Beware quasi-Part 36 offers: a practical view from the Bar

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In his fourth monthly column, James Bickford Smith discusses the Court of Appeal decision in *F & C Alternative Investments (Holdings) Ltd and others v Barthelemy and another* [2012] EWCA Civ 843 to refuse to extend Part 36 principles “by analogy” to non-Part 36 offers. In so holding, the Court of Appeal either called into question, or confined to their own facts, previous decisions in which the High Court appeared to have done exactly this.

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**Part 36 offers: the background**

Part 36 offers are so commonly made, and their importance so widely understood, that one can forget that they mark an exception to the ordinary rules concerning costs (as set out, notably, in CPR 44.3). Those ordinary rules include, in CPR 44.3(4), provisions regarding offers of settlement:

"(4) In deciding what order (if any) to make about costs, the court must have regard to all the circumstances, including:

...

(c) any payment into court or admissible offer to settle made by a party which is drawn to the court's attention, and which is not an offer to which costs consequences under Part 36 apply."

By contrast, the position under CPR 36.10 is as follows:

"(1) Subject to paragraph (2) and paragraph (4)(a), where a Part 36 offer is accepted within the relevant period the claimant will be entitled to the costs of the proceedings up to the date on which notice of acceptance was served on the offeror."
(2) Where –

(a) a defendant's Part 36 offer relates to part only of the claim; and

(b) at the time of serving notice of acceptance within the relevant period the claimant abandons the balance of the claim,

the claimant will be entitled to the costs of the proceedings up to the date of serving notice of acceptance unless the court orders otherwise.

(3) Costs under paragraphs (1) and (2) of this rule will be assessed on the standard basis if the amount of costs is not agreed.

(Rule 44.4(2) explains the standard basis for assessment of costs.)

(Rule 44.12 contains provisions about when a costs order is deemed to have been made and applying for an order under section 194(3) of the Legal Services Act 2007.)

(4) Where –

(a) a Part 36 offer that was made less than 21 days before the start of trial is accepted; or

(b) a Part 36 offer is accepted after expiry of the relevant period,

if the parties do not agree the liability for costs, the court will make an order as to costs.

(5) Where paragraph (4)(b) applies, unless the court orders otherwise –

(a) the claimant will be entitled to the costs of the proceedings up to the date on which the relevant period expired; and

(b) the offeree will be liable for the offeror's costs for the period from the date of expiry of the relevant period to the date of acceptance.

(6) The claimant's costs include any costs incurred in dealing with the defendant’s counterclaim if the Part 36 offer states that it takes into account the counterclaim."

The dilemma

A frequent dilemma faced by parties is whether to make an offer of settlement that falls outside Part 36 (by way of Calderbank letter) and then to rely on CPR 44.3(4) rather than on Part 36. The attraction of doing so is obvious: following the Court of Appeal decision in Home Office v Lownds [2002] EWCA Civ 365 (www.practicallaw.com/9-504-9978), it appears that making even a low Part 36 offer in respect of part of a claim can lead to dramatic costs consequences if it is accepted.
Resolving such dilemmas has been significantly complicated by the different approaches that different courts have taken to the relationship between Part 36 and CPR 44.3 as a whole. Notably:

- In *Medway Primary Care Trust and Dr Ashaq Hussain v Marcus [2011] EWCA Civ 750* (www.practicallaw.com/7-506-7987) (see Legal update, Establishing who was the overall winner for costs purposes (Court of Appeal)), the majority of the Court of Appeal (Jackson LJ dissenting) excused a defendant for not having made such an offer given that "at no stage could the defendants have made a Part 36 offer without incurring a liability in costs wholly disproportionate to the outcome". They were therefore prepared to hold that a claimant who had recovered some £2,000 at trial was not the "successful party" within the meaning of the CPR. The consequence was that the defendant had its costs, despite never having made a Part 36 offer and having had judgment entered against it.

- The thrust of Jackson LJ's dissent in *Medway v Marcus* was that while *Lownds* might be open to criticism, it would be wrong to allow parties to secure the benefits of Part 36 without in fact making a Part 36 offer. That view also underpins Jackson LJ's judgment in *Fox v Foundation Piling Ltd [2011] EWCA Civ 790* (www.practicallaw.com/0-506-8527), a decision handed down a few weeks after *Medway v Marcus* and very difficult to reconcile with it (see Legal update, Jackson LJ clarifies the current law on Part 36). Regrettably, the two cases have yet to be reconsidered by the Court of Appeal. In the meantime, it has been reported that current judicial training is to follow *Fox v Foundation Piling Ltd* (see Legal update, Dominic Regan describes secret abandonment of Court of Appeal costs decision (www.practicallaw.com/9-519-7006)).

The significance of these wider issues emerges in a significant passage from *Fox v Foundation Piling Ltd*, where Jackson LJ held that:

"62. There has been a growing and unwelcome tendency by first instance courts and, dare I say it, this court as well to depart from the starting point set out in rule 44.3(2)(a) too far and too often. Such an approach may strive for perfect justice in the individual case, but at huge additional cost to the parties and at huge costs to other litigants because of the uncertainty which such an approach generates. This unwelcome trend now manifests itself in (a) numerous first instance hearings in which the only issue is costs and (b) a swarm of appeals to the Court of Appeal about costs, of which this case is an example.

63. I hope that the forthcoming amendment to rule 36.14 will point the way to a more clear cut approach to the costs rules in future. In the context of personal injury litigation where the claimant has a strong case on liability but quantum is inflated, the defendant's remedy is to make a modest Part 36 offer. If the defendant fails to make a sufficient Part 36 offer at
the first opportunity, it cannot expect to secure costs protection. Different considerations may arise in cases where the claimant is proved to have been dishonest, but (on the judge’s findings) that is not this case.”

The logic of this position is straightforward: a party that fails to make a Part 36 offer cannot expect to secure costs protection. This has, of course, not stopped parties from trying to secure such protection without making such an offer.

**F & C Alternative Investments (Holdings) Ltd and others v Barthelemy and another**

Such an attempt was at the heart of the Court of Appeal’s decision in *F & C Alternative Investments (Holdings) Ltd and others v Barthelemy and another [2012] EWCA Civ 843* ([www.practicallaw.com/7-520-1716](http://www.practicallaw.com/7-520-1716)) (see Legal update, *Inappropriate to award indemnity costs by analogy with CPR 36.14 (Court of Appeal)*). The underlying dispute was complex, and led to a trial of some 95 days. This raised a series of interesting points, including the duties that members of an LLP owed one another. In short, however, Messrs Barthelemy and Culligan succeeded at first instance in establishing liability of the F & C parties to the value of almost £4 million each plus interest. The issue that then fell to be determined was costs. These were very substantial, with Messrs Barthelemy and Culligan’s untaxed bill running to over £5 million.

At first instance, the judge, Sales J, gave a detailed judgment on costs ([2011] EWHC 2807 (Ch)), much of which consisted of a rejection of the F & C parties’ submissions on costs. Proceeding onwards, however, he held that an offer made by Messrs Barthelemy and Culligan had the effect of a Part 36 offer despite not being such an offer. It is important to set out the material part of that offer in full:

“Unfortunately, this Offer to settle has to be made outside the terms of Part 36. It is clearly necessary that both sets of proceedings be settled in tandem, including both Claim and Counterclaim in the Part 7 proceedings. The fact that formally (although not in substance) your client is in the position of claimant in the Part 7 proceedings, would have the result, were the offer to be made under Part 36, that a rigid application of CPR 36.10 would render our clients liable for the costs of the Part 7 proceedings in the event that the offer was accepted by your client. That would be a nonsensical result, given the fact that in substance our client is in the position of claimant in the Part 7 proceedings and if your client were to accept the offer, it would be making a substantial payment to our clients in respect of their Counterclaim, albeit not the full sum claimed, so that in substance the right costs consequence of that would be that your client should pay our clients’ costs of the Part 7

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proceedings. However, regardless of that absurdity on the facts of the present case, that seems to us to be at least arguably the effect of the rules. Consequently, for that reason and for that reason alone, this offer is made outside the scope of Part 36. However, we shall naturally be drawing this offer to the attention of the Court and relying upon it on the question of costs in both sets of proceedings in accordance with CPR 44.3."

Sales J accepted the argument that there was a "glitch" in Part 36 and that in these circumstances it was legitimate of Messrs Barthelemy and Culligan to have made an offer that "mimicked" Part 36 and that that offer should be given effect to as if it were a Part 36 offer. He therefore made an indemnity costs order for the period postdating the offer.

The Court of Appeal decision

This approach was resoundingly rejected by the Court of Appeal. Davis LJ, giving the lead judgment, held as follows (at paragraphs 53-57):

"53. ... I simply do not think that the judge was justified in drawing an analogy (in assessing the settlement correspondence, and in particular the without prejudice save as to costs letter of 24 December 2009) with Part 36 so as to justify an award of indemnity costs.

54. The starting point has to be that on any view the letter ... was not a Part 36 offer. Not only was it not so headed: but also it in terms stated that it was not a Part 36 offer, explaining why (for reasons which are, it is true, entirely understandable and which the judge plainly considered thoroughly reasonable)...

55. Thus this was not a Part 36 offer and the judge had no jurisdiction to make a costs order under Part 36.14. The judge's jurisdiction as to costs thus fell to be exercised under Part 44.3: as, indeed, the closing words of Part 36.14 mandate. The judge rightly accepted that he was required to exercise the jurisdiction under Part 44.3.

56. Once that position is appreciated, however, I have the greatest difficulty in seeing how the costs regime of Part 36, whether indirectly or by analogy, can properly be invoked. Part 36.14 represents a departure from otherwise established costs practice. It imposes a deliberately swingeing costs sanction, by Part 36.14(3), on a claimant who fails at trial to beat a defendant's Part 36 offer. That is, for policy reasons, designed to encourage a sensible approach of claimants to offers and to promote settlement (that defendants do not get corresponding benefits under Part 36 may be for reasons in part explained by Simon Brown LJ in paragraph 6 of his judgment in the case of Kiam v MGN Ltd [2002] EWCA Civ 66). But there is no reason or justification, in my view, for indirectly extending Part 36..."
beyond its expressed ambit. Indeed to do so would tend to undermine the requirements of Part 36 and the repeated insistence of the courts that intended Part 36 offers should be very carefully drafted so as to comply with the requirements of Part 36. As Mr Browne observed, Part 36 is highly prescriptive with regard to both procedures and sanctions.

57. The judge thought that the failure of Part 36 to extend to the position of litigants in the position of the respondents constituted a "glitch" in the operation of Part 36 and called for adjustment to reflect "the infelicity in the wording" of Part 36. With respect, I do not regard that as a permissible approach. Parliament has decided what the ambit of Part 36 is to be. It is to be regarded as self-contained for these purposes and it is not for the parties or the courts to go around looking for asserted glitches or asserted omissions so as to bring a case indirectly within the reach of Part 36 when it cannot directly be so brought in...

**Comment**

The decision in *F & C Alternative Investments (Holdings) Ltd and others v Barthelemy and another* is extremely significant. First, as to its relationship with previous authority:

- It suggests that the Court of Appeal is adhering to the position set out in *Fox v Foundation Piling Ltd*: to secure costs protection a defendant must make a Part 36 offer.

- The Court of Appeal has not followed the approach in *Carver v BAA plc [2008] EWCA Civ 412* (www.practicallaw.com/5-506-3235) (now in any event of limited significance given the insertion of CPR 36.14(1A)).

- *Huntley v Simmonds [2009] EWHC 406 (QB)* (www.practicallaw.com/8-385-3035) must now be seen to stand only for the narrow proposition that trivial errors in a Part 36 offer do not stop this from being taken into account as a Part 36 offer.

- The Court of Appeal has doubted *Fitzroy Robinson Ltd v Mentmore Towers Ltd [2010] EWHC 98 (TCC)* (www.practicallaw.com/5-520-0807); while Davis LJ held that the overall decision in that case was justifiable, he criticised elements of the judge's approach in that case to non-Part 36 offers.

Secondly, and practically, the decision suggests that:

- Carefully worded Calderbank letters are not to be treated as Part 36 offers. Indeed, while the letter at the centre of the case would seem judicious at least at first sight, Davis LJ ultimately held it to be "in truth... an ingenious and unilateral construct" (paragraph 58 of the judgment).
Attempts to broaden Part 36 “by analogy” are very likely indeed to be rejected. Likewise, attempts to point to gaps or defects in the rules as justification for not making a Part 36 offer are likely to be met with short shrift.

Above all, if one is to rely on a Calderbank letter for costs protection, one must go further and persuade the court that the refusal of that offer was not simply unwise with the benefit of hindsight but was in fact unreasonable.

The best route to indemnity costs may well be to use rejection of an offer made in a Calderbank letter as part of a wider picture of unreasonable conduct, rather than to focus simply on that offer itself.

Thirdly, and following from this final point, it should be noted that while *F & C Alternative Investments (Holdings) Ltd and others v Barthelemy and another* may close the door to attempts to argue “by analogy” with Part 36, it of course remains open to a party to secure indemnity costs orders by reference to the conduct of the other side before and during the litigation. Given the increasing willingness of courts to make such orders, and the tighter view now being taken of Part 36 offers, one should expect an increase in such applications in the future.