

## Legal expense insurance: an experiment in access to justice

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<http://lawfoundation.net.au/report/lei>

Records and evaluates the attempt by the Law Foundation to establish one of the first legal expenses insurance schemes in Australia.

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### Key findings

#### Definitions

- **Group plans** finance legal services for consumers in four ways - the bulk purchase of legal services, the employment of in-house lawyers, the education of members, and the application of insurance principles. The last of these, legal expense insurance, is different in type from the first three. The first three are "prepaid" plans, and do not use insurance principles. They rely on bulk savings to create benefits for policy holders, and are found predominantly in the USA. Prepaid plans in the USA have developed mainly to improve people's access to justice, ie. to reduce the cost of legal advice and representation. They are almost exclusively found in the context of group employee plans, either totally employer-funded, or jointly funded by employers and employees.
- **Legal expense insurance** is a means of financing unpredictable legal costs by spreading the risk of liability among subscribers to a scheme, thereby reducing the cost to each. Legal expense insurance has its origins in Europe, where it is operated predominantly by private businesses for profit. Policies tend to provide cover for unforeseeable legal events. Policies are mainly sold on an individual or add-on basis, but may also be sold to a group.

#### The debate in Australia

- People in the 'middle income' sector of the population - those who do not qualify for legal aid but who cannot usually afford private legal services - have become a focus of concern over access to justice in Australia.
- The Australian Senate's *Cost of Justice Inquiry (1992)*, the *Access to Justice Advisory Committee's Report (1994)* and the Law Council of Australia have raised for discussion the potential of legal expense insurance to increase access to affordable legal services.

#### Operation of Legal Expense Insurance Ltd (LEI)

- The Law Foundation of NSW and the GIO in NSW established Legal Expense Insurance Ltd (LEI) as a project to improve the community's access to legal assistance by providing a commercially viable legal expense insurance product. The LEI project ran from 1987 to 1995.

#### Policies

- Initially, policies were designed for purchase by low to middle income families. Later, specialised policies were developed for groups of workers with specific unmet legal needs, eg. child care workers.
- It was difficult for LEI to design legal expense insurance benefits and premium levels in the absence of fixed fee schedules or predictable litigation costs.
- The indemnity aspect of LEI's policy covered policy holders for a specified range of unforeseeable legal costs. Policies were narrowly designed, and did not trigger many claims.
- LEI chose a closed panel to service the indemnity aspects of its legal expense insurance policies. If high quality lawyers are retained, closed panels are generally significantly cheaper than open panels, and may therefore be a more effective and reasonable method of enhancing access to justice for low to middle income earners.

#### Non-insurance benefits

- LEI's telephone advisory service provided advice and limited document review for all routine legal matters. In-house lawyers provided the telephone advisory service.
- The telephone advisory service was not cost effective to operate in itself, although it may have had a preventative effect in terms of claims lodged, and consequent cost benefit to the company.
- LEI's telephone advisory service and educational efforts were popular with consumers and, in terms of access to justice, were arguably the most worthwhile achievements of LEI.

#### The market

- LEI sold legal expense insurance primarily on a group basis. This reduced the potential for adverse selection, made the task of administering and marketing the scheme easier, and allowed LEI to tailor plans to the specific needs of group policy holders.
- LEI determined that one of its major target purchasers would be employees, and hoped that unions would play a central role in promoting legal expense insurance as an employee fringe benefit. Trade unions and employer groups were, however, reluctant to accept legal expense insurance as a means of providing legal services for their members/employees.

- Legal expense insurance was also sold by LEI as a policy add-on. These sales provided much needed cash flow during the slow development of group sales. Benefits under the add-on policy were limited.
- LEI developed cheaper, stand alone policies with more limited benefits as difficulties with group sales emerged.
- Despite marketing difficulties, group sales seem to have been the optimal method of attempting to sell legal expense insurance to low to middle income earners.

### **Barriers to sales**

- Convincing potential consumers of the benefits of legal expense insurance was a major challenge for LEI, which marketed policies through brokers, agents and LEI staff.
- Potential consumers largely failed to perceive the benefits of purchasing legal expense insurance. Brokers and agents lacked familiarity with the product and did not promote it strongly.
- The public's perception of the general availability of legal aid resulted in there being reduced interest in LEI.
- It was difficult to sell legal expense insurance to employers as an employee benefit in tight economic times and in the absence of any financial incentive.

### **Operational issues**

- The decision to establish a separate corporate entity was costly, but ultimately did not determine LEI's lack of commercial success.
- The attention and commitment provided by a separate, specialist corporate entity is an advantage, but is not essential, to the development and sale of legal expense insurance.
- Adding the product to the product range of an established insurer in the market would have reduced LEI's costs.
- LEI managed to stay afloat financially in the short term because it developed legal expense policies for specialist markets. While this provided worthwhile protection to these groups, it was a different aim from that of enhancing access to justice generally for low to middle income earners.
- The absence of a third commercial partner limited LEI's ability to withstand initial cash flow problems. A union partner may have assisted LEI to break through to the employee benefit market.

### **Conclusions**

- If legal expense insurance is to enhance access to justice for low-to-middle income earners, it must be able to provide a broad, general coverage at an affordable cost, and remain commercially viable.
- Commercially viability for legal expense insurance requires
- selling large numbers of policies so as to achieve significant bulk savings and risk spreading, and
- a high claims ratio which allows benefits to flow through to policy holders.
- Community attitudes and market practices in Australia are not conducive to achieving the necessary sales volume for legal expense insurance.
- The Australian legal system - adversarial, without scheduled fees, and with the availability of costs orders - is not conducive to offering the level of affordable legal expense insurance benefits which would result in a high claims ratio.
- Legal expense insurance and prepaid plans have some potential to reduce the cost of legal services in Australia, and to reduce non-financial barriers to the timely and cost-effective use of lawyers. Conditions in Australia are not, however, directly comparable to Europe and the USA, and the barriers that exist would need to be addressed as a matter of government policy if private insurance products are going to meet the legal needs of low-to-middle income earners.

### **Proposed policy responses**

- Reduce the cost of legal expense insurance policies by
- recognising them as tax deductible expenses for an individual,
- exempting them from fringe benefits tax as an employee benefit, and
- reducing or removing stamp duty.
- Governments should take a role in advocating generally for legal expense insurance as a prudent step for individuals and groups to take.
- To complement promotion of legal expense insurance, educate insurance brokers and agents on legal expense insurance as a product.
- As employers of large numbers of people, governments should support the expansion of legal expense insurance by introducing such schemes through enterprise bargaining. The PSA/CPSU legal expense scheme in South Australia is an example of the way in which government support can promote legal expense insurance schemes.
- The Federal Government's previously proposed Legal Expense Insurance Taskforce would provide an opportunity for a large scale evaluation of legal expense insurance's potential to enhance access to justice in Australia, and an opportunity to consider seriously the role of government in this area.