A German lesson

Andrew Hogan examines how fixed costs work in Germany

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At the time of writing, the referendum on whether or not this country should remain in the EU is some six weeks away. Every day, the respective camps for leaving or remaining tempt the uncommitted voter with the prospect of millions of Albanians, Serbs and Turks moving to the UK should we remain, or the delights of being part of a free-trade area with Montenegro and the Ukraine, as the de facto 51st state in president Trump's America. It is going to be a tough one to call.

This year in January, Jackson LJ set forth a vision for a scheme of fixed costs to apply to all money claims worth up to £250,000, with a prediction that such a scheme, could, if the political will were present, be implemented before the end of 2016. But because this is a referendum year, that seems most unlikely.

The intended consultations on fixed costs for the limited classes of noise-induced hearing loss claims and clinical negligence have not taken place, as the Ministry of Justice goes into lockdown and concentrates on the referendum, in peculiar circumstances where the lord chancellor is on the other side of the political divide to the prime minister.

In such circumstances, it does not seem fanciful to suggest that if the country votes to leave the EU, the ministry's efforts for the next 20 years will be spent uncoupling the country's laws from the EU, and all interest in fixed-costs proposals and similar schemes will just fall off the political agenda.

It follows, in turn, that the financial interests of litigation lawyers will be served by voting for Brexit, the costs tail wagging the constitutional dog. But should the country leave the EU, it will become decoupled from not only EU jurisprudence, but also the comparative jurisprudence of the other member states, including Germany, whose legal system enjoys a much greater incidence of fixed costs than our own, and whose influence is clearly to be seen in the proposals for fixed costs in the vast majority of civil cases.

If the country votes to remain in the EU, and if a comprehensive scheme for fixed costs is introduced in England and Wales (that is two pretty big 'ifs'), then it would be instructive to consider what the German experience – over the last 150 years – has been, and what lessons might be learnt for our own jurisdiction.

GERMAN FIXED COSTS

THE JACKSON REPORT

In volume two of the *Review of Civil Litigation Costs: Preliminary Report* published as long ago as May 2009, Jackson LJ noted how the regime of fixed fees, originally introduced in the 19th century in the German courts, worked:

'The quantum of legal costs that a successful party is entitled to recover from an unsuccessful party, and the fees and expenses of the court which are payable, are prescribed by statute. These rules do not seek to provide a successful party with a complete indemnity for their legal fees. Instead, they provide for the payment of legal fees and court costs in scales which increase in a degressive, non-linear fashion and with the use of multipliers that vary according to the value of the dispute, the stage at which the case is resolved, and other aspects of the case.

'Illustrations are given of how these rules apply to disputes of varying sizes, in respect of the amount payable by the unsuccessful party (leaving aside that party's own legal fees, which it must bear).'

Jackson gave the following examples:

- Amount in dispute = €10,000

Court fees payable of €588.00; Lawyer's fees payable (for one lawyer) of €1,869.37; total payable by unsuccessful party of €2,457.37.

- Amount in dispute = €100,000

Court fees payable of €2,568; Lawyer's fees payable (for one lawyer) of €5,123.07; total payable by unsuccessful party of €7,961.07

- Amount in dispute = €1,000,000

Court fees payable of €13,368; Lawyer's fees payable (for one lawyer) of €16,900.85; total payable by unsuccessful party of €30,268.85

These fees represent the scale applicable in 2004; it is interesting to note that they represent a small proportion of the amounts in dispute, and far smaller sums than one would anticipate being spent to litigate

substantial claims in this country. They also have a particular policy underpinning them. They are intended to ensure cross-subsidisation of the legal profession, with larger cases 'carrying' smaller cases within the same lawyer's caseload. As Jackson LJ put it: 'A notion which underpins the cost scales used in Germany is that of "cross-subsidisation" which, in summary, posits that a lawyer may earn a reasonable living out of their profession by accepting a number of smaller cases where remuneration under the scale of fees is not very great (and there may be only a small profit margin) and in addition accepting a number of medium or large cases where the scale fees are higher. If a lawyer's practice consists of a mix of small, medium and high-value cases, the theory is that the fees from the medium- and large-value cases will "cross-subsidise" those derived from smaller ones, enabling the lawyer overall to earn a reasonable living.'

This is a familiar concept to the English and Welsh regimes of fixed costs, known as 'swings and roundabouts'. But whereas such a system reflected the German legal profession when introduced in the time of Bismarck and the Kaisers, it is creaking under the strain of changes in the legal profession and practice of Germany in the 21st century, including an increase in the size of law firms, increasing specialisation, and the fact that smaller firms, undertaking smaller claims, find it difficult to attract and undertake the larger claims which should be cross-subsidising their caseload.

In recent years, contingency fees have also been declared lawful in Germany, which increases the scope for lawyers to make 'own client' charges, which cannot be recovered from the unsuccessful losing party.

It is interesting to note, however, why fixed costs have been used by Germany on such a large scale. They are seen as integral to the vision of 'access to justice' held in that country. Jackson said: 'The use of cost scales is regarded by the courts as beneficial, as their application gives effect to a central value enshrined in the German constitution, being the "rule of law". The rule of law requires not only that there should be free access to the courts, but that litigation costs should be both predictable and reasonable. It also requires the German legislature to ensure that access to the courts does not depend on the economic situation of an individual. One of the ways in which the legislature ensures access is by offering legal aid to people who meet the relevant criteria for such funding.'

CONTEXT

Context, however, is everything. Although Germany has an adversarial rather than inquisitorial system of courts, there are features of the German system which are very different from our own: there is no process of disclosure, no exchange of witness statements, cross-examination is limited, experts are appointed by the courts, and interlocutory processes are devoted to eliciting what are the relevant issues and disputes, so that the final trial can be very short, rarely lasting more than a day. And with truncated court processes, most cases in the local courts run from commencement to final hearing in just over four months, and in the regional courts just over seven months.

The key point to note here, surely, is that if costs are fixed at a level below the sums in dispute, as a quid pro quo, then the amount of work that the court and the substantive law requires must be reduced, to ensure that it remains feasible for a lawyer to complete it within the scale of fixed costs and still make a profit.

A corollary of a large-scale comprehensive scheme for fixed costs across the bulk of civil litigation has been the effect on the legal expense insurance market in Germany, which is unrecognisable in its extent to a lawyer in England and Wales. Such policies are also far more expensive than the modest premiums charged for before the event insurance in the UK.

Jackson LJ's Interim Report also noted some research called the Soldan study, which revealed that while 35% of litigation was funded by legal expenses insurance in Germany, in the UK only 4% of litigation was: 'What is evident from the Soldan study is the significant role that legal expenses insurance plays in Germany when compared with England and Wales. It is common for individuals in Germany to take out legal expenses insurance to cover their legal fees in the event that they are involved in litigation, whether as a claimant or a defendant. Legal expenses insurance covers individuals for costs according to the statutory scale. The advantage to insurers is that the scale of costs makes the extent of the insurer's exposure predictable. The widespread use of legal expenses insurance is seen as the driver of the widespread use of cost agreements according to the cost scales. It is difficult for lawyers whose clients are covered by legal expenses insurance to negotiate an individual fee agreement for remuneration at a rate above the applicable scale.'

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CONCLUSIONS

From these points, some conclusions seem to leap off the page. Should a scheme of fixed costs be introduced in England and Wales along the lines of Jackson LJ's proposal, it could well cause a restructuring and fragmentation of the legal profession.

Secondly, such a scheme would have to march hand in hand with some fairly radical streamlining and cost cutting of the litigation process, with cherished exercises such as disclosure being ruthlessly curtailed, if not eliminated.

Thirdly, such a scheme might be blunted through the rise of irrecoverable own client charges, a concept inherent in the current principle of proportionality.

Finally, although such a scheme would undoubtedly reduce a lawyer's remuneration on individual cases, it might - just might - through encouraging litigation by making it more affordable, not only increase access to justice, but give opportunities to the cannier lawyers to gain more work too, through an explosion of new claims.

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