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The Insurance Crisis – Don't Forget the Victims

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Introduction

One could hardly have failed, in recent months, to note that the insurance industry, Australia-wide, is in a state of crisis. Many factors have combined to create this state of affairs, but the net effect for many insurance companies has been that they can no longer afford to pay all the claims which they currently face, either at all, or without raising the premiums which they charge to a level which many people requiring insurance simply cannot pay.

Donohue v Stevenson - Law of Negligence

One area of legal practice which has been amended and extended almost beyond recognition during that same period is the one we call "personal injuries". The economic decline in the insurance industry at the same time as the rapid growth in personal injuries claims is no mere coincidence. It is one more lingering echo of what happened over seventy years ago, one lazy Sunday afternoon in the Scottish town of Paisley, which led to the House of Lords in *Donoghue v Stevenson* [1932] A.C. 562 solemnly considering the consequences of allowing a snail into a bottle of soft drink.

The modern law of negligence which has developed from that landmark judgment bears little resemblance to its origins. The principle established in the original case was that if one person (A) could be said to owe what is called a "duty of care" to another person (B), and he or she fails to take "reasonable care" for B's safety, then if B is injured in some way, he or she may sue A for whatever losses are suffered.

In its early form, the law of negligence was easy to grasp, and fairly easy to predict. For example, everyone driving a car, or any other motor vehicle, owes a duty of care to all other road users, their passengers, and indeed even pedestrians walking on the pavement. If a motorist drives negligently, and someone is injured, then that someone can sue the motorist at fault.

Today, in almost every area of life you can imagine, people owe duties of care to other people. Doctors treating patients, shop proprietors and hotel owners who invite customers onto their premises, and even private householders who entertain visitors in their own homes, owe this "duty of care".

The precise nature of the duty will obviously vary from one situation to another. A doctor has to use reasonable care in treating his patient, the owner of premises has to ensure that they are reasonably safe for other people to enter, and so on. But in every case, the end result is the same - if they fail to exercise "reasonable care", then the injured person can sue for damages.

These damages can be astronomical. Several months ago, for example, a court in Sydney awarded over \$4 million to a

young man rendered paraplegic after diving into a sandbank on a patrolled beach. The amount was worked out on the basis that this is what it will cost to look after the victim for the rest of his life, the special equipment and medical care he will need, the fact that he will never again be able to earn a living, and so on.

Nor are damages limited to physical injuries, although these are the most obvious "head" of damage, as lawyers call it. Solicitors who give negligent advice to their clients can be sued for any financial or business loss which the client suffers, and the same is true of other professions such as accountancy and banking. Also, even when people have not suffered any physical injury, they may well be able to claim damages for what is called "nervous shock" if for example they were passengers in a road accident, or even if they simply saw it happen.

The Need for Insurance

Obviously, most people who owe these duties of care simply couldn't pay those damages if called upon to do so. At the same time, they cannot even drive a car, invite people into their homes, or run a business, without exposing themselves to the risk that someone will one day sue them. The "answer" is for them to take out insurance.

An insurance policy is a form of contract under which the insurance company undertakes that if a certain defined event occurs which results in the policyholder being held liable, then the insurance company will meet the damages bill. In exchange for that protection, the person taking out the insurance pays what is called a "premium" to the insurance company. That will vary from company to company, and will obviously depend upon what sort of risk is being insured against.

In many cases, such insurance policies are compulsory before a person can continue in business, or carry out certain processes. For example, part of the registration cost of putting a car on the road every year goes towards what is called "compulsory third party insurance", which is the insurance cover which ensures that if someone is injured by a person driving that car, then the insurance company will meet the damages bill. Employee insurance is compulsory for employers, and professional negligence insurance is compulsory for solicitors.

It is against this basic background that the present insurance crisis has arisen. Insurance companies all around the world - not just in Australia - have been inundated with a volume of claims which they cannot possibly hope to pay out without putting up the premiums for next year to a level which is beyond the resources of those who, without appropriate insurance, cannot carry on in business, or whatever it is they wish to do.

Some insurance companies have already collapsed, either

through mismanagement of their funds by their own executives, or because of the mounting cost of claims. When that happens, people who had policies with them are faced with the prospect of either paying any damage bills for themselves (which will almost certainly wipe them out financially), or paying massively increased premiums to other companies.

One "spin-off" from this primary crisis has been a "secondary" one in the health services, with many doctors threatening to retire from practice because their main insurance provider - the Medical Defence Fund - collapsed as part of the HIH financial disaster. They are now being called upon by new insurers to pay premiums which are so high that they simply cannot continue in practice. This means that not only do they have to give up their professions, but of course the community loses doctors it can ill afford to lose.

Just recently, we have heard of even charity or "non-profit" organisations which can no longer afford the increased premiums to cover their annual fundraising day, surf life-saving clubs which are going to have to fold up their flags and cease covering the beaches, and so on.

Lawyer's Role

But it's not just financial mismanagement by the insurance companies that has led to this sad state of affairs, and much media attention has recently focused - quite rightly - on the role which lawyers have played in the overall mess in which we now find ourselves.

Most people who have a legal claim need a lawyer to help them through the maze of procedure and legal mumbo-jumbo which is necessary in order to successfully launch an action for damages. Once a person who has insurance is notified formally that he or she is being sued, then the matter is reported to the insurance company, and its lawyers take over. So from Day 1 you have lawyers on both sides, racking up the costs as they begin throwing paper at each other in ever-increasing amounts.

At the end of the day, as a general rule, whoever loses is not only liable to pay their own legal costs, but also the costs of the winning side. These can often be higher than the original damages claim. I was involved in a Supreme Court action over 10 years ago in which the original sum sued for was around \$700,000. Two years, two QCs, two junior barristers, two solicitors, one Supreme Court judge and 9 court weeks later, we won, and the combined legal costs came to just under \$1.8 million.

For this reason, insurance companies will often agree to pay out on relatively small claims without going to court, and without formally admitting liability. This has two consequences. First of all, of course, it means that they have to put the premiums up the following year, but perhaps even more importantly, it encourages people to make claims which are sometimes not really all that genuine, or are in some cases downright dishonest.

Legal Costs

There was a time when the main factor which that stopped people from doing that was the need to pay at least some legal costs even if they won, because the legal costs awarded against the other side didn't always cover the full amount charged by their own lawyers. And of course, if they lost, then they had to pay the other side's costs.

There is, of course, no risk of that if you don't have any

money. Getting a court judgment against someone is often the easy bit. If they don't own a car or a house, or have money in the bank, then there's nothing you can do except bankrupt them. Not only does that not get you your money, but it's no great threat to someone who has nothing in the first place.

Even then, people with no assets who wanted to bring a legal claim in the old days still had to find the money to pay their lawyers "up front", or at least as they went along, and that was enough to deter most people. Then lawyers themselves became more desperate to earn more money, as their own costs - including of course insurance costs - got higher and higher every year. And so they hit on the idea of what is politely known in legal circles as "contingent feeing", but which you have seen advertised as "no win, no fee".

What this means is that the lawyer will agree to act for the client for nothing unless and until he wins his claim. If he loses, he pays nothing to his lawyer - and for the reasons already explained, if he is already penniless, then he is under no real risk of having to pay anything to the other side. If he wins, his lawyer takes an agreed proportion of the winnings by way of his fees, some of which has to be paid by the other side anyway - and the "plaintiff", as he is called, makes a net gain. Sometimes, this can be a very substantial amount of money.

This process has already resulted in hundreds and hundreds of potentially "dodgy" claims by people who have nothing to lose, whose lawyers are prepared to run the risk of not getting paid in the hope of making substantial fees if the client is successful. Given the tendency for insurance companies to pay out on some claims without bothering to test the matter in court, it is not long before these insurance companies found themselves facing massive losses which they had to pass on to their clients in higher premiums for the future.

Lawyers are of course not the only ones to blame, and a lot of the responsibility for where we find ourselves today must be shouldered by the increased publicity given to people's "rights", and the inclination to blame someone else for a situation which you have helped to create, and to sue for enough money to keep you comfortably for the rest of your life.

There are, of course, many plaintiffs with genuine claims arising from genuine accidents causing genuine loss and damage, pain and suffering, ruined lives and so on. But the irony is that in future, they will probably be the greatest losers, as both State and Federal Governments begin enforcing policies designed to ease the pressure on insurance company funds.

Law Reforms

What are these new initiatives likely to be? Nothing has yet been set in stone, but the following are among the plans already on government drawing-boards;

- The enactment of new laws which make it impossible to claim for certain types of injury. A person can only claim damages in a situation in which the law says that there is a duty of care owed to him by someone else. If, for example, the Government wanted to cut out all claims arising from injuries sustained on defective fairground rides, it could do so simply by passing a new Act of Parliament which eliminated the duty of care of the operator towards those using those rides. A variant on this theme, recently

announced in Victoria, is to prohibit all claims in which the victim was under the influence of drink or drugs.

- Ban all claims in respect of certain types of injury. By Act of Parliament, for example, it could become the law overnight that no-one could claim for what are called “whiplash” injuries caused in a road accident.
- Prohibit lawyers from working on a “no win, no fee” basis. This would of course unfairly discriminate against genuine claimants who have no money to pay “up front”, but it is being seriously suggested.
- Place a “cap” on the size of the legal fees which could be either recovered or claimed in respect of either a certain category of claim, or below a certain level of pay-out. An example might be a “cap” of, say, \$2000 in legal fees for all pay-outs under \$30,000, or all payouts in respect of “soft tissue” injuries such as pulled muscles or torn ligaments.
- Grant legal immunity to certain types of organisations which do not operate for profit. This would allow, for example, charities and community organisations such as SLSCs to continue operating without any fear of being sued, and therefore without the need to seek insurance. This is already being strongly mooted in New South Wales.
- Place limits on either the total size of any payout, or the way in which it is paid. Most compensation payments at present are paid out in the form of a “one off” lump sum, and it is up to the victim how to spend it. It would help to spread the burden placed on insurance companies if in future, such payouts could be in annual instalments, or paid direct to third parties (e.g. hospitals and specialists who treat the victim’s injuries).

Conclusion

These are just some of the ideas which are currently being considered. Only time will tell which are chosen, and what other ideas are developed. But this is not a topic which can be ignored, and we have most certainly not heard the last of it.

Discussion Point

Do you agree with the proposals for law reform discussed above?

Activity

Think about what you do on a daily basis and list those persons who might owe a duty of care towards you. Why do they owe a duty of care and what might be their obligations?

For example does the school bus driver owe a duty of care towards you as a passenger?

Does your high school teacher owe a duty of care towards you as a student? What might a teacher be obliged to do to satisfy that duty?

Ask your parent what form of insurance they might hold (ie such as public liability insurance and car insurance) and ask them why they hold that form of insurance?