

The Discount Rate

Amanda Yip QC

EXCHANGE
CHAMBERS

Back to basics

- Future loss is capitalised by applying a multiplier to the annual loss
- Multipliers depend on the discount rate to be applied
- The discount rate balances investment returns against inflation
- The aim is to ensure the claimant is neither under or over-compensated

EXCHANGE
CHAMBERS

Hodgson v Trapp

"... the conventional approach is to assess the amount notionally required to be laid out in the purchase of an annuity which will provide the annual amount needed for the whole period of loss."

EXCHANGE
CHAMBERS

Wells v Wells

"A discount must be given for the fact that money is being paid now for a loss which will not arise until some date in the future."

Lord Hope

EXCHANGE
CHAMBERS

What does a negative discount rate mean?

- The rate is not producing a discount but rather an uplift
- The multiplier is higher than the number of years it represents
- Because the impact of inflation is greater than the impact of investment
- Lower discount rates lead to higher damages
- The discount rate may be seen as the net allowance for the return on investment balanced against inflation

Historical Background

Lim Poh Choo v Camden & Islington H.A.

"Perfect justice is not attainable: nor would it be wise in the search for the nearest approximation to justice to abandon principles already judicially determined, whatever one's "saucy doubts and fears." If your Lordships can lay down, by decision in this case, an intelligible and moderate way of assessing damages for catastrophic, but not fatal, personal injuries under the law as it now is, there will have been achieved all that the judicial process can offer towards the improvement of this area of the law."

Cookson v Knowles

"In times of stable currency the multipliers that were used by judges were appropriate to interest rates of 4 per cent. to 5 per cent. whether the judges using them were conscious of this or not."

The Ogden Tables

- First published in 1984
- *"to help the courts in determining upon what lawyers describe as the multiplier."*
- Working Party noted that courts were conventionally using discount rates of 4 to 5%
- Recommended calculating multipliers by reference to ILGS (then 2.5 to 3.5%)

Index-Linked Government Stock

- ILGS introduced in 1981
- Government bonds that pay interest linked to the RPI – therefore meets inflation
- Government guarantees interest and principal payments – therefore very secure investment
- Limitations – release is random; do not mature every year; not available on issue to individuals

Damages Act 1996

- Came into force September 1996
- Lord Chancellor given power to set discount rate
- Court permitted to take a different rate if “more appropriate to the case in question”

Wells v Wells

- House of Lords 1999
- Investment in ILGS held to be the most accurate way of calculating the present value of the future loss
- A claimant who is not in a position to take risks and wants to protect against inflation in the short term will be prudent to invest in ILGS
- It is desirable to have one rate (therefore no distinction for longer periods of investment)
- How claimant will in fact invest is irrelevant
- Guideline discount rate of 3%

EXCHANGE
CHAMBERS

The Damages (Personal Injury) Order 2001

- Lord Chancellor exercised his powers on 25.6.01 setting rate at 2.5%
- Based on three-year average yield on all ILGS
- Further statement on 27.7.01 explaining basis of rate
- Yields considered to be artificially low at the time but likely to return to higher rates (which has not happened as we now know)

EXCHANGE
CHAMBERS

Challenging the 2.5% rate

- **Warriner v Warriner** [2002] 1 W.L.R. 1703: the term “exceptional circumstances” in the LC’s statement was a helpful explanation of when another rate would be “more appropriate” under section 1(2) – would have to be something not in LC’s contemplation
- **Cooke v United Bristol Health Care** [2003] EWCA Civ 1370 – section 1(2) cannot be used in an “illegitimate attempt to subvert the Lord Chancellor’s discount rate” – long life expectancy and high damages not enough

The impact of PPO’s

- Available under section 2(1) of the Damages Act 1996
- Came into force 1st April 2005
- Embraced by NHSLA
- Not available for claims against MPS and MDU
- May mitigate impact of discount rate

Thompstone v Tameside and Glossop Acute Services NHS Trust

- Court of Appeal accepted PPO wholly different creature from lump sum
- Use of earnings based index rather than RPI used to uplift PP's for care
- This could not be compared to the illegitimate attempt in **Cooke** to get round the discount rate
- Demonstrates problem in discount rate being linked to ILGS which in turn is linked to RPI

EXCHANGE
CHAMBERS

Helmot v Simon

- Court of Appeal Guernsey – Jonathan Sumption QC
- Damages Act did not apply – no LC's discount rate
- Used ILGS as basis for discount rate
- Took account of tax and difference in price and earnings inflation
- -1.5% for care and 0.5% for other heads of loss

EXCHANGE
CHAMBERS

Lord Chancellor's review

- First consultation paper 1st August 2012 (following repeated calls and APIL judicial review in April 2011)
- Second paper 2013
- Working party appointed 2015
- Further threat of judicial review
- Announcement 7th December 2016
- New rate -0.75% with effect from 20th March 2017

EXCHANGE
CHAMBERS

Lord Chancellor's statement

- *"I am clear that this is the only legally acceptable rate I can set."*
- *"the government will launch a consultation in the coming weeks to consider whether there is a better or fairer framework for claimants and defendants, with the government bringing forward any necessary legislation at an early stage".*
- Consultation opened 30.3.17 and closed 11.5.17 – response to be published by 11.8.17

EXCHANGE
CHAMBERS

Where are we now?

- Discount rate is now -0.75%
- Defendants anticipating a change in their favour – reluctant to settle claims on basis of -0.75%
- Settlement may require more creative thinking
- Variation clauses?
- Fact sensitive solutions

Impact of the new rate

- Government has set aside extra £1.2 billion a year to meet expected costs to public sector (mainly NHS)
- In theory total awards may be doubled or even tripled
- Biggest impact on long life expectancy cases
- Multipliers of over 100 are being seen
- But remember PP's are wholly unaffected
- Media reports may be overstating the impact in individual cases (capitalising PP's using new discount rate)

Other consequences

- Impact on parties' preferences as to the form of the award
- The Roberts v Johnstone claim

Claims for Accommodation

- **JR v Sheffield Teaching Hospital NHS Foundation Trust** - nil R v J award
- **Wells v Wells** linked multiplicand to discount rate – *"it will be kept up to date by the Lord Chancellor when exercising his powers under section 1 of the Damages Act 1996"*
- Claim must not offend against principle in **George v Pinnock** that the full capital cost cannot be recovered (easily breached with -0.75% multipliers)
- Other options now need to be explored

What comes next?

- *"Following the consultation, which will consider whether there is a better or fairer framework for claimants and defendants, the Government will bring forward any necessary legislation at an early stage."* (Consultation Paper)
- Liz Truss (now the former Lord Chancellor) committed to 100% compensation principle – will this survive though?
- In **Wells v Wells** the judges raised questions about the affordability of increased claims but left this to Parliament
- Will claimants continue to be treated as special category of investor?

Alternative calculation methods?

- See Chapter 4 of the Working Party's 2015 Paper
- *"A financial economics approach can arrive at a range of discount rates, depending on appetite for non risk-free assets."*
- Portfolio could not properly involve less than 50% in ILGS
- 50% ILGS and 50% in a range of other low risk investments would produce 0.75%
- 75% ILGS and 25% other investments would give 0%

Managing the uncertainty

- Understand the underlying principles
- Think sensibly and possibly creatively
- Consider what claimant needs to achieve
- Seize the opportunity

EXCHANGE
CHAMBERS

**AMANDA YIP QC
EXCHANGE CHAMBERS
JUNE 2017**

email:

yip@exchangechambers.co.uk

Twitter: [@AmandaYipQC](https://twitter.com/AmandaYipQC)

EXCHANGE
CHAMBERS