

## Accountancy Update

February 2010

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#### Case notes

##### Requirement to tailor applications to restrict material available to non-parties

In the August edition of Accountancy Update we reported the decision of the court to restrict access to a statement of case in an action involving the National Policing Improvements Agency (NPIA), so that the statement of case could refer to matters which were confidential to NPIA. A more recent case is a useful illustration of the court’s determination to preserve, so far as possible, the principle of open justice. [More...](#)

##### A useful reminder of the effect which a lawyer’s annotations on a document may have on its privileged status

This decision reconfirms the extent (and limitations) of legal professional privilege (and presumably also litigation privilege, although this is not expressly referred to in the decision). It can only apply to instructions to and correspondence with counsel and experts, notes arising from meetings or discussions with counsel and experts and underlying documents where the advice trend is clear. [More...](#)

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The case of *Edwards v Bruce & Hyslop (Brucast) Limited* acts as a reminder of the rules regarding communications between parties and a single joint expert. [More...](#)

#### Round-up

Our Round-up section includes reports on corporate governance guidance for both auditing firms and corporates, a recent regulation requiring the disclosure of insurance details and the OFT’s investigation into corporate insolvency. [More...](#)



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#### Firm news

We will be hosting our next breakfast briefing on Wednesday 12 May. [More...](#)

#### Any comments or queries?

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## Litigation costs – from hot tubs to funding regulation – it’s time for action

The dust has settled after the publication of Lord Justice Jackson’s final report in his year-long Civil Litigation Costs Review. We focus here on six key issues considered by Jackson LJ which are of most relevance to accountants.



### Part 36

Jackson LJ made two significant recommendations for reform of Part 36:

- That the Court of Appeal decision in *Carver v BAA*<sup>1</sup> (on the interpretation of “advantageous” in CPR 36.14(1)) be reversed
- That where a defendant fails to beat a claimant’s Part 36 offer, the claimant’s recovery be enhanced by 10%

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By way of reminder, the *Carver* decision considered the effect of the new Part 36 rules introduced in April 2007. Those rules provide that costs consequences follow when “a claimant fails to obtain a judgment more advantageous than a defendant’s Part 36 offer”. In *Carver* the Court of Appeal decided that money was not the only factor the court should take into account when deciding whether a judgment is “more advantageous”. Litigation is time-consuming and emotionally and financially costly. The court in *Carver* said that all these (not necessarily quantifiable) factors have to be taken into account. The decision has attracted much criticism for introducing uncertainty into the Part 36 process. Jackson LJ said that it put “unreasonable pressure on claimants to accept offers which are not quite high enough”.

Defendants, of course, may have found the *Carver* decision helpful for precisely that reason. Jackson LJ recommends that *Carver* is reversed either judicially (if the opportunity arises) or by rule change. The latter could happen relatively quickly – we understand that changes to be implemented by means of a rule change are likely to be introduced in the October 2010 rules update. In the meantime, this leaves defendants in an even more uncertain position as to the basis upon which the court will assess any Part 36 offers which are currently “live”, and any Part 36 offers which may be made post-Jackson, but before *Carver* is reversed. Defendants must assume that by the time their Part 36 offer comes to be assessed, the court may be required to consider whether or not the claimant has beaten the offer on a purely monetary basis.

Defendants also need to factor in Jackson LJ’s second proposal: that a claimant who makes a Part 36 offer which is unbeaten should be given a 10% uplift on damages recovered. The aim of this rule change is to provide a greater incentive for claimants to make reasonable offers, and for defendants to accept them. It is also seen as a way of compensating claimants in successful CFA funded cases who would now (under Jackson LJ’s other proposals) no longer recover CFA success fees from defendants.

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#### Footnotes

1 [2008] EWCA Civ. 412

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Jackson LJ indicates that legislation will be required to implement this change. He also suggests that there should be further consultation, if this proposal is accepted in principle, on the question of whether it would be appropriate to scale down the uplift for higher value cases (say those above £500k). Defendants will see this proposal as harsh, particularly those involved in high-value commercial litigation where even a scaled down uplift could be significant.

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## Experts

Firms which provide forensic accounting services will be interested in the proposed reforms affecting experts. The report identifies expert evidence as one of several parts of the litigation process which sometimes increase costs unnecessarily. Jackson LJ made a number of proposals to contain the costs of expert evidence:

- Increased and better use of the court's existing case management powers. In heavier cases, it may even be appropriate to hold a separate case management conference (CMC) for determining the scope of expert evidence
- Judges should make greater use of their existing powers<sup>2</sup> to restrict recoverable costs in relation to expert evidence
- CPR Part 35 should be amended to require a party seeking permission to adduce expert evidence to provide an estimate of the costs of that evidence to the court
- Greater use of costs sanctions, where the expert evidence is unnecessarily prolix or irrelevant, leading to wasted costs.

More radical is Jackson LJ's suggested pilot of the Australian practice of "hot tubbing" (or concurrent evidence). The Preliminary Report explains how the practice operates: experts in the same discipline are sworn in at the same time and the judge chairs a discussion between them. Counsel join in the discussion and are able to put questions to the experts, as and when the judge permits. The experts can also put questions to each other. Feedback from the Australian legal profession is that the procedure is effective and saves both time and costs. Jackson LJ recommends that this practice be piloted, but only in cases where the parties, the experts, the lawyers and the judge all consent to the procedure. Professional experts need to be prepared now to embrace this option in appropriate cases.

## Third Party Funding

Following the recent third party funding arrangement in the *Stone & Rolls* litigation<sup>3</sup>, Jackson LJ's proposals for third party funding are of particular interest.

In his Preliminary Report, Jackson LJ touted the possibility of a statutory code to govern third party funders. However, in the intervening period between his Preliminary and Final Report, the Civil Justice Council (with the assistance of the Third Party Litigation Funders Association) published a draft voluntary code ("the draft code") for third party funders.

It is anticipated that the draft code will become final in March 2010, and it is likely to adopt Jackson LJ's suggested amendments which include:

- **Withdrawal of the funder:** the draft code currently provides that a funder can terminate a funding agreement by giving 21 days

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### Footnotes

<sup>2</sup> CPR Rule 35.4(4)

<sup>3</sup> *Stone & Rolls Ltd (in liquidation) v Moore Stephens (a firm)* [2009] UKHL 39

notice, subject to paying all accrued liabilities, where it is no longer satisfied of the merits of the claim and/or proceedings are no longer viable.

Jackson LJ considers the provision unsatisfactory and recommends that a funder should be obliged to continue funding whatever it originally contracted to provide unless "*there are proper grounds to withdraw*", but he does not explain what he considers to be proper grounds for withdrawal. We will have to await the publication of the final version of the code for clarification.

- **Capital adequacy:** with the economic climate seemingly at the forefront of his mind, Jackson LJ recommends revising the capital adequacy sections of the draft code, which currently provide that a funder should have "*adequate resources of cash or cash equivalent to meet its liabilities for at least the next three months*". Jackson LJ comments that this does not adequately protect a potential client, given that litigation can go on for years.

Intriguingly, Jackson LJ also suggests that third party funders, in particular their capital adequacy requirements, could be regulated by the FSA. He did not consider that this was required in the short term but should be revisited in the future. Advising third party funders on capital adequacy requirements may well be required in the future.

Jackson LJ also makes two further recommendations of interest to third party funding arrangements:

- **Reversal of the rule in *Arkin v Borchard Lines Ltd*<sup>4</sup>.** The rule in *Arkin* provides that a third party funder is only responsible for an adverse cost order to the extent of the funding provided. Jackson LJ recommends that the extent of a third party funder's liability should instead be left to a judge's discretion.
- **Maintain the rule on maintenance and champerty.** However, provided that a third party funder complies with the system of regulation (likely to be the finalised draft code mentioned above) their funding arrangement should not be overturned on these grounds.

## Contingency Fee Agreements

Currently solicitors are prohibited from entering contingency fee arrangements for contentious business. Jackson LJ recommends that this rule be abolished.

However, a number of safeguards to be introduced in secondary legislation are recommended to protect litigants considering a contingency fee agreement, including: (i) a requirement that a client obtain independent legal advice; (ii) that clear and transparent advice on costs and other expenses is given to clients; (iii) setting a maximum percentage from which costs would be recoverable from damages, anything above the prescribed amount would be met by the successful litigant; and (iv) a requirement to agree at the outset who of the solicitor or client will bear any adverse costs orders.

It is likely that, at least initially, contingency fee agreements will be seen in group litigation. A potentially ripe area would be the various tax group litigation orders such as the VAT Interest Cars Group Litigation and the Thin Cap Group Litigation.

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### Footnotes

4 [2005] EWCA Civ 655

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## Fixed costs

Jackson LJ recommends fixed costs for fast track cases of £12k to trial (£13.5k in London). Outside of the fast track, Jackson LJ recommends the introduction of “benchmark” costs in insolvency proceedings. A system of “benchmark” costs is already in operation for HMRC’s costs in “routine” insolvency proceedings, which Jackson LJ recommends expanding.

In more complex insolvency proceedings, Jackson LJ noted that concerns had been raised about the level of remuneration charged by office-holders for their work in connection with insolvency litigation. Jackson LJ recommends the development of cost management procedures to control such costs, including the use of cost budgets in complex insolvency proceedings, whereby a party will need to explain as the proceedings progress why an estimate has been exceeded.

## Cost Management

Generally, Jackson LJ recommends that the judiciary should make better use of their existing case management powers to control costs. He also recommends some specific changes to assist cost management:

- The introduction of a definition of “proportionality” within the CPR – the CPR require that costs are proportionate, but do not define what this means. Jackson LJ suggests that the definition of proportionality should relate to *“sums in issue, the value of non-monetary relief, complexity of the litigation, conduct and any wider factors such as reputation or public importance”*. Further, when assessing costs on a standard basis the court should first determine whether the costs are reasonable and then, on a global basis, decide whether costs are proportionate, with an immediate reduction if costs are deemed *disproportionate*.
- Reverse the effect of existing case law<sup>5</sup> which links proportionality to necessity. Removing the link between necessary costs and proportionate costs, will make management of low value, complex cases difficult. Costs can easily escalate in establishing necessary facts, which, if Jackson LJ’s recommendation is implemented, may no longer be considered proportionate and will therefore be irrecoverable.

Jackson LJ’s Final Report is lengthy and comprehensive. Its potential to have a lasting and wholesale impact on the litigation costs landscape cannot be underestimated. Although some of the recommendations require primary legislation (which may be lost in an election year), many recommendations are achievable through rule changes which we may see as soon as October 2010. It appears that the judiciary in particular see Jackson LJ’s recommendations as a “done deal”. As Lord Neuberger, Master of the Rolls, said at the press conference to launch the Final Report *“I suggest that the time for discussion and for debate is over. It is now time for action”*. Mere words? We shall see.....

If you would like to see our more general summary of Jackson LJ’s recommendations “Nothing is Sacred” – click here: <http://www.rpc.co.uk/FileServer.aspx?oID=805&IID=0>

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### Footnotes

- 5 *Lownds v Home Office* [2002] EWCA Civ 365

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## Case notes

### Requirement to tailor applications to restrict material available to non-parties

In the August edition of Accountancy Update we reported the decision of the court to restrict access to a statement of case in an action involving the National Policing Improvements Agency (NPIA), so that the statement of case could refer to matters which were confidential to NPIA. A more recent case is a useful illustration of the court's determination to preserve, so far as possible, the principle of open justice.

The recent case of *G&G v Wikimedia Foundation Inc*<sup>1</sup> demonstrates the court taking a different approach and confirms that parties must be specific in their applications to restrict access to material by non-parties which would otherwise be available pursuant to CPR 5.4C.

In *G&G*, Mr Justice Tugendhat was asked to restrict access to the Statements of Case. However, he ordered that the Statements of Case in question should be edited (to remove the reference to the applicants' names) and held that this was a sufficient measure to protect them, based on the facts as they were presented to him. He reminded the parties that applicants who were relying on CPR 5.4(4) should limit their requests for restriction to documents to "*no more than is necessary and proportionate in the circumstances of the particular case*".

### A useful reminder of the effect which a lawyer's annotations on a document may have on its privileged status

This decision reconfirms the extent (and limitations) of legal professional privilege (and presumably also litigation privilege, although this is not expressly referred to in the decision). It can only apply to instructions to and correspondence with counsel and experts, notes arising from meetings or discussions with counsel and experts and underlying documents where the advice trend is clear.

In *Vivian Imerman v (1)Robert Tchenguiz and others*<sup>2</sup>, the claimant applied for an order to ensure compliance by the defendants with an order for delivery up of documents in their possession.

The claimant had obtained summary judgment against the defendants prohibiting them from using and copying confidential material in their possession. The parties then agreed that the defendants would deliver up all hard copy documents containing such material. The defendants failed to deliver up any documents. One reason given was that some of the documents were protected by legal professional privilege because they formed part of the papers accompanying counsel's instructions (which had now been returned to the defendants' solicitors by counsel) and had been annotated by counsel.

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#### Footnotes

- 1 [2009] EWHC 3148 (QB)
- 2 [2009] EWHC 2902 (QB)

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The court held that the doctrine of legal professional privilege did not extend to hard copy papers returned by counsel merely on the ground that they had formed part of counsel's instructions. Further, the underlining or highlighting of documents did not, of itself, give rise to legal professional privilege and the appropriate test was whether or not the annotations would give another party an idea of the trend of the advice – in this case, no such trend was ascertainable from counsel's markings. The court also considered (and dismissed) an argument that the absence of an annotation from some pages might reveal that these papers were considered not relevant by counsel and, therefore, reveal a trend in the advice.

### “Secret communications” taint a single joint expert’s report

The case of *Edwards v Bruce & Hyslop (Brucast) Limited*<sup>3</sup> acts as a reminder of the rules regarding communications between parties and a single joint expert.

The court’s consideration of these rules arose out of a dispute between an architect, Mr Edwards, and his client, Bruce & Hyslop (B&H). The parties had appointed a single joint expert (an architect) to consider whether or not Mr Edwards’ work (which involved manufacturing, supplying and installing three wrought iron balconies) was of a sufficiently good standard. The expert opined that the work was of a sufficient standard.

Notwithstanding this decision, there remained a dispute between the parties regarding payment for the work and Mr Edwards issued proceedings. Given the relatively low quantum involved, the court ordered that a single joint expert should be appointed and it was agreed that the same expert that was used in the pre-action stage should be retained again.

The expert’s second report was unfavourable to the architect, Mr Edwards. Mr Edwards’ solicitors then learnt that B&H had been engaging in “secret” communications with the expert. They applied to the court for permission to obtain their own expert evidence on the basis that the single joint expert’s evidence was tainted.

The application was granted and then subsequently appealed. B&H argued on appeal that the judge had given insufficient weight to the usual course of events (which, in modest value cases, was to appoint a single joint expert) and that the judge had not found that the expert’s integrity had been impaired by “inappropriate” access.

Mr Justice Coulson dismissed the appeal. He concluded that whilst it was the usual course of events to appoint a single joint expert in modest value cases, given the “secret” communications it was appropriate for Mr Edwards to appoint his own expert on this occasion. He also confirmed a previous ruling<sup>4</sup> that where a single joint expert had been appointed it is not permissible for one party to have a conference with the expert, in the absence of the other party, without the latter’s prior written consent.

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#### Footnotes

3 [2009] EWHC 2970

4 *Peet v Mid Kent Area Healthcare NHS Trust* (2002) 1 WLR 210

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## Round-up

### ICAEW release a Governance Code for audit firms

The ICAEW have released an 18 page document that codifies audit governance standards. Although adherence to the Code will be voluntary, compliance with the Code will be encouraged and a “comply or explain” system will be utilised by the ICAEW. The Code is designed for the UK’s eight largest audit firms and will place pressure on those firms to adopt many of the same corporate practices as their clients. The audit firms have welcomed the Code and are committed to implementing it. Sir Christopher Hogg, chairman of the FRC, “*strongly encourage[d] audit firms and investors to grasp the opportunities the Code presents to strengthen their dialogue*”.

The Code grew out of the fear of a Big Four collapse, which would leave as many as 20% of the 7,200 largest businesses in the G20 without an auditor. Some of the Code is already standard practice in many firms; for example, the use of non-executive directors, internal controls and whistle blowing policies, whilst other measures may require some change to practices.

### FRC proposes reforms to the UK Corporate Governance Code

The FRC has launched a consultation on its proposals to reform the UK’s Corporate Governance Code. The proposals take into account the lessons of the recent financial crisis that are relevant to all companies. The main proposals are:

- Annual re-election of the chairman or the whole board in order to enhance accountability to shareholders
- New principles on the leadership of the chairman, the roles, skills and independence of the non-executive directors and their level of time commitment to ensure the board is well balanced and challenging
- External facilitation of board evaluation reviews every three years and the chairman should hold regular development reviews with each director to enhance awareness of the board’s performance and strengths and weaknesses
- New principles on the board’s responsibility for and handling of risk to improve risk management
- Performance-related pay should be aligned to the long-term interests of the company and its policy on risk

Consultation on the draft ends on 5 March 2010. Readers can comment on the proposed changes by sending an email to: [codereview@frc.org.uk](mailto:codereview@frc.org.uk). Subject to the outcome of the consultation, the FRC intends for the Code to apply to all listed companies with a Premium Listing for financial years beginning on or after 29 June 2010.



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## HM Treasury publishes Walker Review final recommendations

HM Treasury has published its final report and recommendations of Sir David Walker's review of corporate governance in UK banks and other financial industries entities. Amongst the recommendations are:

- Strengthen the role of non-executive directors and give them new responsibilities to monitor risk and remuneration
- Require non-executive directors of FTSE 100 listed banks or life assurance companies to invest a greater time commitment – a minimum of 30 to 36 days
- Strengthen the FSA's interview process for non-executive directors proposed for FTSE 100 listed banks or life assurance companies so that it involves questioning and assessment by one or more senior advisers with relevant industry experience
- Introduce a new Stewardship Code to require institutional investors and fund managers to play a more active role as owners of businesses
- Make the FSA responsible for monitoring compliance with the Stewardship Code
- Extend the role of the remuneration committee to cover firm-wide remuneration policy and give the committee oversight of all "high-end" employees
- Require the disclosure of the number of "high-end" employees for FTSE 100 listed banks and comparable unlisted entities
- Similar disclosure requirements for FSA-authorized banks that are UK subsidiaries of foreign entities.

Alistair Darling has commented that *"Sir David's proposals are the blueprint for how banks must be run in the future. His interim report recommended changes to control bonuses that have already become part of a global standard agreed by the G20. The Government strongly supports his recommendations and will take steps to implement them as soon as possible"*.

## The Provision of Services Regulations 2009

On 28 December 2009, the Provision of Services Regulations 2009 came into force. These regulations require the providers of professional services to make certain information available to their customers. This includes, for service providers subject to a requirement to hold professional liability insurance, an obligation to make available details of that insurance – in particular the identity of the firm's insurer and the territorial extent of the insurance cover. This information can be made available in a number of ways, including in information documents supplied to the customer or by notifying the customer of where the information can be found on a publicly available website.

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## OFT's investigation into insolvency practices

Following concerns expressed by the Government and the Insolvency Service, the Office of Fair Trading has launched an investigation into the world of corporate insolvency. A recent World Bank report revealed that the costs of closing a business in the UK are higher than other countries with similar or better recovery rates. The study will look at the structure of the market, the appointment process for insolvency practitioners and any features in the market which could result in harm, such as higher fees or lower recovery rates for certain groups of creditors.

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## Firm News

We will be hosting our next breakfast briefing on Wednesday 12 May. Jane Howard and other members of our Professional Risks team will be looking at fraud and whose duty it is to detect it. For more information please email us at [seminars@rpc.co.uk](mailto:seminars@rpc.co.uk).

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