Forensic Actuaries

by John H. Prevett (United Kingdom)

The U.K. National Report submitted to the last IACA Conference in Hawaii included a section on the assessment of damages in personal injury and fatal accident cases. It referred in particular to the then recent publication by a joint working party of actuaries and lawyers of a booklet incorporating actuarial tables with explanatory notes prepared by the Government Actuary's Department. The introduction to the booklet by the Chairman, Michael Ogden, Q.C. argued that the availability of index-linked Government securities provided a natural yardstick for the determination of a rate of interest for discounting future losses which would avoid the necessity for the courts to speculate as to future rates of inflation.

This section of the 1984 National Report concluded with the words

"It is believed that the work of the Working Party and the publication of the tables will bring some welcome additional status to the actuarial profession in the eyes of the courts."

The wheels of the law turn very slowly, however, and this optimism has not yet been justified by events. In one or two cases, courts of the first instance have even found the new tables to be inadmissible so we are still in the position that until the new approach and the new tables have been taken by a plaintiff to the Court of Appeal, and probably also to the House of Lords, they will have no authority. It is likely that the plaintiff in such a test case will be a young paraplegic or quadraplegic backed by a trade union, and I am aware of such cases "in the pipeline".

It is understandable that insurers and those lawyers who normally act for defendants should be concerned at the possible escalation of the levels of damages awards which would inevitably result from a more scientific approach to assessment and, in particular, from the acceptance of index-linked yields as a yardstick. But I am surprised that legal opinion generally has not been more ready to accept an objective approach which does offer a solution to the problem of future inflation that has troubled the courts for so long. On the joint working party, of which I was a member, this approach received the unanimous and enthusiastic support of the solicitors and barristers, including a number of distinguished leading counsel.

The Chairman put it this way in his introduction to the booklet:

"The Working Party concluded that the following arguments could not be faulted. The Courts seek to put the wage earner, or, if he has been killed, his dependant, into the same financial position as if the accident had not happened. Investment policy, however prudent, involves risks and it is not difficult to draw up a list of blue chip equities or reliable unit trusts which have performed poorly and, in some cases, disastrously. Index-Linked Government Stocks eliminate the risk. Whereas, in the past, a Plaintiff has had to speculate in the form of prudent investment by buying equities or a "basket" of equities and gilts or a selection of unit trusts, he need speculate no longer if he buys Index-Linked Government Stocks."

There are other active campaigners for reform in the legal profession. David Kemp, Q.C., the author of the principal reference work on damages, has published persuasive articles in the Civil Justice Quarterly (April 1984) and the Law Quarterly Review (October 1985). His first article opens with these words:

"The primary purpose of this article is to demonstrate that the court's present practice in assessing damages for future pecuniary loss is erroneous. It substantially under-compensates plaintiffs for future pecuniary loss, whether for future loss of earnings or for future expense. This error causes injustice, particularly to younger plaintiffs.

A secondary purpose is to urge the greater use of actuarial calculations in assessing such damages."

The current practice of applying a discount rate (if one is identified at all) of 4 to 5 per cent, ignoring tax in all but the largest cases, derives from a dictum of Lord Diplock in the 1970 case of Mallett v. McMonagle. David Kemp points out that it was Lord Diplock again in the 1983 case of Wright v. British Railways Board who, after making a careful analysis of the net rate of return on index-linked securities, concluded that it was by reference to such yields that the courts should determine an appropriate rate of interest to award on the non-pecuniary portion of a plaintiff's general damages from the date of service of the writ up to the date of judgment.

The courts have not yet accepted that the same principles should be applied in determining a real rate of return for the purpose of discounting future losses. David Kemp comments in his second article as follows:

"Although the immediate subject matter in Wright's case was different, the court's quest was the same as in the subject presently under discussion. In each case the court is, or should be, seeking a net rate of interest which represents the real return to be derived from the investment in question: in Wright's case it is the real return to be derived from the past realisation of an index-linked investment: in the present case it is the real return to be derived in the future from the present receipt of a lump sum as compensation for future pecuniary losses.

It would be a facile and ill-founded comment to say that the reasoning in Wright's case does not apply to the topic under discussion because that case dealt with pre-trial interest and the present discussion relates to future interest. The truth is that in both cases the court is seeking and should adopt a net rate of interest which represents the real return on the "investment" in question and that Lord Diplock's own analysis shows that the previous "Diplock approach" can no longer be regarded as valid."

I must apologise for such extensive quotation, but it is worth including the conclusion of David Kemp's article in the Law Quarterly Review, a publication which is considered to have some influence on the thinking of the judiciary:

"If my contention is well founded, current practice is contrary to the cardinal principle governing compensation for pecuniary loss and plaintiffs are being deprived of very large sums of money. Accordingly, I venture to hope that the House of Lords may have occasion to consider this important topic at an early opportunity. But if any plaintiff's legal advisers should be contemplating such course, it would be essential to provide the proper factual basis at the trial. Actuarial evidence should be called to establish the difference in

multiplier which would result from discounting at a rate equivalent to the net return from index-linked securities rather than at 4 per cent to 5 per cent.

An alternative is legislation. If the Government is unwilling to act, the topic would be suitable for a private member's Bill, the operative part of which could be short and simple: e.g.

"When the court assesses damages as compensation for future pecuniary loss, the discount rate to be used for the purpose of the assessment shall be a rate roughly equivalent to the net return to the plaintiff, as at the date of trial, upon an index-linked investment."

Hopefully, when we meet in Bermuda there will be more to report. If change does occur, actuaries are likely to become more involved in these areas of litigation. We need, however, to take note of the growing interest of members of another profession, namely the accountants.

There is no doubt that accountants are already instructed in far more cases than we are. This is particularly so where the estimated pattern of future losses will depend on business projections (for example, in respect of self-employed plaintiffs) or where the tax aspects are complicated. In recent years, accountants have addressed many conferences on damages emphasising that they can offer a package of calculation services dealing with all heads of damage in a single comprehensive report. They do not appear to have championed any reform in the assessment of future losses and are happy to refer to published actuarial tables or derive their own "multipliers" by a discounted cash flow approach to future losses or costs. They have been known to argue that a judge will understand the evidence of an accountant more readily than that of an actuary.

It is not difficult to envisage the areas where accountants will get into difficulties and commit errors. If they are not simply accepting multipliers derived from case law, they adopt the technique of the annuity certain for a period of expectation of life. If there is a loss of earnings and a loss of pension, they are not familiar with the concepts of temporary (e.g. work life) expectation and deferred (e.g. post-retirement) expectation. The consequences may be peculiar if the plaintiff's mortality is impaired such that his reduced expectation is to an age less than pension age.

Each profession has a role to play in this area. I think we have to be vigilant in keeping our role before the public in general and the legal profession in particular by being as active as are the accountants in writing articles and addressing conferences and seminars. The title of this article was in fact suggested by the growing use of the term "forensic accountancy" in publicising the role of accountants.

Since we last met, there has been a useful addition to actuarial literature in the U.K. Two young actuaries in my firm presented a paper to the Institute of Actuaries Students' Society in March 1985 entitled "The Actuary in Damages Cases – Expert Witness or Court Astrologer?" A particularly valuable feature of this paper is the inclusion of check lists of the information and instructions required by the actuary in personal injury and fatal accident claims and in claims for wrongful or unfair dismissal.