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## Insurers, Their Lawyers and Today's Economic Challenges

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*Written by JHK Legal Senior Associate Shan Auliff*

### INTRODUCTION

Australian Insurers are finding the honeymoon may be over. With floods, fires and cyclones in multiple States of Australia, corporate collapses resulting in multi-million dollar Insurance claims by out of pocket investors and shareholders and the global financial crisis, Insurers are understandably frightened, timid and seeking to minimise their costs wherever possible.

Their lawyers are finding there is a growing need to respond to the economic pressures on the Insurance Industry and the resultant cost minimisation mind-set of Insurer Clients.

This article will explore the changing landscape of Australian Insurance and the ways that lawyers representing Insurers may seek to modify their practices to meet this change. The article will also explore the potential benefits of two ways legal service providers may seek to modify their practice, alternative fee arrangements and seeking to reduce the costs of litigation.

While no single strategy will totally reduce the pressures faced by Insurers with regard to the legal services they use, Legal Service providers must work with their clients to not only minimise legal costs, but more importantly develop strategies to maximise value and profitability for the client.

### GLOBAL CRISIS, LOCAL CATASTROPHE, THE FLOW-ON EFFECT

The global economic crisis has had implications for both Insured parties and the companies that insure them. For Insured parties, economic conditions have resulted in increases in insurance premiums and reductions in or difficulty obtaining coverage.<sup>[1]</sup> For Insurers, corporate collapses have led to increased claims under Director and Officers Liability and Statutory Liability Insurance Policies and Insurers have found themselves being joined as parties to civil litigation between their client's and third parties.<sup>[2]</sup>



The combination of these global economic pressures and significant weather events across Australia over the last 24 months have resulted in significant decreases in profitability for some of Australia's major Insurers.[3] It is as a result of these changes to the insurance landscape that legal service providers need to review their relationships with their clients and find ways to better service their needs.

### **FIXED FEE, TENDERS, ALTERNATIVE FEE ARRANGEMENTS**

There is no question that the current economic climate has had and will continue to have an effect on client's attitudes to legal costs.[4] The Insurance Industry in particular is increasingly cost conscious, a trend reflected in an increased number of client requests to move from the traditional time billing methods used by the vast majority of law firms to alternative billing methods.[5]

The disadvantages of time billing for both clients and lawyers have been well publicised and include a lack of cost certainty for the client and a focus on the time spent on a file by legal practitioners, rather than the value of work completed to the client. Alternative fee arrangements such as fixed costs, staged costing, value billing and capped fees can serve to alleviate these disadvantages.[6] For a cost conscious client seeking to minimise their legal spend, alternative fee arrangements may be able to provide the budget certainty required to enable legal action to remain a viable method of resolving disputes.[7]

Additional benefits of alternative fee arrangements are that they can have the effect of removing any enticement for lawyers to over-service a matter to meet billable hour targets. As an example, fixed cost billing can provide lawyers with motivation to ensure that only those tasks required to achieve a positive outcome are undertaken, and to reduce time spent on matters wherever possible. These inducements arise as it is only through these actions that law firms can ensure that fixed fee arrangements are financially viable for not only the client, but the law firm itself.

However, as always in the law, there is a reverse side to the alternative fee arrangement coin. Some opponents have raised concerns that where billing is fixed or capped, lawyers can be incentivised to cease working on a file once the maximum fee has been reached, or have work conducted by less experienced solicitors and paralegals to reduce costs. There are also many cases where time billing is still considered the most appropriate billing method for both clients and lawyers, such as where there are variables that make assessing the cost of a file impossible, or where court approval is required for fees.[8] Time billing also allows for the highest level of client scrutiny for work done, time spent and the costs associated, as it allows a client to contemporaneously monitor work that has been completed and costs charged for items of work.

What becomes apparent from the above is that there is no one set panacea that can be implemented to lower legal costs for Insurance Clients. However it is equally clear that in order to respond to client's increased scrutiny of legal costs and requests for changes to traditional billing methods; it is necessary for legal service providers to be open to alternative fee arrangements and structures.[9]

### **THE NEED TO REDUCE THE COST OF LITIGATION**

It is not only in the calculation of legal costs that there are opportunities to meet the changing needs of Insurance Clients. It is also possible to identify and take advantage of opportunities for 'mutual long term benefit (seeking better value) rather than simply short-term gain (cheaper legal

fees').<sup>[10]</sup> Reducing the cost of litigation is a key method that can add value to the services provided to Insurance Clients.

Insurance Litigation contributes a large proportion of common law and commercial litigation in Australian Courts, and the industry pays the large proportion of costs associated with this litigation.<sup>[11]</sup>

Litigation itself is known to be a costly, time consuming and unreliable process of settling disputes, although often the only option left available to parties.<sup>[12]</sup> Although time billing is often blamed for the increased legal costs incurred by clients, some attribute much of this rise to an increase in litigation and the general costs associated.<sup>[13]</sup>

As Australia's primary litigator, the Insurance Industry has a significant vested interest in reducing the costs of litigation wherever possible.

Insurers can often be guilty of overusing experts in litigated matters. It has been suggested that in an effort to reduce the costs of litigation, insurers should attempt wherever possible to agree on a joint independent expert, which can effectively halve the costs involved and may lead to early settlement where both parties agree to be bound by the independent expert's opinion.

As research shows that the longer a matter is delayed, the greater the cost to the parties, a key way to reduce the costs of litigation is to reduce delay wherever possible.<sup>[14]</sup>

Early settlement of matters is a significant tactic in which delay and legal costs can be avoided. Due to the high costs involved in litigating a matter to trial, it has been documented that reduced (or increased, in defended matters) offers of settlement at an early juncture of a matter can result in lesser costs than if the matter continues to and is decided at trial, even where a party is successful. It is therefore necessary for lawyers to expertly assess the chances of success at an early stage of litigated matters, to ascertain whether there are opportunities for a beneficial early settlement, or indeed whether it is more economical for the client to abandon the matter.<sup>[15]</sup>

Negotiating outcomes with other insurers in litigated matters also holds significant benefits for the ongoing commercial relationship that exists between the parties. Insurers increasingly recognise that settling disputes via means other than litigation can be more conducive to maintaining effective long term business relationships with other Insurance companies.<sup>[16]</sup> The more effective the business relationships are between insurers; the less likely there will be disputes in need of resolution, via either litigation or through other less formal legal processes.

## **CONCLUSION**

The above strategies outline just a couple of ways that lawyers representing the insurance industry may modify their practices to respond to the economic pressures faced by the industry. It seems apparent that in order to address the cost minimisation priorities of the industry Legal Practitioners must see the economic downturn as an opportunity to revisit their billing procedures, practices and their relationships with their clients to create positive change. During this period of instability it will be more important than ever for lawyers representing the insurance industry to focus on the quality, efficacy and value of the services they provide to ensure that their relationships with their clients can outlast the slump.

[1] John Morgan, "The impact of the global economic crisis on the Australian Insurance Industry: A legal perspective" (2009) 24(5) *Australian Insurance Law Bulletin* 62 at 62.

[2] Greg Pynt, 'The year that was: in some ways, insurers might prefer it wasn't' (2011) 27(2) *Australian Insurance Law Bulletin* 33.

[3] See M McNamara, 'Floods, Cyclones, Bushfires and the UK: Why IAG's Profits are Down' (2011) *Business Review Australia*, < <http://www.businessreviewaustralia.com/sectors/floods-cyclones-bushfires-and-uk-why-iag-s-profits-are-down>> at 19 June 2012 ; 'QBE Insurance Group reports profit fall, upbeat on 2011 outlook', *Perth Now* 28 February 2011 < <http://www.perthnow.com.au/business/qbe-insurance-group-reports-profit-fall-upbeat-on-2011-outlook/story-e6frg2rl-1226013528953>> at 19 June 2012.

[4] Hon James Jacob Speigelman AC, 'Implications of the current economic crisis for the administration of justice' (2009) 18(4) *Journal of Judicial Administration* 205 at 208.

[5] Brian Armstrong, 'Adding some science to the billing debate' January 2011 *Australasian Law Management Journal* 5 at 5.

[6] David Vilensky, 'The benefits of fixed fee pricing' 39(1) *Brief* 12 at 12.

[7] Jeffrey Carr, 'Future Firm: how to set prices under a fixed fee model' November 2009 *Australasian Law Management Journal* 1 at 1.

[8] Richard Reed, 'Billing Innovations, New Win-Win ways to End Hourly Billing' (1996) at 13-15.

[9] Jeffrey Carr, 'Future Firm: how to set prices under a fixed fee model' November 2009 *Australasian Law Management Journal* 1 at 2.

[10] John Chilsolm, 'A billing discussion worth its time' (2010) 470 *Lawyers Weekly* at 19.

[11] Hon Mr Justice T R H Cole, 'Insurance and the Cost of the Law' (1994) 4(1) *Journal of Judicial Administration* 55 at 55.

[12] Michael Mills and Nicholas Furlan (2002) 'Resolving insurance disputes: the value of less formal processes' 5(1) *ADR Bulletin* 7.

[13] Anne Priestly (2009) 'Breaking the billable myths' 463 *Lawyers Week*

[14] Hon Mr Justice T R H Cole, 'Insurance and the Cost of the Law' (1994) 4(1) *Journal of Judicial Administration* 55 at 56.

[15] Hon James Jacob Speigelman AC, 'Implications of the current economic crisis for the administration of justice' (2009) 18(4) *Journal of Judicial Administration* 205 at 208.

[16] Michael Mills and Nicholas Furlan (2002) 'Resolving insurance disputes: the value of less formal processes' (2002) 5(1) *ADR Bulletin* 7 at 10