

Briefing Note: **Indexation and the NHSLA 2008 Report and Accounts**

Ian Gunn, 19th August 2008

The publication of this document offers a further insight into the indexation cases and future expectations. I have set out below my thoughts on its contents, highlighting the most important elements of the statements. Quotations are from the NHS Litigation Authority 2008 Report and Accounts, and are Crown copyright.

In the Chief Executive's Report, Mr Steve Walker states:

“Also, last year, in respect of the indexation of Periodical Payments, I alluded to our efforts to persuade the Courts that the Damages Act 1996, as amended, expressed Parliament's intention that the Retail Prices Index (RPI) should be the index of choice, with an option for the Courts to vary that only in exceptional cases. Both at first instance and in the Court of Appeal that argument has not been sustained and the Courts have reserved the right to apply whichever index they considered to be more appropriate at the time of settlement.

It is not proposed to pursue this matter further by taking it to the House of Lords.

In practice, as mentioned elsewhere in this report, the effect of adopting alternative indices is inflationary in respect of individual claims, and in the aggregate. In the short term, CNST, and therefore the NHS, benefits from certainty and cash flow, but the long term impact means that our provisions have been dramatically increased. The difficulties of calculating provisions can be understood when one considers that the currently chosen index, ASHE 6115, fluctuates against RPI over time, and the matter is further compounded by the fact that we cannot know in advance which, if any, cases will settle on the basis of Periodical Payments, either by election or by the order of the Court.

*Against those difficulties for the NHS and for CNST, it should be remembered that this Authority is obliged, once liability has been established, to secure “appropriate access to remedies” for patients, and **from a patient perspective, it will certainly appear that the Courts have been correct in their interpretation of Parliament's intentions.**”*

Mr Tom Fothergill, Director of Finance, continues:

“Periodical payments are damages settlements which include payments made on a regular basis, usually throughout the claimant's life, in place of the traditional single lump sum to cover all future needs.

The Authority continues to encourage the use of periodical payments when appropriate.

At 31 March 2008, we were making periodical payments in 548 cases, compared with 471 at 31 March 2007, the provisions for which total £900,775,621 (£662,964,855). **We consider that these payments are the fairest method of settling most, if not all, large personal injury claims, when future costs are so significant.**

As mentioned above, the decision of the Court of Appeal in the Thompstone case has had a significant impact on these periodical payments.

The Authority, via its actuaries, has created a model to establish the extent of this impact on its open claims and any claims which have been incurred but not yet reported. The global value of this increase in provisions recorded in these accounts as at 31st March 2008 is £1.5 billion. This increase is so substantial because the element of damages which relates to future care in clinical negligence claims tends to be a substantial proportion of the overall settlement and this proportion tends to grow larger as the overall value of the claim increases i.e. it has a larger proportional impact on the more expensive claims types since a large element of the agreed damages will relate specifically to the future care needs of the claimant.

For example, a claim which might have a traditional lump sum value for damages of £4m will be made up of a number of elements but **future care traditionally accounts for in excess of 45% of the award** i.e. £1.8m of the damages will be to enable the claimant to purchase their future lifetime care needs and as a result of this judgement the agreed annual value at the inception of the periodical payment order (PPO) will now be inflated at, say, 4% per annum rather than 2.5% (**assuming RPI is 2.5%**) thus a payment of £100,000 per annum for life would, using RPI, be costing the Authority approximately £185,000 per annum in 25 years' time whereas using ASHE 6115 at 4% per annum (assuming RPI at 2.5% and ASHE at 1.5% greater) the same initial payment will be costing approximately £266,000 in 25 years' time. The Authority will, in subsequent years, need to review its actuarial models to recognise alterations in its assumptions due to actual data on the various indices and also where the take up of PPOs is outside the forecasts assumed currently. Such variations will, when applied, inevitably alter the provisions of the Authority which, it should be remembered, are best estimates of the likely value of all claims against the NHS should they all be settled in full at the point of creating these accounts whereas the reality is that these cases will both materialize and be concluded at some point into the future.

Note 9 on page 61 explains this further.”

Note 9 states:

“During November 2007 the Court of Appeal heard a group of cases where the claimants had argued that an index, other than the traditional Retail Price Index (RPI), be used to inflate the annual payments made to the claimant under a Periodical Payments Order (PPO). The Authority has referred to this group of cases as ‘Thompstone’ and reported progress in a previous annual report and accounts.

The decision of the Court of Appeal was to uphold the original judgement and therefore allow an alternative index to be used to calculate the uplift for the part of the PPO which relates to the purchase of care. i.e. the Court agreed with the claimant that RPI should not apply to the portion of the annual payment which the claimant was expected to use to purchase future care which would normally take the form of employing specialised staff.

Essentially the Court accepted that these expenses are likely to naturally inflate at a rate higher than RPI since wages generally grow faster than RPI. The Court awarded the claimants an index referred to as Annual Survey of Hours and Earnings (ASHE) 6115. This index is collected annually and is available across of number of sub headings which are linked to specific groups or types of workers and the Court felt that it offered a more appropriate link to the actual costs likely to be borne by claimants who were in receipt of damages via a PPO.

The decision of the Court potentially means that all cases which the Authority subsequently settles via a PPO, whether agreed between the parties or imposed by the Court, will now receive ASHE 6115 as the relevant index to inflate care costs.

The impact of the judgement in Thompstone has therefore to be reflected in the financial accounts of the Authority since there is a likelihood that future settlements will attract this revised index.

In order to calculate the potential impact on claims the Authority has had to assume a future value for the index since, unlike RPI, there is no current accepted forecast value (this is one of the reasons the Authority chose to oppose the original claims) and thus there is no way for the Authority, or indeed the claimant, to plan appropriately without making an assumption. **The Authority has, with advice from its actuaries, opted to assume that over time the average differential between ASHE 6115 and RPI will be +1.5% i.e. that ASHE will be 1.5% higher than RPI.**

Having established a value for ASHE compared to RPI **the Authority has then assumed that a PPO will be the preferred settlement route, as compared to a traditional one off lump sum award, in 75% of the claims where part of the damages relates to future care** i.e. where the agreed compensation includes an assumption that the claimant will have to buy care which is not freely available via the state and where the care is appropriate to deal with the damage caused by the original negligent treatment. We have not assumed a 100% take up rate for PPOs because (a) not all cases will require interaction with the Courts and thus PPOs may not be imposed upon the parties and (b) some claimants will be able to demonstrate, even when there is interaction with the Courts, that a PPO does not offer an appropriate route to settlement for e.g. where a family plan to emigrate.”

Some of the more notable facts and figures disclosed include:

- Liabilities under the various schemes administered by the NHSLA total just over £12 billion. Of this, £1.4 billion is expected to be paid out within one year, a further £3.8 billion over years 1 to 5, and the remaining £6.9 billion after more than five years.
- To put this in context, the revenue expenditure for the entire NHS in 2007-08 was approximately £87 billion.
- During the year, the number of periodical payments cases increased by 77 on the total of all cases since 1995.
- This is a 16% increase on the previous cumulative total of cases.
- However, the number of cases parked pending the outcome of the *Thompson* group of cases resulted in the payout for 2007-08 being lower than expected. It is therefore not without some irony that an immediate consequence of the indexation litigation was to reduce the annual contribution of individual NHS Trusts to the CNST, as surplus cash is being returned to them.
- The increase in liabilities resulting from the indexation cases is valued at £1.5 billion. This is based on a model developed by the NHSLA's actuaries, which contains the following assumptions:
 - ASHE 6115 will increase at the rate of 1.5% per annum above the RPI;
 - Future care makes up 45% of the value of each substantial award;
 - The RPI will increase at the rate of 2.5% per annum into the future (the annual RPI inflation rate to July was double this, at 5.0%);
 - 75% of all substantial cases will involve periodical payments.
- Interestingly, expert evidence given by the Defendants' actuary during the indexation litigation, a partner in the same firm acting for the NHSLA, also placed a value of £1.5 billion on the impact of linking periodical payments to ASHE 6115. However, his figure was arrived at using a different set of assumptions. One interpretation of this could be that the evidence presented to the courts was overly pessimistic.

The 2008 Report and Accounts seem to me to give a clear indication that the NHSLA expects that the vast majority of cases will include periodical payments. It is our experience that this is likely to be a self-fulfilling prophecy, in that the NHSLA will frequently only offer terms including periodical payments and will rarely offer terms on a conventional lump sum alone.

Finally, on the pertinent issue of security (of PPO's), the Report includes the following comment:

“The global valuation recorded in the balance sheet recognises provisions that will crystallize in future years and will be funded by future contribution payments or departmental funding. This future income is calculated to fund annual outgoings, and in the case of the departmental funding is subject to parliamentary control.

There is no reason to believe that this future funding, future parliamentary authority, and the contribution payments from members will not be forthcoming. It has therefore been considered appropriate to adopt a going concern basis for the preparation of these accounts. In addition, the NHS (Residual Liabilities) Act 1996 requires the Secretary of State to exercise his statutory powers to deal with the reported liabilities of this Special Health Authority if it ceases to exist.”

The protective legislation referred to in Section 1 of that Act was repealed by section 6 of, and Schedule 4 to, the National Health Service (Consequential Provisions) Act 2006 on 1st March 2007. The successor provision, which came into force on 1st March 2007, is section 70 of The National Health Service Act 2006.

Although broadly similar, the new provision includes a power to transfer the liabilities of an NHS body to a Foundation Trust. As such an organisation may become insolvent, continued vigilance is necessary when drafting the PPO to ensure it is as secure as possible. In claims falling under the CNST, which are funded by its members, an appropriate protocol already exists, following the cases of *YM* and *Kanu*. As yet, there is no such protocol for claims falling under the centrally-funded ELS or ex-RHA schemes.

Ian Gunn

The contents of this document are © Personal Financial Planning Limited 2008 and all rights are reserved. No liability is accepted by PFP Limited or by any of the authors of the contents for any loss or damage caused to any person relying on any statement or omission in this briefing. You should seek case specific independent legal and financial advice if it is of sufficient importance for you to do so.