

Managing the Business of Recovery Litigation

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Introduction

In the continuous search for improvements to the bottom line, insurers are increasingly turning to the recovery area, seeking to maximize the recoupment of monies paid out on first-party losses. Traditionally, subrogation and recovery work was considered an afterthought, to be undertaken when and if the claims department decided a case was strong enough to warrant the pursuing of recovery claims. Unfortunately, too often good recovery chances were lost through the passage of time, the failure to investigate properly or at all, or just straight organizational inertia.

Generally speaking, the traditional approach is no longer acceptable to most insurers. With every first-party loss comes a potential opportunity to shift the loss to some other responsible parties, an opportunity that must be properly evaluated and pursued. The role of specialised counsel in assisting with these efforts is becoming more appreciated as time progresses.

I propose to exam a number of issues relating to the conduct of recovery actions in Canada. My remarks are not directed at the many smaller claims where a more administrative process, not involving the time and trouble inherent in legal assistance, is appropriate. Rather, we are here contemplating cases with sufficient money at stake that a more comprehensive effort to pursue recovery is warranted. In our firm, we use the benchmark of \$100,000 as being the rule-of-thumb dividing these categories of cases. The point being examined is how insurers can go about obtaining the best results in the most cost-efficient fashion.

Investigation and Early Intervention

It is not possible to develop a comprehensive checklist that details all the activities or procedures that need to be performed when investigating a loss, be it fire or building collapse, etc. Common sense and experience will usually suggest procedures that are generally desirable to

follow during the investigation of any loss. There may also be procedures specifically applicable to various kinds of property losses, including fires, building collapses and “acts of God”.

The reality is that the appropriate procedure to follow in any particular loss will always vary depending on the circumstances. As well, the extent of property damage suffered by the insured, the number of potential recovery targets which are identified as the investigation progresses, the potential for an ongoing criminal or quasi-criminal regulatory investigations, the extent of various potential hazards at the site, the urgency of commencing site restoration activities, and countless other factors will all influence the format the investigation takes.

Given that there is no uniform investigation checklist to be used in all losses, the people investigating and supervising the investigation of a loss must rely heavily upon their experience and common sense. It is safe to say, however, that it is not possible to be sure an adequate, complete, investigation is being performed, unless one is able to:

- (a) recognize the potential liability theories;
- (b) build the right team of experts and direct it appropriately; and
- (c) identify the evidence that must be preserved and determine how that should safely be done.

The legal theories pertinent to each of these three major considerations are continually evolving and an experienced legal counsel will be able to guide the insurer through this potential minefield. Each of these three points is addressed below, with some practical, everyday, examples given to help highlight the issues.

Recognizing all Potential Liability Theories

When conducting property loss investigations, the logical first step is to determine the relevant facts and then determine possible targets for recovery. This requires the insurer’s representatives to get to the scene and begin investigation as soon as possible and to communicate with legal counsel to determine what factual inquiries are truly important. This is because it is not always possible at the outset of an investigation to determine which facts are important unless there is an appreciation of the potential liability theories. If those in charge of conducting the investigation are not aware of all the potential liability theories, vital evidence

and potential recovery opportunities may be lost forever early in the investigation. It is always important to bear in mind that there can be more than one cause of a loss and early, proper investigation is necessary to identify the various potential causes.

The following are some types of losses and examples of how investigation efforts should be focused:

1. In fire losses, even where the cause and origin of the fire cannot be conclusively determined, or there is no responsible party with a “deep pocket”, or the fire was started by the insured, there may be avenues of recovery that can be identified with proper investigation. For example:
 - (a) There may have been delay in detecting the fire because of a defective fire alarm
 - (b) The fire may have been permitted to spread because of an improperly designed or malfunctioning fire prevention and/or fire suppression system(s).
 - (i) A severe fire in a sprinklered structure or in an installation equipped with automatic fire suppression systems, is a situation calling for detailed inquiry.
 - (ii) A fire in a large structure such as a warehouse or factory is also a situation calling for detailed inquiry, as often large structures will have to meet National Building Code and National Fire Code design requirements intended to lessen potential fire damage. Such requirements are the installation of firewalls and the use of building materials designed to be fire resistant.
 - (iii) The occupant of the building, if different than the insured, may be a target, as their activities may have contributed to the cause or spread of the fire. For example, the occupant may improperly store its stock or delay notifying the fire department.
2. In “Act of God” losses, appropriate investigation can often reveal potential recovery targets that were not, on first review, identified.
 - (a) In the case of a roof collapse due to excessive snow load, consider whether the mass of the snow exceeded the Building Code design standards. Often, Building Codes require portions of a roof’s supporting structure where drifting can be expected to occur, to be specially constructed. The fact that a roof collapsed on an insured’s building, but not on buildings in

the same area, is a signal that design and/or construction could have been improper.

- (b) Where high winds cause damage to buildings, it is important to determine if similar damage was caused in the vicinity of the loss. If not, there may have been design or construction problems that caused the building to not meet Building Code requirements. It is also desirable to determine, if possible, actual wind speed at the loss site at the loss time; Environment Canada data, while convenient to obtain, is often of limited use as wind speed can vary over short distances.
- (c) In the case of plumbing freezes, something usually has gone wrong somewhere, often because of somebody else's negligence. A furnace may have malfunctioned, the heat may have been turned down, a window could have been left open, a pipe may not have been adequately insulated, or an unprotected pipe may have been inadvertently left filled with water.

One crucial step in the investigation of losses, particularly the type described above, is choosing the right experts to help investigate and identify theories of liability.

Building the Right Team of Experts:

Identifying the proper expert to retain is an important first step in any investigation. Usually, common sense determines which type of experts are appropriate for particular losses. The crucial consideration is to ensure the need for each type of expert is identified early enough so the expert can be of maximum assistance. This is not as easy as some assume: many of the expert companies that work for the insurance industry purport to be expert in all matters and will not readily admit that the case should be referred elsewhere. Also, there are some experts who will undertake a broad-based investigation, when a narrower, more focused effort is called for, because of a desire for billings, confused thinking, lack of real expertise in the relevant area, or all of the above. An insurer can benefit significantly from having a lawyer experienced in putting together and presenting recovery claims, do the work to select, brief and control the expert team.

Early successful intervention usually requires that an expert must be retained immediately following a loss so that they can get on site as soon after the loss as possible, before any crucial evidence is lost or altered. The following are two examples of the need to have the expert attend the loss site as fast as possible:

1. In fire loss cases, often the first expert to be chosen is a cause-and-origin expert who can determine the cause of the fire. However, in cases where the cause-and-origin expert may identify the insured as the cause of the fire, it may become necessary to retain an engineer who can determine whether the building and its fire suppression systems complied with the applicable Fire Code and Building Code provisions. It is very important that this engineer be able to inspect these systems and the remnants of the building before clean-up occurs, so that they can see the systems in as close to their pre-fire state as possible.
2. In “Act of God” cases it is important that the expert be retained as soon as possible so that they can examine the loss before remediation begun. In snow-collapse cases, the expert will need to get on site quickly to determine the snow load at the time of the collapse, as well as to see the building components in their collapsed state, before site remediation begins.

General Tips for Retaining Experts

There is no generally applicable checklist for choosing and retaining experts but the following tips should be kept in mind when retaining an expert, regardless of the type of loss:

1. Stay away from “generalist” or “jack-of-all-trade” experts who claim to be experts in everything. Expert witnesses who spread their expertise across many areas are susceptible to attack by a competent defence counsel. There is also a greater possibility that such an expert can overlook a crucial piece of evidence during their investigation, than a more-focused expert who is a true specialist.
2. Experts with strong credentials in their field, but who do not appreciate the limits of their own abilities and want to do it all for you, should be avoided. Many fire loss cases require the services of a qualified cause-and-origin investigator. Often, these investigators are relied on to conduct a preliminary investigation during which the need for other experts is identified. For example, the determination of a fire’s cause and origin can require the elimination of alternative causes, such as electrical failure. Eliminating these causes may fall beyond the expert’s abilities.
3. “Full service” consulting firms should be used with some caution. These firms often have qualified personnel on staff, but this does not mean that every expert at the firm is the particular expert you want to work on a particular loss. The benefits of individually selecting the most appropriate experts outweigh the efficiency of using multiple experts from the same firm, if some of those experts are not appropriate for the task at hand. One wrong step in an expert’s analysis can be disastrous for a case.

When the right team of experts has been put in place and has conducted their investigation, the next step is to obtain a report, but the timing for this must also be kept in mind.

When to Obtain an Expert Report

Consider carefully whether and when an expert should issue a written report, and for what purpose. Assuming that the expert is providing adequate oral updates either directly, or through legal counsel, on the state of their investigation and analysis, writing a report before completion of discovery may not be necessary and could be potentially dangerous. Often, only after examinations for discovery are complete can one be sure that there is a proper and full factual background for an expert to issue an opinion. It is not that the facts will change, but there may simply not be adequate access to all the important facts, particularly those known only to the defendant, until after discovery has been conducted. In the Ontario litigation process, an expert report often does not need to be served on a defendant until 90 days before trial is to start.

Another problem with having an expert report prepared prior to the commencement of litigation, is that courts can take a liberal view regarding the discoverability of expert's reports and the scientific work underlying them. Addressing the reports to counsel can assist in protecting reports from production through privilege; however, there is no guarantee that the defendant will never see the report, if it is unfavourable and, if the expert is produced as a witness at trial, report will likely be the subject of inquiry. At trial, the court may order the expert's entire file, including his notes, to be produced. It is prudent to assume that any written reports prepared by an expert will eventually fall into the hands of an opposing party.

Some experts like to issue preliminary reports based upon their first impression of the circumstances of a loss. Often these reports are not necessary and can be dangerous to a case as they are usually based on an incomplete or inaccurate understanding of the important facts. Such reports can damage the expert's credibility and opinion, as a competent defence counsel will attack the expert as pre-judging the circumstances of the loss and tailoring their investigation to lead to a pre-determined conclusion. At the very least, the expert will have to justify any changes in view between the preliminary and final reports.

Another potential problem is an expert report which focuses exclusively on pinning responsibility on a party with no assets or insurance coverage or which is protected by a

limitation of liability or waiver of subrogation in a commercial contract or lease. These reports can significantly harm recovery efforts against defendants with “deep pockets”. It may be that these reports are better left un-written so that the expert can focus on other parties.

Identifying the Evidence Which Must Be Preserved and How to Preserve It

Identifying and gathering important evidence can be a time-consuming and, at times, mundane task. It is, however, a vital part of a successful recovery effort. Like determining which steps to take when investigating a loss, experience and common sense will be important elements that guide the recovery team. The following factors are generally applicable to gathering evidence after a loss although there is, again, no standard checklist:

1. Whenever possible, loss sites should be thoroughly photographed. Videotaping, when possible, can also be extremely helpful.
2. A surprising number of fires and disasters are videotaped while in progress. It is not uncommon for news media, bystanders, curious neighbours or freelance photographers/videographers who are nearby to take interest and bring their camera, so asking people on site for any pictures or video they have is worthwhile.
3. Critical dimensions should be diagrammed in cases involving structural damage. This is because the dimensions of a structure may lead to specific Building Code requirements.
4. Identifying and interviewing all potentially important witnesses and taking witness statements while the witnesses are available, willing to talk and their memories are still fresh is very important. Interviewing witnesses can help put the events in context as well as give a good idea of whether their evidence is capable of belief and will be accepted by a court. Taking written or recorded statements is also helpful as litigation can occur many years after a loss occurs and witnesses may rely on their statement taken at the time of the loss to refresh their memory at trial.
5. Gather as many important documents from the insured or other interested people and entities as soon as possible. Occasionally, potentially important information, such as recordings of “911” calls and burglar and fire alarm records, can help establish good timelines of when important events occurred. In the events of fires and building collapses, municipalities may have important designs and drawings in their records relating to the approval of building permit applications. Sometimes, it can take a while to go through the Freedom of Information request process.

6. The light fixture, toaster, or other device that is alleged to have caused the fire could well have been purchased and installed on the premises at the same time as one or more essentially identical devices that may have been manufactured at the same time as the device in issue. Examining undamaged exemplars is of invaluable assistance in identifying the failure mode in the accused product, and will assist in levelling the playing field against a product manufacturer who is going to be intimately familiar with that product. Exemplars of the same model and vintage as the accused product are often hard to come by, if they are not available at the loss site.

The Spoliation Defence

In many instances, an expert investigates a loss scene, takes pictures of whatever the expert deems must be photographed, and saves whatever physical evidence the expert thinks should be saved. The expert may then conduct whatever destructive testing they feel is necessary to verify their theory and then wrap up their investigation. At some later point, usually after the loss site has been cleaned up and rebuilt, the subrogation action commences. At that time, the defendant retains an expert but, because the loss site is no longer available, the defence expert can only rely on the plaintiff's expert's photographs and any physical evidence that was preserved during the investigation of the loss, to develop an opinion that contradicts the plaintiff's expert's theory. The defence expert (and defence counsel) might also challenge the adequacy of the plaintiff's expert's investigation and analysis, and might also challenge the adequacy of the evidence supporting the plaintiff's expert's theory.

There is an increasing trend in Canadian recovery litigation for defendant's to raise evidence-spoliation arguments. The basis for the argument is that there should be a "level" playing field, as far as the gathering, documentation and preservation of evidence is concerned. Typically, a defendant's counsel will argue that because a defendant was not permitted to examine the site after the loss occurred and that it was not given an opportunity to test its product or work, the plaintiff should not be allowed to lead its evidence. While it is clear that there is no independent tort of spoliation of evidence, this area of law is still evolving in Canada; the likely consequence of spoliation is trial judge-imposed limitations on what evidence and opinion can be lead at trial to support the plaintiff's case. In the United States, there are many cases where the plaintiff's case was dismissed for spoliation of evidence.

The best way to avoid evidence spoliation arguments is to let potentially adverse parties examine the loss site before it has been disturbed, under the insurer's supervision. The potentially adverse party can be put under whatever constraints may be necessary in the circumstances. That way, the potentially adverse party's representative(s) can examine and document whatever evidence it wishes. They can also ask to have preserved any physical evidence that they wish. This will tend to preclude a potential defendant from later complaining about something being unavailable, because they had the opportunity to examine it for themselves.

The downside to this approach is that it can slow the investigation and make it more costly, especially in an investigation where potentially responsible adverse parties are identified as the investigation progresses. When the benefit of these extra costs are weighed against the detriment - a possible failed recovery action because of evidence spoliation - it seems clear that the extra expense is worthwhile.

Often times, the site of fire or other property losses cannot be maintained in an undisturbed setting for very long. The insured will often wish to have their business or home restored as soon as possible, so that they can resume business or rebuild their life. This is often in conflict with the subrogating insurer's need to take careful steps to conduct a proper investigation and prevent evidence spoliation.

Most courts should be sympathetic to these real-world concerns, so long as some effort and consideration to the opposing parties' points of view has been made. It is hard to imagine a court expecting a policy-holder to delay restoration efforts to keep a site available for inspection, assuming that an appropriate effort has been made to identify and notify potentially responsible parties and give them a fair chance to inspect the site.

Dealing with Insured and Uninsured Losses

There is an increasing trend in the insurance industry for large corporations to have complex insurance schemes. It is not uncommon to see large self-insured retentions and multiple layers of coverage. Many large companies are becoming more comfortable with insuring themselves for very large amounts. In cases where there is a large self-insured retention or

losses which, for business or other reasons, the insured decided it was comfortable not insuring itself against, the insured may attempt recovery of its own losses. In these situations, the insurer must proceed carefully with its recovery efforts. In situations involving losses not caused by fire, the insured will likely have the right to be made whole, before the insurer has any right to the recovery proceeds. In these situations, the aggressive insurer will be at risk of going to significant expense and effort, but not bearing any fruits of recovery. The following are examples of some of the problems that can arise when there are uninsured losses:

1. The insured will usually make getting back in business its primary goal following a loss. This means quickly cleaning up the loss site and starting the necessary rebuilding as soon as possible. The insured may not be concerned or equipped to fully investigate the cause of a loss. This goal is at odds with the insurer's obligation to investigate the circumstances of a loss and to be as thorough and careful as possible when doing so, in order to maximize recovery possibilities. The insurer will also be under pressure to get the insured back in business to minimize indemnity, further complicating matters.
2. In situations where the insured is not made whole, it will usually have the right to drive the recovery investigation and litigation. In these circumstances, if the insured is not equipped with the knowledge or resources to conduct a proper and full investigation, avenues of recovery can go undiscovered, leaving potential sources of recovery untapped and increasing the possibility that the insurer will not be able to recover its losses.
3. In situations where there is a substantial uninsured loss, the insurer is in an even worse position because it might go to great effort and expense to fully investigate the loss and drive recovery efforts, but because the insured must be "made whole" before the insurer can recover, the insurer runs the risk that only the insured will benefit from the insurer's recovery effort and expense. This can occur in situations where the most responsible third party does not have adequate insurance coverage or is insolvent, such that its pockets are not sufficiently "deep" to cover both the insured and uninsured losses. In those situations, the insured will recover first, leaving the insurer in the position of going to great expense for little, if any, recovery.
4. The insured may seek to inflate its uninsured losses as much as possible, which can make settlement with defendants more difficult. Further, if the responsible parties do not have sufficient insurance coverage to pay both the insured and uninsured losses, the inflated uninsured loss will likely reduce the insurer's recovery.
5. The insurer has to sue any responsible third-parties in the name of the insured, it cannot commence its own separate lawsuit. As a result, it is virtually impossible for the insurer and insured to commence separate lawsuits against the same third-

parties. Instead, they must work together to conduct the litigation. This can be difficult when a defendant makes an offer to settle which is suitable to the insured, but not the insurer. If the insured is not made whole, it may have the right to settle the litigation, leaving the insurer with little recourse to recover its losses.

Pro Rata Agreements

In situations where there are uninsured losses, a useful tool to protect the insurer's ability to recover is a pro-rata agreement. Under a pro-rata agreement, the insurer and insured agree to share in recovery from the first dollar based upon an agreed percentage. Normally, but not always, the percentage corresponds to the provable, recoverable damages claimed by each party. Expenses incurred in pursuing the joint claim can be allocated according to the same percentages, subject to any costs recovery at the end. In many cases, however, the insurer will bear the expenses during the course of the case, and obtain reimbursement of the insured's share of expenses out of the insured's share of the recovery at the end of the case. In other cases, the insurer will agree to bear all the expenses in return for the insured entering into the pro-rata agreement.

Both parties will benefit from a fair pro-rata agreement. The insurer avoids the potential that the insured will have to be made whole, which will reduce or eliminate the insurer's recovery. The insured benefits too, because it will often not have the resources or expertise to properly investigate a loss and make efforts to recover its loss. Because the insured has a definite stake in the litigation, the insured has more incentive to cooperate actively in the subrogation case, which can drag on for years after the insured's 1st-party claim has been paid.

There is no standard pro-rata agreement that covers all situations, but, generally speaking, the following principles should be kept in mind when negotiating a pro-rata agreement.

1. A pro-rata agreement should have a mathematical formula that details how any recoveries will be allocated between the insurer and insured. A key to arriving at this formula is to accurately determine each party's losses. This will have an added benefit of crystallizing the actual value of the uninsured losses, such that the insured cannot inflate them.
2. The key to negotiating a fair pro-rata agreement is to verify what the actual "uninsured" losses are. This means that, even when a loss clearly exceeds policy

limits or sub-limits, the adjuster should nevertheless establish the total amount of the losses sustained for each element of the insured's claim, both on an actual cash value and replacement cost basis.

3. The power to settle any litigation must be clearly outlined in the pro-rata agreement.
4. The insurer should ensure that the insured waives any right it may have to first recovery in exchange for the fruits of the insurer's investigation. This is often the major reason an insured is willing to enter into a pro-rata agreement, as it may not have the resources, knowledge or desire to conduct proper investigation itself.
5. Clearly outline the degree to which any party will be responsible for the expenses of the recovery efforts.

When a pro-rata agreement has been finalized, the parties are free to put their resources into their mutual goal of recovery. At this stage of the game, the goal will be moving the case ahead as efficiently as possible to a conclusion which maximizes the cost/benefit ratio.

Developing the Damages

An essential component to being paid sooner rather than later is a presentation of the damages claim. Too often, the claim outline and substantiation that results from the settlement of the first-party loss, governs the recovery action, at least in its early stages. This is a mistake: the liability targets or their insurers will not be interested in dealing with the claim until the quantum of it has been properly put together and presented. In this jurisdiction, most first-party losses are settled on a replacement-cost basis. Because of the first-party relationship, estimates and rounded numbers are often used. Claims are negotiated without proper substantiation from time to time. All of these factors are significant difficulties for the prosecution of the recovery action, since the target defendants will not accept this manner of quantifying the claims against them.

Further, Canadian law is that the measure of quantum of loss for purposes of a first-party insurance claim is not necessarily the same as the measure of damages in a tort or breach of contract action; in fact, in some circumstances the measure of damages can be quite different. Therefore, it cannot be assumed that the process of setting quantum that arose between insured and insurer, even with some modification, can be readily used to prosecute a recovery action.

If attention is paid to possible recoveries from the early stages of a claim, issues relating to the development and quantification of the damages can be dealt with efficiently and in a timely manner. For example, to the extent an ACV measurement of loss assists in the potential recovery action, it can be worked out on a proper basis during the course of the adjustment. Too often, the ACV is not terribly relevant or useful to the first-party adjustment and is given short shrift in that process; this can be hard to deal with some months or years later, when it comes time to deal with the presentation of the recovery claim as against the target defendants.

Just as the preservation of physical evidence to prove liability is important, the financial and documentary evidence required to prove the loss must be preserved from early on. This is particularly true in the case of insureds whose business may be failing or about to be sold or merged. Early advice and direction from experienced recovery counsel can be essential in making sure the insurer's interests are protected in these circumstances.

Uninsured losses are often a subject of controversy in dealing with both first-party and recovery claims. It is not unusual for an insured to feel that a significant proportion of its loss was not compensated in the first-party adjustment. Such an insured often wishes to pursue its claim against the perceived responsible parties. While including an uninsured claim in the insurer's recovery action can be fraught with problems, it is generally a good thing from the point of view of encouraging interest and assistance in the litigation from the insured. The proper quantification, support for and evaluation of the uninsured loss is another feature which good recovery counsel can bring to bear in dealing with the claim from an early time.

Controlling Costs: The Role of Contingency Fees

Although contingency fees have been legal in various parts of Canada for some time, it is only recently that their use in Ontario has been fully sanctioned by the legislature, the Law Society and our courts. Generally speaking, the culture of the insurance community here has called for hourly-rate billing on recovery matters and this has had the following effects:

- (a) Because of an intense desire not to "throw good money after bad", insurers have tended to refer matters to counsel for recovery action in only the clearest of cases;

- (b) Again to avoid legal expense, insurers have tended to establish their own recovery departments, staffed by claims people who have or develop expertise in pursuing recovery claims. In at least some instances, this had the effect of having claims personnel making numerous decisions on what is or is not a good recovery claim without the expertise to properly judge the liability situation, or the chances of recovering through the court processes;
- (c) Depending on internal workloads, personnel changes etc. and depending on the personal views of those handling the claims, an insurer's claims department can close many files without seriously examining potential recoveries;
- (d) Even where recovery possibilities are examined, the examination is often seriously hampered by the failure, during the first-party adjustment, to pay proper attention to the investigation and development of recovery possibilities;
- (e) Even where a recovery action is commenced, an insurer has the pleasure of paying regular and perhaps sizable legal bills without any idea of whether there will be a pot of gold at the end of this particular rainbow;
- (f) Where lawyers work on an hourly-fee basis, there is always the suspicion that the lawyer's interest lies in maximizing the number of hours spent on a matter, since that has the effect of maximizing the billings to the client.

It is not surprising that insurers have, in recent times, looked for some alternatives.

Probably the best alternative is the contingency fee arrangement. This arrangement can take many and different forms, depending on the negotiations between counsel and client. However, some typical features are:

- The law firm collects a fee for its work in the recovery action only if a recovery is made;
- The fee collected by the law firm is in proportion to the recovery made, with the result that an insurer is not faced with the prospect of making a recovery that is then eaten up by legal costs;
- The lawyers' and insurers' interests are bound up together in what amounts to a joint enterprise on the claim. There is congruence between the insurer's and a law firm's desire to get the matter settled or otherwise resolved on the best possible basis within the shortest possible time;

- The insurer client bears only the expenses (including expert expense) of proceeding with the recovery action, such expenses being billed on an interim basis;
- Some mechanism is usually provided (in our experience, unnecessarily) for the situations that may arise where insurer and law firm have a falling out or a disagreement as to the handling of the matter;
- Normally, the contingency percentage varies according to the stage of the claim proceedings the settlement has reached, sometimes the size of the claim and sometimes if a regular flow of recovery work is directed to the law firm by the insurer.

At our firm, we firmly believe in the efficacy of the contingency fee arrangement for a regular client and, in fact, for most clients who wish to conduct recovery actions. The arrangement allows recovery counsel to focus on what will cause the case to succeed, without sacrificing any essential element of the preparation of the case. It provides motivation for counsel to do an effective and competent job at early intervention as described earlier, as well as in the conduct of any negotiations or lawsuit. The client can generally rest assured that the matter is being prosecuted properly in the mutual interests of the insurer and law firm involved.

By retaining recovery counsel under a contingency fee arrangement, the insurer can save significant out-of-pocket costs that it would otherwise pay. For example, the conduct of an effective liability investigation, including selection, briefing and supervision of experts, can consume a significant amount of independent adjuster's time and/or company employee's time. What may well be a better job can be achieved, for no out-of-pocket cost, by having expert recovery counsel do the work under a contingency fee arrangement.

In our experience, the best form of contingency fee arrangement governs a flow of business, rather than an individual case. This has the advantage of allowing the insurer to obtain top-quality review of its claims files, for recovery purposes, without paying an immediate or direct price for such review. It suits the law firm's interests in that both good and bad cases will be referred under the contingency arrangement, will be properly evaluated for potential recoveries and will benefit from early intervention. It creates the sort of ongoing joint venture or partnership that allows for the achieving of optimal results and the ready straightening out of any problems that arise.

Parenthetically, you might be interested to know that our firm offers to its clients that have not been under a flow-of-business arrangement, the possibility of a review of first-party claims that were closed without the undertaking of any recovery activity, essentially in order to see whether there is undiscovered potential that should be pursued. This provides something of a check on the claims department's handling of recovery possibilities and can lead to some successful recoveries that are truly "found money". For all practical purposes, this service is free to the insurer.

Some insurers purport to be unenthusiastic about contingency fees, because of the notion that the law firm may make a "killing" on a successful larger case. In our view, this is misguided thinking. First, the law firm risks the entirety of its fee on such a successful result and no one knows at the beginning whether the case will be won or not; there should be some reward for that risk. Secondly, larger cases usually require larger effort to prosecute and this leads to greater out-of-pocket cost for the law firm, as well as greater risk; a large fee is justifiable in these circumstances. Thirdly, the incentive provided to the law firm from the potential of a large fee is a highly desirable element to achieve the insurer's purposes – to get the law firm to work efficiently for the best possible result at the earliest possible time and at the least possible cost. Finally, our legal-costs system provides for a good opportunity for an insurer to recoup from the unsuccessful defendant a significant proportion of its legal costs of having proceeded with the subrogated action.

This represents another advantage of the flow-of-business model: the insurer takes advantage of the small number of lucrative successes for the law firm, by having the firm do a substantial amount of review and prosecution work which is, essentially, completely for free. The benefits of such a program are tangible and counterbalance any windfall nature of a large loss successfully recovered.

One of the measures of the potential benefit of contingency fees for an insurer, is to look south of the border. In the U.S., a high proportion of recovery work is done on a contingency fee basis and the insurers there generally tend to think only in these terms in pursuing recoveries. It is our view that, given the advantages of the contingency fee arrangement for both parties to

the agreement, we are likely to see a substantially increased use of this device in recovery actions in the insurance business here.

The Large Document Case

As commercial transactions become ever more complex, the quantity of relevant documentation for any recovery claim – and particularly for the litigation of such claims – gets ever larger. As any litigation counsel will tell you, the collecting, cataloguing and handling of the documents in a larger case consumes a significant and increasing amount of time - and someone's money - in this era of more complex claims litigation.

To address this money-eater, smart law firms have in recent years increasingly turned to electronic litigation support assets – i.e. the hardware and software necessary for the convenient cataloguing, reproduction and searching of large document databases. Any firm that is not equipped with this capability is simply not in the game.

Some large-document cases are sheep in wolves' clothing: they still boil down to a small number of documents that are crucial to the liability and/or damages decisions. However, it is rarely obvious in the early stages of a matter that this is the case; usually, the documents must be collected, examined, analysed and distilled in order to determine what subset of the documents are the truly important ones. Accordingly, even in this sort of case, the ability to electronically store, retrieve and search documents is essential.

What electronic litigation support of this nature really does is to capture the intellectual product of those working on the documents, in a manner which preserves that product and makes it useable both by the same practitioner or others, in the future. This process is somewhat deceptive: it requires a larger up-front investment of time and effort to develop the database and annotate it properly, but this investment can pay off hugely down the road in a recovery claim. For example, a large collection of potentially relevant documentation must be reviewed by the clerks or the lawyers in a law firm, in order to determine what documents are to be produced to support the claim and/or as relevant to the pleaded issues. If this is done manually, any preservation of the intellectual product of that process depends upon the notes and memory of the personnel working on it and the huge task of preparing an affidavit of documents will

normally still be faced in the future. Under an electronic database system, much of the basic cataloguing of the document collection is done at minimum cost to the insurer, leaving the time of the more highly paid professionals to be engaged in actual analysis of the important documents. Further, once the electronic database has been created, an affidavit of documents can be generated in a fraction of the time required by the more traditional, manual approach.

Another example of the efficiency savings of proper electronic document database support is the reproduction of documents for client, expert or the opposing counsel. A disk of electronic copies of documents, together with any desired cataloguing or notes, can be produced in a few minutes and shipped conveniently to its intended destination. Compare this to the vastly more expensive process of producing photocopied versions of massive document collections (at .25¢ a page!), the shipping of it at significant expense and the difficulties in cost of storage at both ends of that process. In our experience, the savings in copying, shipping and storing costs alone can outweigh the initial cost of the creation of the electronic document database.

Entire programs have been done on the use of electronic litigation support in this area. My purpose here is to just simply demonstrate that this is one area in which specialized recovery counsel can keep costs down and more efficiently reach the optimal result.

Moving the Case

Probably the single biggest complaint about the conduct of recovery actions as traditionally practiced here, is the slow rate of progress of such cases towards a resolution. This starts from the beginning: subrogation/recovery is often not even thought about until after the first-party loss has been settled, often 1 to 2 years after the events. At that time, the matter is often shipped to litigation counsel who then set about evaluating and preparing the case for presentation and, if necessary, litigation. Because there is no deadline on this process (other than a limitation period which, until recently, was typically the rather generous 6-year period provided by statute), time urgency was lost and it has been absolutely customary for subrogated actions to not commence until 3 or 4 years after the events. Because most counsel handling such actions are not specialized to any great extent, and are working on an hourly basis, with interim billing, the claims and litigation are handled on a leisurely timeline with other matters often interfering.

A properly conducted recovery effort, especially under a contingency fee arrangement, significantly alters this equation. Recovery counsel are generally expert in and devoted to making recoveries for their clients. Especially under a contingency fee arrangement, the pay-off for the law firm generally comes at the end of the matter, creating a significant incentive for moving the case ahead. With consistent and persistent application of effort, these cases can be made to move much more quickly than the traditional pattern would indicate.

As anyone who is familiar with our litigation system will tell you, it is not designed to be a fast-moving beast. There are many ways in which a party who wishes to delay and defer, can do so. However, there are definite limitations on how long such delay tactics can go on, in the face of persistence by claimant's counsel. Essentially, claimant's counsel's objective is to settle the matter before litigation or, where that is not possible, to get the matter approaching trial. This is when many liability insurers are prepared to look seriously at settling a case.

It is also a near-universal pattern that the longer a matter persists in our litigation system, the more costly it is. A contingency fee arrangement creates a real incentive for the claimant's law firm to avoid this syndrome. Further, the recovery lawyer that moves the case along will benefit from the lessened cost in legal time.

Consequently, we have focused additional effort and thought to how matters can be moved along to avoid the traditional handling syndrome. Available measures include:

- early intervention, analysis and decision on the prosecution of a recovery claim;
- possible recovery/subrogation agreements with the insured, where there are still outstanding first-party issues;
- early preparation of the tort damages presentation and supporting brief;
- early notice to and involvement of the insurers of the recovery targets;
- one serious pre-litigation attempt to get the defendants and their insurers to pay attention and settle;

- early institution of litigation without waiver of defence for more than a modest amount of time;
- compelling documentary disclosure on a timely basis;
- moving to discoveries at the earliest possible time;
- taking all reasonable steps to maintain discovery dates once set;
- getting undertakings implemented at an early date;
- setting the matter down for trial as soon as possible;
- obtaining pre-trial conference and mediation dates at an early time.

That is the plan; it is not always possible to meet these objectives, but consistent effort along these lines should produce timely results at lower cost.

Conclusion

The cost-efficient handling of larger, more complex claim requires a commensurate response in terms of the application of talent and energy to the development and prosecution of the claim. The steps outlined in this paper will go a long way to limiting costs and maximizing benefits of the recovery efforts that all agree are worthwhile.