).
   b) An even split between both UK and Overseas.
   c) 1/3rd UK to 2/3rds Overseas (excluding UK).

3) Splitting the Alternative Asset Class evenly between Property and Absolute Return strategies

To mirror the above allocation I have considered the use of the following funds:

Asset Class	Investment
Cash	iShares Core Cash ETF
Gilts (Nominal)	Vanguard UK Gilt ETF
Gilts (Index-Linked)	iShares Index Linked Gilt Index Fund
Equities (UK)	iShares UK Equity Index Fund
Equities (Overseas excluding UK)	Vanguard FTSE Developed World ex-UK Equity Index Fund
Alternatives (Property)	iShares Developed Real Estate Index Fund
Alternatives (Absolute Returns)	Goldman Sachs Absolute Return Tracker Portfolio

These funds were selected for the following reasons:

- They focus on replicating the returns of the sectors identified;
- The guidance assumes passive funds would be used[3]; and
- All funds are available to retail investors.

I acknowledge that there are limitations to the above selection, and additional funds may be needed to correctly replicate the portfolio used by the Government Actuary. This considered, the information provided in the guidance is very limited, and as such I believe that the above selection would be sufficient for the purposes of this analysis.

[3] Government Actuary's Advice to the Lord Chancellor on the Personal Injury Discount Rate; point 4.16

Cautious Portfolio – Asset Allocation

Cautious Portfolio 1	
Cash	12.50%
Gilts (Nominal)	23.33%
Gilts (Index-linked)	11.67%
Global Corporate Bonds	22.50%
UK Equity	15.00%
Overseas Equity	7.50%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 2	
Cash	12.50%
Gilts (Nominal)	17.50%
Gilts (Index-linked)	17.50%
Global Corporate Bonds	22.50%
UK Equity	15.00%
Overseas Equity	7.50%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 3	
Cash	12.50%
Gilts (Nominal)	11.67%
Gilts (Index-linked)	23.33%
Global Corporate Bonds	22.50%
UK Equity	15.00%
Overseas Equity	7.50%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 4	
Cash	12.50%
Gilts (Nominal)	23.33%
Gilts (Index-linked)	11.67%
Global Corporate Bonds	22.50%
UK Equity	11.25%
Overseas Equity	11.25%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 5	
Cash	12.50%
Gilts (Nominal)	17.50%
Gilts (Index-linked)	17.50%
Global Corporate Bonds	22.50%
UK Equity	11.25%
Overseas Equity	11.25%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 6	
Cash	12.50%
Gilts (Nominal)	11.67%
Gilts (Index-linked)	23.33%
Global Corporate Bonds	22.50%
UK Equity	11.25%
Overseas Equity	11.25%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 7	
Cash	12.50%
Gilts (Nominal)	23.33%
Gilts (Index-linked)	11.67%
Global Corporate Bonds	22.50%
UK Equity	7.50%
Overseas Equity	15.00%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 8	
Cash	12.50%
Gilts (Nominal)	17.50%
Gilts (Index-linked)	17.50%
Global Corporate Bonds	22.50%
UK Equity	7.50%
Overseas Equity	15.00%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio 9	
Cash	12.50%
Gilts (Nominal)	11.67%
Gilts (Index-linked)	23.33%
Global Corporate Bonds	22.50%
UK Equity	7.50%
Overseas Equity	15.00%
Alternatives (Property)	3.75%
Alternatives (Absolute Return)	3.75%

Cautious Portfolio – Performance

Cautious Portfolio 1			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	2.94%	1.56%	+1.38%
25/06/2020 to 24/06/2021	5.17%	3.14%	+2.03%
25/06/2021 to 24/06/2022	-8.92%	10.12%	-19.04%
25/06/2022 to 04/01/2023	-4.98%	5.41%	-10.39%
25/06/2019 to 04/01/2023	-5.73%	21.59%	-27.32%

Cautious Portfolio 2			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.05%	1.56%	+1.49%
25/06/2020 to 24/06/2021	5.03%	3.14%	+1.89%
25/06/2021 to 24/06/2022	-8.70%	10.12%	-18.82%
25/06/2022 to 04/01/2023	-4.73%	5.41%	-10.14%
25/06/2019 to 04/01/2023	-5.43%	21.59%	-27.02%

Cautious Portfolio 3			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.15%	1.56%	+1.59%
25/06/2020 to 24/06/2021	4.89%	3.14%	+1.75%
25/06/2021 to 24/06/2022	-8.48%	10.12%	-18.60%
25/06/2022 to 04/01/2023	-4.48%	5.41%	-9.89%
25/06/2019 to 04/01/2023	-5.13%	21.59%	-26.72%

Cautious Portfolio 4			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.63%	1.56%	+2.07%
25/06/2020 to 24/06/2021	5.23%	3.14%	+2.09%
25/06/2021 to 24/06/2022	-8.98%	10.12%	-19.10%
25/06/2022 to 04/01/2023	-5.16%	5.41%	-10.57%
25/06/2019 to 04/01/2023	-4.97%	21.59%	-26.56%

Cautious Portfolio 5			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.74%	1.56%	+2.18%
25/06/2020 to 24/06/2021	5.09%	3.14%	+1.95%
25/06/2021 to 24/06/2022	-8.76%	10.12%	-18.88%
25/06/2022 to 04/01/2023	-4.91%	5.41%	-10.32%
25/06/2019 to 04/01/2023	-4.67%	21.59%	-26.26%

Cautious Portfolio 6			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.85%	1.56%	+2.29%
25/06/2020 to 24/06/2021	4.95%	3.14%	+1.81%
25/06/2021 to 24/06/2022	-8.54%	10.12%	-18.66%
25/06/2022 to 04/01/2023	-4.66%	5.41%	-10.07%
25/06/2019 to 04/01/2023	-4.37%	21.59%	-25.96%

Cautious Portfolio 7			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	4.33%	1.56%	+2.77%
25/06/2020 to 24/06/2021	5.29%	3.14%	+2.15%
25/06/2021 to 24/06/2022	-9.05%	10.12%	-19.17%
25/06/2022 to 04/01/2023	-5.33%	5.41%	-10.74%
25/06/2019 to 04/01/2023	-4.21%	21.59%	-25.80%

Cautious Portfolio 8			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	4.43%	1.56%	+2.87%
25/06/2020 to 24/06/2021	5.15%	3.14%	+2.01%
25/06/2021 to 24/06/2022	-8.83%	10.12%	-18.95%
25/06/2022 to 04/01/2023	-5.08%	5.41%	-10.49%
25/06/2019 to 04/01/2023	-3.91%	21.59%	-25.50%

Cautious Portfolio 9			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	4.54%	1.56%	+2.98%
25/06/2020 to 24/06/2021	5.01%	3.14%	+1.87%
25/06/2021 to 24/06/2022	-8.61%	10.12%	-18.73%
25/06/2022 to 04/01/2023	-4.83%	5.41%	-10.24%
25/06/2019 to 04/01/2023	-3.61%	21.59%	-25.20%

Cautious Portfolio – Performance from 25th June 2019 to 4th January 2023

25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
-5.00%
-10.00%
-15.00%
-20.00%
-25.00%
-30.00%

1 2 3 4 5 6 7 8 9

Portfolio CPI +1 Real Return

Central Portfolio – Asset Allocation

Central Portfolio 1		Central Portfolio 2		Central Portfolio 3	
Cash	10.00%	Cash	10.00%	Cash	10.00%
Gilts (Nominal)	20.00%	Gilts (Nominal)	15.00%	Gilts (Nominal)	10.00%
Gilts (Index-linked)	10.00%	Gilts (Index-linked)	15.00%	Gilts (Index-linked)	20.00%
Global Corporate Bonds	17.50%	Global Corporate Bonds	17.50%	Global Corporate Bonds	17.50%
UK Equity	21.67%	UK Equity	21.67%	UK Equity	21.67%
Overseas Equity	10.83%	Overseas Equity	10.83%	Overseas Equity	10.83%
Alternatives (Property)	5.00%	Alternatives (Property)	5.00%	Alternatives (Property)	5.00%
Alternatives (Absolute Return)	5.00%	Alternatives (Absolute Return)	5.00%	Alternatives (Absolute Return)	5.00%
Central Portfolio 4		**Central Portfolio 5**		**Central Portfolio 6**	
Cash	10.00%	Cash	10.00%	Cash	10.00%
Gilts (Nominal)	20.00%	Gilts (Nominal)	15.00%	Gilts (Nominal)	10.00%
Gilts (Index-linked)	10.00%	Gilts (Index-linked)	15.00%	Gilts (Index-linked)	20.00%
Global Corporate Bonds	17.50%	Global Corporate Bonds	17.50%	Global Corporate Bonds	17.50%
UK Equity	16.25%	UK Equity	16.25%	UK Equity	16.25%
Overseas Equity	16.25%	Overseas Equity	16.25%	Overseas Equity	16.25%
Alternatives (Property)	5.00%	Alternatives (Property)	5.00%	Alternatives (Property)	5.00%
Alternatives (Absolute Return)	5.00%	Alternatives (Absolute Return)	5.00%	Alternatives (Absolute Return)	5.00%
Central Portfolio 7		**Central Portfolio 8**		**Central Portfolio 9**	
Cash	10.00%	Cash	10.00%	Cash	10.00%
Gilts (Nominal)	20.00%	Gilts (Nominal)	15.00%	Gilts (Nominal)	10.00%
Gilts (Index-linked)	10.00%	Gilts (Index-linked)	15.00%	Gilts (Index-linked)	20.00%
Global Corporate Bonds	17.50%	Global Corporate Bonds	17.50%	Global Corporate Bonds	17.50%
UK Equity	10.83%	UK Equity	10.83%	UK Equity	10.83%
Overseas Equity	21.67%	Overseas Equity	21.67%	Overseas Equity	21.67%
Alternatives (Property)	5.00%	Alternatives (Property)	5.00%	Alternatives (Property)	5.00%
Alternatives (Absolute Return)	5.00%	Alternatives (Absolute Return)	5.00%	Alternatives (Absolute Return)	5.00%

Central Portfolio – Performance

Central Portfolio 1

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	1.25%	1.56%	-0.31%
25/06/2020 to 24/06/2021	8.19%	3.14%	+5.05%
25/06/2021 to 24/06/2022	-7.62%	10.12%	-17.74%
25/06/2022 to 04/01/2023	-3.60%	5.41%	-9.01%
25/06/2019 to 04/01/2023	-1.91%	21.59%	-23.50%

Central Portfolio 2

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	1.35%	1.56%	-0.21%
25/06/2020 to 24/06/2021	8.07%	3.14%	+4.93%
25/06/2021 to 24/06/2022	-7.43%	10.12%	-17.55%
25/06/2022 to 04/01/2023	-3.39%	5.41%	-8.80%
25/06/2019 to 04/01/2023	-1.65%	21.59%	-23.24%

Central Portfolio 3

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	1.44%	1.56%	-0.12%
25/06/2020 to 24/06/2021	7.95%	3.14%	+4.81%
25/06/2021 to 24/06/2022	-7.25%	10.12%	-17.37%
25/06/2022 to 04/01/2023	-3.18%	5.41%	-8.59%
25/06/2019 to 04/01/2023	-1.39%	21.59%	-22.98%

Central Portfolio 4

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	2.25%	1.56%	+0.69%
25/06/2020 to 24/06/2021	8.28%	3.14%	+5.14%
25/06/2021 to 24/06/2022	-7.71%	10.12%	-17.83%
25/06/2022 to 04/01/2023	-3.86%	5.41%	-9.27%
25/06/2019 to 04/01/2023	-0.81%	21.59%	-22.40%

Central Portfolio 5

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	2.35%	1.56%	+0.79%
25/06/2020 to 24/06/2021	8.16%	3.14%	+5.02%
25/06/2021 to 24/06/2022	-7.53%	10.12%	-17.65%
25/06/2022 to 04/01/2023	-3.65%	5.41%	-9.06%
25/06/2019 to 04/01/2023	-0.55%	21.59%	-22.14%

Central Portfolio 6

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	2.44%	1.56%	+0.88%
25/06/2020 to 24/06/2021	8.04%	3.14%	+4.90%
25/06/2021 to 24/06/2022	-7.34%	10.12%	-17.46%
25/06/2022 to 04/01/2023	-3.43%	5.41%	-8.84%
25/06/2019 to 04/01/2023	-0.29%	21.59%	-21.88%

Central Portfolio 7

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.26%	1.56%	+1.70%
25/06/2020 to 24/06/2021	8.37%	3.14%	+5.23%
25/06/2021 to 24/06/2022	-7.81%	10.12%	-17.93%
25/06/2022 to 04/01/2023	-4.12%	5.41%	-9.53%
25/06/2019 to 04/01/2023	0.28%	21.59%	-21.31%

Central Portfolio 8

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.35%	1.56%	+1.79%
25/06/2020 to 24/06/2021	8.24%	3.14%	+5.10%
25/06/2021 to 24/06/2022	-7.62%	10.12%	-17.74%
25/06/2022 to 04/01/2023	-3.90%	5.41%	-9.31%
25/06/2019 to 04/01/2023	0.54%	21.59%	-21.05%

Central Portfolio 9

Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	3.44%	1.56%	+1.88%
25/06/2020 to 24/06/2021	8.12%	3.14%	+4.98%
25/06/2021 to 24/06/2022	-7.43%	10.12%	-17.55%
25/06/2022 to 04/01/2023	-3.69%	5.41%	-9.10%
25/06/2019 to 04/01/2023	0.80%	21.59%	-20.79%

Central Portfolio – Performance from 25th June 2019 to 4th January 2023

25.00%
20.00%
15.00%
10.00%
5.00%
0.00%
-5.00%
-10.00%
-15.00%
-20.00%
-25.00%
-30.00%

1 2 3 4 5 6 7 8 9

Portfolio CPI +1 Real Return

Less-Cautious Portfolio – Asset Allocation

Less-cautious Portfolio 1		Less-cautious Portfolio 2		Less-cautious Portfolio 3	
Cash	7.50%	Cash	7.50%	Cash	7.50%
Gilts (Nominal)	15.00%	Gilts (Nominal)	11.25%	Gilts (Nominal)	7.50%
Gilts (Index-linked)	7.50%	Gilts (Index-linked)	11.25%	Gilts (Index-linked)	15.00%
Global Corporate Bonds	15.00%	Global Corporate Bonds	15.00%	Global Corporate Bonds	15.00%
UK Equity	28.33%	UK Equity	28.33%	UK Equity	28.33%
Overseas Equity	14.17%	Overseas Equity	14.17%	Overseas Equity	14.17%
Alternatives (Property)	6.25%	Alternatives (Property)	6.25%	Alternatives (Property)	6.25%
Alternatives (Absolute Return)	6.25%	Alternatives (Absolute Return)	6.25%	Alternatives (Absolute Return)	6.25%
Less-cautious Portfolio 4		**Less-cautious Portfolio 5**		**Less-cautious Portfolio 6**	
Cash	7.50%	Cash	7.50%	Cash	7.50%
Gilts (Nominal)	15.00%	Gilts (Nominal)	11.25%	Gilts (Nominal)	7.50%
Gilts (Index-linked)	7.50%	Gilts (Index-linked)	11.25%	Gilts (Index-linked)	15.00%
Global Corporate Bonds	15.00%	Global Corporate Bonds	15.00%	Global Corporate Bonds	15.00%
UK Equity	21.25%	UK Equity	21.25%	UK Equity	21.25%
Overseas Equity	21.25%	Overseas Equity	21.25%	Overseas Equity	21.25%
Alternatives (Property)	6.25%	Alternatives (Property)	6.25%	Alternatives (Property)	6.25%
Alternatives (Absolute Return)	6.25%	Alternatives (Absolute Return)	6.25%	Alternatives (Absolute Return)	6.25%
Less-cautious Portfolio 7		**Less-cautious Portfolio 8**		**Less-cautious Portfolio 9**	
Cash	7.50%	Cash	7.50%	Cash	7.50%
Gilts (Nominal)	15.00%	Gilts (Nominal)	11.25%	Gilts (Nominal)	7.50%
Gilts (Index-linked)	7.50%	Gilts (Index-linked)	11.25%	Gilts (Index-linked)	15.00%
Global Corporate Bonds	15.00%	Global Corporate Bonds	15.00%	Global Corporate Bonds	15.00%
UK Equity	14.17%	UK Equity	14.17%	UK Equity	14.17%
Overseas Equity	28.33%	Overseas Equity	28.33%	Overseas Equity	28.33%
Alternatives (Property)	6.25%	Alternatives (Property)	6.25%	Alternatives (Property)	6.25%
Alternatives (Absolute Return)	6.25%	Alternatives (Absolute Return)	6.25%	Alternatives (Absolute Return)	6.25%

Less-Cautious Portfolio – Performance

Less-cautious Portfolio 1			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	-0.57%	1.56%	-2.13%
25/06/2020 to 24/06/2021	11.44%	3.14%	+8.30%
25/06/2021 to 24/06/2022	-6.22%	10.12%	-16.34%
25/06/2022 to 04/01/2023	-1.88%	5.41%	-7.29%
25/06/2019 to 04/01/2023	2.38%	21.59%	-19.21%

Less-cautious Portfolio 2			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	-0.50%	1.56%	-2.06%
25/06/2020 to 24/06/2021	11.35%	3.14%	+8.21%
25/06/2021 to 24/06/2022	-6.08%	10.12%	-16.20%
25/06/2022 to 04/01/2023	-1.72%	5.41%	-7.13%
25/06/2019 to 04/01/2023	2.57%	21.59%	-19.02%

Less-cautious Portfolio 3			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	-0.43%	1.56%	-1.99%
25/06/2020 to 24/06/2021	11.26%	3.14%	+8.12%
25/06/2021 to 24/06/2022	-5.94%	10.12%	-16.06%
25/06/2022 to 04/01/2023	-1.56%	5.41%	-6.97%
25/06/2019 to 04/01/2023	2.77%	21.59%	-18.82%

Less-cautious Portfolio 4			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	0.74%	1.56%	-0.82%
25/06/2020 to 24/06/2021	11.55%	3.14%	+8.41%
25/06/2021 to 24/06/2022	-6.34%	10.12%	-16.46%
25/06/2022 to 04/01/2023	-2.21%	5.41%	-7.62%
25/06/2019 to 04/01/2023	3.81%	21.59%	-17.78%

Less-cautious Portfolio 5			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	0.81%	1.56%	-0.75%
25/06/2020 to 24/06/2021	11.46%	3.14%	+8.32%
25/06/2021 to 24/06/2022	-6.20%	10.12%	-16.32%
25/06/2022 to 04/01/2023	-2.05%	5.41%	-7.46%
25/06/2019 to 04/01/2023	4.01%	21.59%	-17.58%

Less-cautious Portfolio 6			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	0.87%	1.56%	-0.69%
25/06/2020 to 24/06/2021	11.37%	3.14%	+8.23%
25/06/2021 to 24/06/2022	-6.06%	10.12%	-16.18%
25/06/2022 to 04/01/2023	-1.89%	5.41%	-7.30%
25/06/2019 to 04/01/2023	4.20%	21.59%	-17.39%

Less-cautious Portfolio 7			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	2.04%	1.56%	+0.48%
25/06/2020 to 24/06/2021	11.66%	3.14%	+8.52%
25/06/2021 to 24/06/2022	-6.46%	10.12%	-16.58%
25/06/2022 to 04/01/2023	-2.55%	5.41%	-7.96%
25/06/2019 to 04/01/2023	5.25%	21.59%	-16.34%

Less-cautious Portfolio 8			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	2.11%	1.56%	+0.55%
25/06/2020 to 24/06/2021	11.57%	3.14%	+8.43%
25/06/2021 to 24/06/2022	-6.32%	10.12%	-16.44%
25/06/2022 to 04/01/2023	-2.39%	5.41%	-7.80%
25/06/2019 to 04/01/2023	5.44%	21.59%	-16.15%

Less-cautious Portfolio 9			
Period	Portfolio	CPI+1	Real Rate of Return
25/06/2019 to 24/06/2020	2.18%	1.56%	0.62%
25/06/2020 to 24/06/2021	11.48%	3.14%	+8.34%
25/06/2021 to 24/06/2022	-6.18%	10.12%	-16.30%
25/06/2022 to 04/01/2023	-2.23%	5.41%	-7.64%
25/06/2019 to 04/01/2023	5.64%	21.59%	-15.95%

Less Cautious Portfolio – Performance from 25th June 2019 to 4th January 2023

Portfolio performance and IA sectors relative to CPI+1%

15%
10%
5%
0%
-5%
-10%
-15%
-20%
-25%

Jul '19 | Nov | Mar '20 | Jul | Nov | Mar '21 | Jul | Nov | Mar '22 | Jul | Nov

A B C D E F

- A - UK Consumer Price Index + 1% TR in GB [0.00%]
- B - Discount Rate Research - Less-Cautious 5 GTR in GB [-13.76%]
- C - IA Mixed Investment 20-60% Shares GTR in GB [-13.76%]
- D - Discount Rate Research - Central 5 GTR in GB [-17.57%]
- E - IA Mixed Investment 0-35% Shares GTR in GB [-19.32%]
- F - Discount Rate Research - Cautious 5 GTR in GB [-21.02%]

25/06/2019 - 04/01/2023 Data from FE fundinfo2023

Additional Comments:

- All of the portfolios modelled outperformed the benchmark of CPI+1 in the period between June 2020 and June 2021.
- In all other periods the funds have failed to meet the intended need, often by a significant amount.
- The higher risk portfolios have fared better, as have the portfolios with more of a lean towards Overseas (as opposed to UK) Equities.
- No variant of the 'Cautious' portfolio I have modelled has provided positive returns since June 2019 before or after inflation is considered. Assuming CPI+1% the real impact to such an investor is shown to be loss of over a quarter of the amount invested over the period.
- The above also does not consider the assumption that the funds would be rebalanced regularly or that the Claimant would be drawing on the portfolio. If these factors are considered the forecast would likely be worse as the investor would need to withdraw/switch when markets have fallen.
- The portfolios with more growth assets ('Less-Cautious portfolios') have provided positive returns before inflation since June 2019, but real returns are negative in all cases.

Zurich UK's Response to the Request for Views on the PIDR in Northern Ireland

June 2023

Zurich UK provides a suite of general insurance and life insurance products to retail and corporate customers. We supply personal, commercial, and local authority insurance through a number of distribution channels, and offer a range of protection, retirement, and savings policies available online and through financial intermediaries for the retail market and via employee benefit consultants for the corporate market. We therefore welcome the opportunity to respond to the Request.

Zurich would like to begin its specific response by stating that it replied in detail to the Call for Evidence relating to the PIDR in England and Wales earlier in 2023 and that respecting the different jurisdiction of Northern Ireland entirely, we believe that a great many of the same considerations apply between the jurisdictions of the UK and as such, Zurich would like to draw your attention to the response that Zurich submitted in response to the Call for Evidence in England & Wales, which is attached for your consideration.

We can confirm that Zurich's approach to the concurrent Request from the Scottish Government is along the same lines as contained within this document, recognising that there are some differences within the Damages Act 1996 in relation to the various jurisdictions of the UK.

Specifically addressing the bullet-points made in the communication of 31st May, we respond as follows, with each bullet-point shown below corresponding to the factors in their order of appearance in the relevant communication.

- One of the largest challenges we have in considering PIDR issues is a lack of information from the plaintiff / pursuer / claimant ("PPC") community as to precisely what comprises their actual investment portfolios nor crucially what returns are achieved. We hear anecdotally of returns considerably in excess of those assumed using the current (and previous) PIDR, but what is required is detailed disclosure of the actual investment behaviour of those entrusted with investments on behalf of PPC.

In relation to the notional investment portfolio itself, our view is that gilts are unlikely to comprise such a large overall percentage of an investment portfolio of the properly-advised hypothetical investor. Equally, our view is that property is likely to account for a larger share of the portfolio than the table assumes, what with consistently high and stable returns on property investments over a long period.

Also, in the Government Actuary's Department 2019 report to the Lord Chancellor on the PIDR in England & Wales, it was suggested that equities would comprise 32.5% of the portfolio of a moderately cautious low risk portfolio. Equities have been identified by certain sources as producing consistently better returns than assumed by GAD in the referenced report.

A view we wish to stress is that investment behaviour across the UK should be assumed to be similar, with PPC accessing investment opportunities across the entire UK and not just within the UK jurisdiction where the claim was brought and settled. Our view is that a properly-advised hypothetical investor would access the broader UK investment market (noting that a degree of overseas investment is also assumed within the table) and so economic factors local to the relevant factors in setting the PIDR should not be unduly taken into account. In short, Zurich favours the same PIDR applying to the UK as a whole.

- The assumed period of investment of 43 years is broadly consistent with Zurich's portfolio of personal injury claims to which the PIDR is applicable and is therefore supported. It is considered a reasonable reflection of the relevant population and its life expectancy.

- In terms of inflation, we consider it crucial that inflation over the long-term be taken into account when calculating the PIDR. Short-term inflation can be very volatile. The Discount Rate should be set based on real investment returns, net of inflation. Taking account of the elements for which damages subject to the PIDR are intended to compensate, we wish to suggest that RPI is no longer a suitable index. RPI has processing flaws which overstate inflation (recognised by the Office for National Statistics) and is no longer considered a national statistic due to its failure to meet international standards. Further, CPI replaced RPI from 2011 as preferred measure of inflation for benefit and tax uprating purposes by the UK Government.

  Our view is that the CPI is a more reliable measure of inflation and should be adopted for the purpose of assessing the PIDR. It is noted that the UK is experiencing an unusually high level of inflation in recent times, due to a range of factors, which we respectfully suggest should not be unduly accounted for when looking at the long

term, noting that the Bank of England aims to return inflation to 2% annually, which it is expected to do in the next few years.

- Zurich takes the view that a further margin (currently 0.5%) is unnecessary and inappropriate, noting that we already consider that the PIDR overly allows for taxation, the costs of investment advice and management. The further margin is to unwarrantedly layer prudence on top of an already conservative approach, such that resultant damages settlements amount to more than full compensation. It is our understanding that the current discount rate of -1.5% in Northern Ireland is the lowest in the world, which contributes toward significant additional cost to liability insurance customers and the NHS.

Turning to the question of whether single or multiple rates should apply, this issue was covered at length in the response to the Call for Evidence in England & Wales, but for completeness here, we emphasize that both approaches are capable of achieving the aim of 100% compensation for a PPC, but it is entirely dependent on the PIDR and specific multiple rate methodology chosen.

We wish to point out that in relation to multiple rates, Zurich only supports the switched-dual rate system such as is in operation in Ontario. Zurich's position overall is that the current single-rate system ought to be maintained, due to our confidence that it can achieve the aim of 100% compensation for PPC as far as is possible, but we wish to see a PIDR set that is reflective of actual investment returns secured for PPC.

Overall, we do not believe that there is a compelling case for change in the current single rate approach.