

# Regulatory Impact Statement

## Allocation of Legal Costs between Parties

### Agency Disclosure Statement

This Regulatory Impact Statement has been prepared by the Ministry of Justice.

It provides an analysis of options to update the “daily recovery rates” and “time allocations” which are used by judges to determine the allocation of legal costs between parties at the end of civil court proceedings.

The analysis relies on suggested new time allocations provided by the Rules Committee. However the Committee is an expert body established under statute for the purpose of determining rules of court procedure.

The analysis also relies on increases in the cost of personal and corporate legal services, as measured by the producers price index (PPI), which is derived from a representative sample of legal services providers. The PPI is the most accurate way to measure changes in the cost of legal services. This is because there is no other readily available information or methodologies to measure the cost of legal services.

The preferred policy option is likely to impose a minor increase in costs on individuals and businesses that are involved in litigation and are ordered to pay costs to another party. However, this will benefit the party who receives the cost payment. The policy options are not likely to:

- impair private property rights, market competition, or the incentives on businesses to innovate and invest, or
- override fundamental common law principles (as referenced in Chapter 3 of the Legislation Advisory Committee Guidelines).



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## Status quo and problem definition

1. This statement relates to a proposal to ensure the equitable allocation of legal costs between parties to civil cases in the District Courts and the High Court.
2. Civil cases include disputes between individuals, companies and sometimes local or central government. Disputes may relate to matters such as a breached contract, a debt, a company going into liquidation or bankruptcy, insurance claims, disputes between neighbours, or harassment. There were about 4200 civil cases disposed of in the High Court and about 11,900 civil claims made in the District Courts that potentially resulted in cost orders for the year ending 30 June 2011.
3. Legal costs to be paid by one party to another as part of a court case are determined by a judge (unless agreed between the parties). The judge has discretion when making a costs order, and will consider a set of principles which include:
  - the unsuccessful party should pay the successful party's costs
  - the amount awarded should reflect the complexity and significance of the matter
  - the amount of the costs should be assessed by applying the appropriate "daily recovery rate" to the time considered reasonable for each step required in the matter (the "time allocations")
  - costs should be approximately two-thirds of the daily recovery rate
  - the appropriate daily rate and what is a reasonable time does not depend on the particular lawyer's skill, nor the time actually spent
  - the award should not exceed the actual costs incurred by a party, and
  - the determination of the costs should be predictable and expeditious.
4. This system helps ensure consistency between cases and provide certainty for parties about the likely costs of a case.
5. Time allocations refer to the time it should reasonably take for a lawyer to complete different steps in a proceeding, depending on the level of complexity of the proceeding. The following table contains two examples:

Example	Straightforward proceeding	Average proceeding	Complex proceeding
Commencement of proceeding by plaintiff	1.6 days	3 days	10 days
Commencement of defence by defendant	1 day	2 days	3 days

6. The High Court daily recovery rates are \$1070 per day for straightforward proceedings, \$1600 per day for proceedings of average complexity, and \$2370 for complex proceedings. The District Courts rates are set at 80 percent of the High Court rates.

7. The time allocation and daily recovery rate system has been in place since 1 January 2000. The rates were subsequently increased on 1 January 2004, 1 June 2006, and 24 May 2010. When these adjustments were made, the rates were increased by the movement in personal and corporate legal services in the producers price index (PPI), rounded to the nearest \$10.

#### *The problem*

8. The cost of legal services has increased, and so it is likely that costs awards using the current rates are becoming more disproportionate to actual costs. The PPI shows an increase in the cost of personal and corporate legal services of 5.84 percent since the last daily recovery rates adjustment. While the increase is relatively minor, a small adjustment provides assurance to parties to civil proceedings, lawyers and judges that the rates are being reviewed regularly to ensure they remain current.
9. There have also been some changes to court rules since the time allocations were last adjusted, which means the time allocations do not reflect changes in how much time it takes to complete a task. The time allocations should be adjusted to reflect these changes.

#### *Costs and benefits of the status quo*

10. Retaining daily recovery rates at the current level while legal expenses continue to increase means successful parties are likely to recover a smaller proportion of their actual legal expenses. If the rates remain at current levels for a long period, the rates are likely to become more disproportionate to actual legal costs. This would disadvantage successful parties and, as a result, public confidence in the court system could decline.
11. If the status quo remains, it is possible that successful parties will increasingly ask the court to order that they are paid higher costs than provided for by the standard rates, to better reflect their actual costs. This may create uncertainty for parties, require additional court time to resolve costs issues, and may cause delays. If the rates are not adjusted, these risks will increase over time as legal costs rise, and may result in a decline in confidence in the costs award process.
12. In some cases, rates that are lower than actual reasonable costs may provide a stronger incentive for parties to settle out of court. Early settlement will be an advantage in some cases, but may also deny some people full access to justice if they settle for less than they are entitled to because they are concerned about not being able to recover enough of the cost of litigation.

#### **Objectives**

13. The mechanisms for awarding costs in civil proceedings should:
  - be transparent and predictable to provide certainty to parties and consistency between cases
  - ensure that the amount of money the unsuccessful party pays to the successful party is reasonable and appropriate to the nature of the proceedings

- encourage the efficient use of judges' time, court resources, lawyers' and clients' funds, and
- be reviewed when necessary to ensure they more accurately reflect the actual reasonable cost of proceedings.

### **Regulatory impact analysis**

14. The options that have been identified for adjusting court costs are:

- 1) increasing the daily recovery rates (preferred option),
- 2) maintaining the status quo, and
- 3) removing the daily recovery rates and time allocations from court rules.

#### **Option 1 (preferred option): Increase the daily recovery rate and adjust time allocations**

15. The current system for awarding costs, where the judge exercises discretion in making costs orders guided by the daily recovery rates and time allocations, meets the objectives of transparency and predictability and efficient use of court time. However, the integrity of the current process depends on realistic daily recovery rates and accurate time allocations.
16. Although court rules do not specify how often the daily recovery rates should be reviewed, a regular review is appropriate to ensure the rates are up-to-date.
17. Minor adjustments to time allocations will make calculations of the actual time required to undertake particular tasks more accurate. This will benefit parties who will be subject to fairer costs awards.
18. The PPI measures the change in price of a fixed basket of goods and services for the productive sector between two time periods. The PPI also individually measures the change in prices received by personal and corporate legal services providers. Statistics New Zealand publishes PPI statistics every quarter. The daily recovery rates were last adjusted using PPI (personal and corporate legal services) statistics to the March 2009 quarter.
19. This option would increase the daily recovery rates by 5.84 percent, based on the increase in the cost of personal and corporate legal services between the March 2009 quarter and the latest quarter (December 2011). The figures would be rounded to the nearest \$10, as was done last time the rates were adjusted.
20. The PPI is the most accurate way to measure changes in the cost of legal services. This is because there is no other readily available information or methodologies to measure the cost of legal services.

#### **Option 2: Maintaining the status quo**

21. This option is not preferred because it will not address the problem. As discussed in paragraphs 9 to 11 above, if the status quo remains:
  - successful parties are likely to recover a smaller proportion of their actual legal expenses

- rates are likely to become more disproportionate to actual legal costs
- public confidence in the court system could decline
- parties may make more attempts to obtain increased costs awards, which could create uncertainty, require additional court time, and cause delays, and
- some people could be denied full access to justice if they resolve their dispute out of court because they are concerned about not being able to recover enough of the cost of litigation.

### **Option 3: Removing the daily recovery rates and time allocations from court rules**

22. Removing the daily recovery rates from court rules would leave it up to judges to decide what costs were reasonable. This is likely to lengthen court cases and increase legal costs for parties as judges would be required to hear submissions about the reasonable amount of costs in each case. Deregulating may also lead to uncertainty for parties, which could be a barrier to litigation.
23. Without regulation, judges are likely to develop their own systems for determining a reasonable level of costs. The disadvantages of an ad hoc system include:
  - disparity between individual judges and individual cost awards
  - undue cost rewards for inefficient practitioners
  - unpredictability for settlement and planning purposes, and
  - lack of any incentive to work within known budgets.

### **Consultation**

24. The Rules Committee released a consultation paper on its website. Feedback was received from four submitters (the New Zealand Law Society, New Zealand Bar Association, and two law firms).
25. The Bar Association and two law firms did not comment on the daily recovery rates, but made some suggestions about time allocations. Following consideration of submitters' views, the Rules Committee amended the time allocations to reflect the comments received.

### **Conclusions and recommendations**

26. There is no reason to remove time allocations and daily recovery rates as the current system for determining costs in civil proceedings. The current system provides greater certainty for parties and consistency between cases. The introduction of the current system followed an extensive period of consultation with legal practitioners and other organisations.
27. There is evidence that legal fees have increased. There is no advantage in deferring an increase in the daily recovery rates because it will result in a greater increase later on and create more of a burden for parties.

## **Implementation**

28. Under section 51C of the Judicature Act 1908 and section 122 of the District Courts Act 1947, court rules are made by the Governor-General in Council, with the concurrence of the Chief Justice and two or more of the members of the Rules Committee.
29. The proposed rules include transitional provisions which provide that the updated rates will apply to any proceeding begun after the new rules come into effect. For proceedings underway when the new rules commence, steps that occurred before the commencement date will be determined at the old rate, and steps that occur after the commencement date will occur at the new rate. The amendment rules do not affect other legislation.
30. There are no significant implementation risks. There is a small risk that some lawyers may use the increase as a justification for increasing their fees, but lawyers' fees are not regulated and they are free to increase their fees when they choose. Lawyers will need to identify which steps occurred before the new rules took effect and which occurred after. No implementation problems were reported following the previous adjustments to the daily recovery rates.

## **Monitoring, evaluation and review**

31. Time allocations and daily recovery rates will continue to be periodically reviewed by the Rules Committee and the Ministry of Justice.