

The First Annual Hailsham Chambers Costs Seminar

13 and 14 July 2005

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CONDITIONAL FEE AGREEMENTS AND AFTER THE EVENT INSURANCE: ALL CHANGE AGAIN?

Alexander Hutton

(1) CONDITIONAL FEE AGREEMENTS

(a) Success Fees

1. Two recent decisions by the Court of Appeal have finally provided much-needed guidance for success fees.
2. In Atack v Lee; Ellerton v Harris [2004] EWCA Civ 1712, the Court held:
 - (1) In Atack that, in relation to an RTA case involving a roundabout issue which went all the way to trial on liability (and quantum), a 100% success fee was not justified because, on proper analysis, at the time the CFA was entered into the prospects of success were better than 50-50; and the 50% success fee allowed below was upheld. However, it is of note that they considered it would have been reasonable to allow anything up to 67% success fee;
 - (2) In Ellerton, a case involving reversing a car in a car park and knocking down an elderly pedestrian, the guidance given by the Court in Callery v Gray (No.1) [2001] EWCA Civ 1117; [2001] 1 WLR 2112 was appropriate and the 20% success fee allowed there was applied.
3. What emerges from this judgment in terms of general principles is:

- (1) It is simply the risk as it appeared to a reasonable solicitor of losing the case at the time when the CFA was entered into which was the vital issue on the setting of an appropriate success fee in each individual case– see paragraphs 8 (cf Lord Scott in Callery [2002] 1 WLR 2000) and 37;
- (2) Nevertheless, statistical evidence as to the percentage of those type of claims which succeed can be of assistance to a solicitor in setting his success fee in a particular case, and thus also to the court in determining a success fee – see paragraph 12.
- (3) However, the fixed fee agreements in relation to RTA claims (now enshrined in CPR 45 Parts II and III) cannot apply to cases where CFAs were agreed before those provisions came into effect;
- (4) Factual matrices used by Claimant’s solicitors to calculate success fees and which attach particular percentages when particular factors are present (e.g. value of claim, letter denying liability etc) are of no value at all – see paragraph 37.
- (5) The mere fact that a defendant denies liability vigorously before a CFA is entered into does not in itself justify a 100% success fee. While that is a relevant factor in setting the success fee, the question is what the risk truly was on a proper analysis of the merits and otherwise of the case (paragraph 38).
- (6) Further, the mere fact that a case goes all the way to trial on liability does not necessarily mean that 100% is justified. Firstly, this is not strictly relevant as it uses hindsight (see more below), but also it is inevitable that some litigants (i.e. in this instance, defendants) do fight cases where their prospects of success are, on a proper analysis, less than 50%. While fighting a case all the way to trial makes the defendant’s argument on a detailed assessment more tricky, the lesson is “don’t give up!”;

- (7) The apparent rule in Callery (Court of Appeal, paragraph 100) that a solicitor is entitled to sign up a client to a CFA as soon as he walks through the door is not absolute: in Ellerton it was held that one simple phone call to find out one piece of evidence would have resulted in a reduction of the risk before the CFA was entered into, and that the success fee should be assessed on the basis that a reasonable solicitor would have made such a phone call at that stage: paragraph 49.
- (8) Again, Callery-style two stage success fees (i.e. 100% reducing retrospectively to a lower percentage if it settles by a certain point) were encouraged.

4. KU (A child, by her Mother and Litigation Friend PU) v Liverpool City Council [2005] EWCA Civ 475 was a tripping case in which a 4 year old girl stepped into a hidden hole in a grass verge between a public car park and a road. The solicitors agreed a 100% success fee. The Defendant had not disputed the 100% initially but contended that, for the period after a Defence was filed admitted liability, the success fee should be reduced to 5%. The District Judge agreed with them but HHJ Stewart QC held that there was no power to award different success fees in this way and altered it to 100% throughout. The Defendants then contended on their further appeal to the Court of Appeal that not only the Judge was wrong on the law but that 100% was too high anyway.

5. The Court of Appeal decided:

- (1) That 100% was too high at the time the CFA was entered into – this was a case where the reasonable solicitor ought to have concluded the prospects of success were 2:1, and that was consistent with statistical evidence about the success of tripping claims. Therefore the appropriate success was 50% (using the

“ready reckoner” (see paragraph 25), albeit the actual result was not altered (see paragraph 54);

- (2) Conclusively that, if a CFA is agreed with a single success fee throughout, the Court has no power to direct that a success fee is recoverable at different rates for different periods of the proceedings. The task of the Court was to consider what a reasonable success fee would have been at the time the CFA was entered into on the information available then to a reasonable solicitor. There was no room for the application of hindsight subsequently to reduce the success fee in the light of later events changing the risk (see Francis v Francis and Dickerson [1956] P 95) - see paragraph 20.
- (3) CPD 11.8(2), which states that the court can award different success fees in respect of different periods is inconsistent with the language of Section 58 of the Courts and Legal Services Act, the Conditional Fee Agreements Regulations 2000 and CPR 43.2. It is therefore wrong and should be ignored: “...*a practice direction has no legislative force. Practice directions provide invaluable guidance to matters of practice in the civil courts, but in so far as they contain statements of the law which are wrong they carry no authority at all.*” (see paragraphs 46-49).
- (4) The District Judge (as is commonly the case) misunderstood Callery in thinking it gave him authority to allow different success fees for different periods – it does not (paragraph 50).
- (5) Again encouraging two stage success fees, that DJ’s and Costs Judges should be more willing to allow higher success fees for cases which do not settle early if the CFA was agreed with a two stage success fee with a much percentage applicable if the claim had settled at an early stage (paragraph 57).

6. Quite apart from their conclusions on the law, the general tenor of those judgments are that the profession is claiming excessive success fees and, to some extent, the courts are allowing them. Further, in Begum v Klarit [2005] EWCA Civ 210 the Court of Appeal had themselves to assess a success fee in relation to an appeal before them, which had essentially been dismissed.

Brooke LJ (again) held that :

“anybody assessing in a careful and thoughtful manner the prospects of the appeal from the point of view of the respondents would have been likely to appreciate ...that they were pretty close to a stone-cold certainty of successfully resisting the appeal.”

7. He described Counsel’s claim for a success fee of 100% and the solicitor’s for 70% as being at a level which “*discredit and devalue the whole of the arrangements for conditional fee agreements*”, and referring to the House of Lords’ concern in Callery that there was no incentive to keep success fees down, went on to say this:

“I hope this is the last occasion on which this court will have to express itself quite so strongly about the level of success fee proffered for approval. In our judgment, there was a small amount of risk in this litigation, which would properly have been provided for by a success fee of 15 per cent.”

Profession be warned.....

8. However, in Burton and Haynes v Kingsley and Harper [2005] EWHC 1034 (QB), Richards J allowed a success fee of 50% (reduced from a claim of 100%, but distinguishing Callery) for two passengers claims in respect of serious injuries because “there remained a possibility that this was an accident for which no-one was to blame, or that the blame lay with the untraced driver, or the claimants would not be able to establish who was to blame).

(b) Assignment of CFA’s

9. Does a new CFA needs to be entered into if the client moves firms (usually because the fee earner moves firms and takes the client with them) and/or the

old firm comes to an end and a new firm rises up in its place, or can this be dealt with by assignment of the contract between the old firm and the new firm.

10. The answer at Costs Judge level is that it is lawful to assign a CFA in this manner and, even if it wasn't and thus there was a breach of Regulation 4 by failing to take the client through those matters, such a breach would not be "material" under the Hollins v Russell test: see Jenkins v Young Brothers Transport Ltd (Costs Judge Campbell 22nd June 2005), where the conducting fee earner moved firms twice during the course of the litigation and both times the CFA was assigned.

(c) BTE Cover and Breaches of the CFA Regulations

11. Due to the amount of successful technical challenges to recovery of costs on the basis of minor breaches of Section 58 and/or the CFA Regulations 2000, which resulted in a total disallowance of costs, the Court of Appeal eventually had to make up some new law to ensure the whole scheme was viable in the conjoined appeals Hollins v Russell [2003] 1 WLR 2487 where they held that the question of whether the requirements were "satisfied" introduced a test of materiality of breach (paragraph 107):

"Has the particular departure from a Regulation pursuant to Section 58(3)(c) of the 1990 Act or a requirement in Section 58, either on its own or in conjunction with any other such departure in the case, had a materially adverse effect either upon the protection afforded to the client or upon the proper administration of justice?"

12. This slowed but has certainly not put a stop to challenges to the validity of CFA's. For instance, the most fruitful source of challenge has been in relation to Regulation 4(2)(c) which is the requirement to inform the client

"whether the legal representative considers that the client's risk of incurring liability for costs in respect of the proceedings to which the agreement relates is insured against under an existing contract of insurance."

13. The Court of Appeal held in Sarwar v Alam [2002] 1 WLR 125 (CA) that it was not good enough for a solicitor simply to ask the client whether he had any available existing insurance as clients would often not know. Therefore, it was necessary to ask the client to bring in any relevant motor insurance policy, household insurance policy, any standalone BTE policy belonging to the client or partner living with him/her.
14. In Culshaw v Goodliffe, HHJ Stewart QC (unreported, Liverpool CC, 24th November 2003) the solicitor simply asked the client and relied on his saying he had no policy, but in fact the client did have an appropriate policy; held that there was a material breach of Regulation 4(2)(c), rendering the agreement unenforceable so that no costs were recoverable. There was a similar outcome in Adair v Cullen where there was also an appropriate BTE policy which was not discovered (unreported, HHJ Holman on 14th June 2004).
15. In Samonini v London General Transport Services Ltd [2005] EWHC 90001 (Costs) Senior Costs Judge Hurst found that a solicitor relied solely on the fact that an unqualified employee of a claims handling company had asked the client if she had LEI and he said not. In fact, he did not even have LEI. Nevertheless, the Costs Judge found that inadequate steps had been taken, the breach of Regulation 4(2)(c) was material and all costs were disallowed. He also held that a premium of £750 for a case worth £2,000 would have been disproportionate in any event.

The Future

16. There has been a general recognition that the recoverability system introduced in 2000 has, in general, been an unwieldy and expensive disaster. This has led to some calling for the introduction of US-style percentage contingency fees

and/or the abolition of between the parties' costs. The Department of Constitutional Affairs (DCA) first tried to simplify the procedures to stop technical challenges in 2003 by introducing "CFA-lites" in amended Regulation 3A, but these were so full of holes that almost no-one dared use them.

17. They now propose to take a far more radical approach. In January this year they produced draft Regulations revoking all the CFA and Collective CFA Regulations. The only statutory requirements would therefore be that the agreement be in writing, it does not apply to criminal or family proceedings and that the success fee must be stated and cannot be more than 100%. There would be no requirement that it even be signed, let alone that it have all the "consumer protection" requirements in the current Regulations. In effect, the CFA could simply be a simple letter. Query whether this allows US-style contingency fees? On this subject, see comments by the Privy Council (including Lords Hope, Hutton and Scott) in Kellar v Williams (Privy Council Appeal no. 13 of 2003, 24th June 2004 at paragraph 21, echoing the views of Millett LJ in Thai Trading v Taylor [1998] QB 781).
18. The policing of CFA's (such as it would be) would then be done by amendments to the Solicitors' Costs Information and Client Care Code 1999 making it a disciplinary matter and not one which could be relied upon by the paying party.
19. However, although the intention is to end the satellite litigation, this might fail. Practice Rule 15 requires compliance with the Solicitors' Costs Information and Client Care Code, and the Practice Rules themselves are delegated legislation as if it were set out in the Schedule to an Act of Parliament: see Swain v The Law Society [1983] 1 AC 598 (HL) Awwad v Geraghty [2001] QB 370 (CA). Therefore, the question of the effect of

breaches of Practice Rule 15 (does it render the contract of retainer unlawful and thus unenforceable?) will be ripe for further litigation.

(2) ATE INSURANCE PREMIUMS

20. Despite the fact that assessing an insurance premium is not a subject which District Judges and Costs Judges are likely to have had any experience at all before such could be recovered on detailed assessments of costs from April 2000 onwards, and, according to the House of Lords in Callery v Gray (No. 1 and 2) [2002] 1 WLR 2000, the Costs Judge is the only check on reasonableness of the premium as there is no genuine competition on price, there has been precious little guidance on the proper approach to take.
21. It was established in Claims Direct Test Cases [2003] EWCA Civ 136 and Accident Group Test Cases [2004] EWCA Civ 575 [2004] 3 All ER 325 that a “premium” is only recoverable under Section 29 of the Access to Justice Act 1999 to the extent that it is a genuine insurance premium to cover the risk of having to pay out on the claim. If other additional costs are claimed as part of the premium (for instance the costs of providing a whole claims management package), then the costs of this must be stripped out to find the reasonable premium.
22. In the RSA Pursuit Test Cases (Senior Costs Judge Hurst, 27th May 2005) the court had to consider various issues arising from a policy which calculated the premium based on a percentage of the solicitors’ own base costs (before assessment). This had resulted in some very substantial premiums. Master Hurst held:
- (1) A premium based on a percentage of the solicitor’s own base costs was not champertous (para 306) or void for uncertainty (para 277-282);
 - (2) In considering the proportionality of an ATE premium, the Court must look both at the size of the premium as compared to the realistic value of the claim (see Lownds v Home Office [2002] 1

WLR 2450) and the size of the premium compared to the likely adverse costs potentially covered by the premium – paragraph 261;

- (3) Just because a client accepts a policy on the basis of a solicitor’s advice which cannot in itself be held to be “negligent” in a technical legal sense, does not mean that the premium has to be allowed in full (cf Sarwar v Alam [2000] EWCA Civ 1401). Negligence of the solicitor is not the appropriate test as to whether a premium is reasonable or proportionate - see paragraph 264;
- (4) Just because the particular premium in question may be the only one available does not mean that it must, as a matter of law, be allowed as claimed on the basis that the claimant had no other choice. The premium itself must still be reasonable and proportionate even if there was no choice available of a cheaper premium – see paragraph 265;
- (5) The fact that any shortfall in the premium may fall on the client because he is contractually bound to pay the entire amount (and may have no recourse to a solicitor-own client assessment under Section 70 of the Solicitors Act 1974 in respect of an insurance premium) does not alter the Court’s task or approach on this issue – see paragraph 267;
- (6) The court cannot simply rely upon the market to test whether a premium is reasonable because, even now, the ATE market is still developing – see paragraph 268 – and “*There is no evidence before me of any efficient market for ATE products dealing with this type of case [complex PI and clinical negligence]*”;
- (7) The level of the insurer’s profits on the product are not relevant – see paragraph 270;
- (8) Calculating a premium which was extremely sensitive to the accuracy of estimates of costs both for the claimant and the

defendant is “*inherently likely to be arbitrary*” and flawed – paragraph 346;

(9) Basing a premium on costs as claimed not as assessed is likely to be unreasonable and disproportionate – paragraph 347;

(10) It is not appropriate to use hindsight in calculating the premium – cf KU (above) – paragraph 355.

(11) The RSA Pursuit policy was “*inherently and seriously flawed*” in that it assumed a constant relationship between own costs and the other side’s costs which is not true in practice – see paragraph 362;

(12) However, increasing the premium to allow for the fact that the premium is not chargeable in losing cases is allowable (paragraph 362);

(13) Having found the method of calculation “*inherently and seriously flawed*”, the task of the court was to allow such sum as was reasonable and proportionate to expect the paying party to pay having regard to all the circumstances in the case – see paragraph 363.

(14) The question of whether the policy was taken out unreasonably late in the proceedings, thereby resulting in a higher premium than if it had been taken out earlier (cf the opposite argument run in Callery v Gray (No.2) [2001] 4 All ER 1) has to be based on the individual facts in each case. In general, it is not unreasonable to wait until the client is at risk of paying the other side’s costs: paragraph 374.

23. A related topic is that of “stepped premiums”: i.e. ones which go up the nearer one gets to trial. In principle, there is little doubt that the Courts will like them, as they provide an incentive to settle early and accord with the principle of the Court of Appeal’s much loved two-stage success fee. But how are they to be calculated in an off-the-peg ATE policy for ordinary fast track litigation?

24. In this regard, see the case of Tyndall v Battersea Dogs Home currently being fought between Master O'Hare and the Defendant's argument that the Europ Assistance premium includes double charging because the small number of expensive losing cases are already accounted for in the Stage 1 or Stage 2 premiums, and thus in the Stage 3 premium, the Defendant is being asked to pay for those expensive losers twice. Watch this space.....

Alexander Hutton

Costs caps and estimates: have they now got teeth?

Clare Price and Roger Mallalieu

Costs caps

1. There can be no question but that the Court is keen to control the level of costs incurred in litigation: one of the principal objectives behind the Woolf reforms was the reduction of costs. However, it appears that the objective has not always been achieved (for example, costs which exceed the value of a claim are frequently seen as are high claims in cases involving experts) and it is therefore not surprising that the Court has sought to impose more rigorous controls on the level of costs to be allowed. Further, since it is apparent that retrospective control at the assessment stage (the time at which costs are usually addressed) is not always an effective control method, it is little surprise that the Court has considered whether it can prospectively limit the amount to be spent on litigation.
2. The need for parties to adopt a prospective approach to controlling costs was emphasised by Lord Woolf CJ early in the life of the CPR in *Jefferson v National Freight Carriers* [2001] 2 Costs LR 313 when he adopted HHJ Alton's approach and focused on the need for parties to make an assessment of costs at the outset of a claim so as to identify, for example, the level of fee-earner to be employed on the case and the time to be spent on it. Experience has shown that Lord Woolf's hopes in this regard have not been fulfilled and budgeting by solicitors alone is unlikely to be sufficient in every case. If there is to be real and effective control on costs expenditure, the Court itself must have power to impose limits. Thus, in *Griffiths v Solutia* [2001] EWCA Civ 736, [2002] PIQR P176, Mance LJ observed that judges should make full use of their powers to obtain costs estimates and that they should exercise their powers in respect of costs to keep them within the bounds of the proportionate in accordance with the overriding objective. The possibility of the Court imposing a cap on costs was raised, though how that would be achieved in practice was not addressed.
3. However, how effective is the costs cap as a means of restricting expenditure? It is clear that the Court believes they could be usefully employed: see Dyson LJ in *Leigh v Michelin* [2003] EWCA Civ 1766, [2004] 1WLR 846:-

"There is, however, much to be said for costs budgeting and the capping of costs. ...We recognise that the use of CPR 43 PD para 6.6 to control costs by taking costs estimates into account at the assessment stage is not the most effective way of controlling the cost of litigation. It seems to use that the prospective fixing of costs budgets is likely to achieve that objective far more effectively."

When, and in what circumstances, should the Court impose a costs cap?

4. Are they only to be made in group litigation cases where costs can become very high? In *The Ledward Claimants* [2003] EWHC 2551 (QB), Hallett J made a costs capping order in a case where there had been a Group Litigation Order and eight lead cases identified. The parties were agreed on the need for a costs capping order and Hallett J was satisfied she had power to make such an order as a result of Section 51 Supreme Court Act 1981, the Court's wide ranging case management powers and the overriding objective, expressing concern that the costs would otherwise "spiral out of control, if they have not already done so". However, it is clear the Court does not regard the power to impose a costs cap as being restricted to group litigation only. In both *Smart v East Cheshire NHS Trust* [2003] EWHC 2806 and the *Nationwide Organ Group Litigation* [2003] EWHC 1034 (QB) Gage J observed that the imposition of a costs cap is not limited to GLO's and that the jurisdiction existed in other cases as well.
5. Are they thought to be of universal application? Can practitioners expect to see them imposed as a matter of course? Each case will turn on its own facts. However, there is now considerable experience of how the issue will be approached in the context of clinical negligence cases. In *Smart*, Gage J observed that:-

"it seems to me very unlikely that it would be appropriate for the court to adopt a practice of capping costs in the majority of clinical negligence cases."

In his judgment, the correct test for the Court was that it should only consider making a costs cap where:-

- i) the applicant shows by evidence that there is a real and substantial risk that without such an order costs will be disproportionately or unreasonably incurred ('spiralling out of control');
- ii) that risk may not be managed by conventional case management (e.g. orders limiting the expert evidence allowed or defining the issues to be tried) and a detailed assessment of costs after a trial;
- iii) it is just to make such an order.

Gage J stated that he would expect that in the ordinary run of cases it would be rare for the test to be satisfied. The Court also emphasised that there should not be a proliferation of expensive and lengthy applications for costs caps – the need for evidence to support the application and the risk of there then following expensive satellite litigation may well be factors which mean that, in practice, few such orders are made.

6. *Musa King v Daily Telegraph* [2004] EWCA Civ 613 provided an example of the use of costs caps in more unusual circumstances. It is, perhaps, unfortunate that it

was only late in the day that the Defendant in this case asked the court to order a cap on costs (at first instance and initially on appeal the application had been for security for costs). The case did, however, usefully provide Court of Appeal approval for the use of costs caps. Brooke LJ held that in defamation cases where the Claimant acted under a CFA without ATE insurance a capping order should be made as a matter of course at the allocation stage. However, as Brooke LJ pointed out, 'a costs capping regime is one thing. A costs capping regime in a CFA context is another'. Accordingly, the Court limited its decision to the very narrow circumstances set out. Guidance as to the use of costs caps in more general circumstances (and the principles to be adopted) will have to await a suitable case.

Recent Developments

7. In *Sheppard v Essex Strategic Health Authority* (2005), Hallett J was prepared to impose a costs cap where the estimated costs to trial were £516,000 (as opposed to the Defendants' estimate of £151,000) and there was apparently a very real dispute as to both liability and quantum. It was made clear that it was not necessary to make any adverse findings as to the way the solicitor had conducted the matter (unlike in *Ledward*). Nor did a costs cap carry any stigma or implied criticism. Hallett J accepted the submissions of the Defendant's counsel that there may come a time when such caps are standard, but considered that, at present, a case still required some unusual feature before a cap would be imposed.
8. However, the case of *Weir v Secretary of State for Transport* (2005) decided only a few weeks earlier indicates that the approach which will be adopted cannot yet be predicted with certainty. Lindsay J, in contrast to the approach of Hallett J, adopted the principles from *Smart*. Further, he considered that if the discretion to impose a cap was to be interpreted any wider, as an irreducible minimum the court would have to consider whether the claim would be stifled if a cap was not imposed. Given the discretionary nature of the power to impose caps and the differing approaches adopted, it is likely that appellate guidance will be required before the position is resolved.

Costs estimates

9. *Leigh v Michelin* [2003] EWCA Civ 1766, [2004] 1WLR 846
Here, the Court of Appeal had to consider how to deal with a costs estimate which was given at the allocation questionnaire stage of litigation, was not subsequently updated at the listing questionnaire stage, and which proved to be "hopelessly inadequate" when compared with the final bill of costs (i.e. costs to date of AQ were £3,000 plus VAT, final costs estimated at £6,000 plus VAT and the bill of costs was £21,741.28). The Court of Appeal held that a costs estimate may be taken into account in determining the reasonableness of the costs claimed on assessment in the following circumstances (although this was expressly said not to be an exhaustive list):-

- a) Estimates of the overall costs of litigation should provide a useful yardstick by which the reasonableness of the costs finally claimed may be measured. If there is a substantial difference between the estimate and the final figure, then the difference calls for explanation. In the absence of a satisfactory explanation, the Court may conclude that the difference itself is evidence from which it can conclude unreasonableness.
 - b) The Court may take the estimate into account if the other party shows that it relied on the estimate in some way, giving the example of B being able to show he relied on A's estimate of costs in deciding not to settle a case but to carry on with it in the belief that he knew his potential liability for costs if unsuccessful.
 - c) The Court may take the estimate into account if it would have made different case management decisions had it known the final costs would be much higher than the estimated ones, e.g. it would have reduced the number of experts for whom permission was given.
 - d) However, it would not be appropriate to use the estimate to reduce the costs payable simply because it was an inadequate estimate. If the other party did not rely on it, the Court would not have made different directions and the costs are otherwise reasonable and proportionate, it would be wrong to reduce the costs simply because they exceeded the estimate. To do so, would be tantamount to treating the estimate as a costs cap.
10. The final part of this conclusion leaves it unclear what sanction, if any, a court can apply properly if it concludes that any explanation is unsatisfactory and therefore the difference itself is evidence that the costs are unreasonable.
11. The Court of Appeal recognised the risk of satellite litigation about, for example, whether the Court would have made different case management decisions but concluded that, if the estimates could not be taken into account at the assessment stage, then there was in effect no point to them. Dyson LJ said that it should not be difficult to decide whether a paying party had relied on a costs estimate to his detriment or whether the Court would have made a different order without a lengthy and expensive investigation. Whether this is so remains to be seen.
12. In *Burns v Novartis Grimsby Ltd* (2004), the estimated costs at AQ were £17,500 to date and £35,000 in total but the amount claimed in the bill was £99,215.52 (excluding the premium and success fee, it was £71,082.20). However, the Claimants said the case had changed dramatically from the time of their estimate because of the progression of *Fairchild* through the Courts and it had become a contested case which went to trial. As a result, much more work was needed than originally anticipated and they should not be held to their original estimate. Although the Defendants did not then pursue their point on the costs estimate, it seems the argument about effect of *Fairchild* would have found favour with Master

Hurst and he would have accepted that there was a satisfactory explanation for the substantial difference between the estimate and final bill. Once again, the way in which the court would have reflected the estimate on assessment in absence of a satisfactory explanation was not properly addressed.

13. If costs estimates are to be of any substantial benefit to parties then the conclusions reached in Leigh demonstrate that the time to address the estimate is at the case management stage of proceedings by, for example, seeking to limit the number of experts which may be called, rather than by simply relying on an underestimate at detailed assessment. If the later course is to be pursued then a paying party will have a much stronger case if it can clearly show that it had regard to the estimates during the case and that it conducted its own case in light of the estimates which had been given. As ever, good record keeping and documentary evidence will be vital in this regard.

Clare Price
Roger Mallalieu

The effect of conduct on costs: Aaron v Shelton, mediation and misconduct

Andrew Post

The CPR costs rules are full of references to conduct, so it is scarcely surprising that there has been persistent controversy over the effect on costs of the parties' conduct in the course of the proceedings.

The key issues are:

- a. When can the point be taken?
- b. What sort of conduct will lead to a penalty in costs?
- c. What is the effect?
- d. What can you do if the issue was not raised at the time of the costs order?

a. When can a point on conduct be taken?

This is the point addressed by the decision of Jack J in *Aaron v Shelton* [2004] EWHC 1162 QB:

Where a party wishes to raise in relation to costs a matter concerning the conduct of his opposing party (either before the litigation or during it), it is his duty to raise it before the judge making the costs order where it is appropriate to do so.

Will Aaron be reversed?

Aaron is not an entirely satisfactory decision, not least because Mr Aaron appeared in person and Shelton was not represented by a costs specialist. Two relevant cases - Booth v Britannia [2002] EWCA Civ 579 and Shirley v Caswell [2001] 1 Costs LR 1 were not cited.

The decision was, however, certainly reasonable on the facts and although the judge decided the case in a rather broader fashion than might have been desirable, the rule is workable and sensible so long as proper regard is paid to the words "where it is appropriate to do so". It is therefore unlikely that the Court of Appeal will disapprove the decision, even though it was reached without citation of significant cases.

What is the practical effect?

The practical effect is that it is essential that conduct is considered when a costs order is to be made at the end of proceedings or after any important interlocutory hearing.

The old school approach to costs was "costs follow the event; everything else can be sorted out on assessment". That attitude should have died out long ago given the flexibility allowed by CPR 44.3, but all too often we see cases in which a party has agreed to a standard form costs order, even where there are good grounds for a completely different order.

The decision is therefore yet another reason why parties should consult their costs draftsman or, in a substantial case, perhaps even speak to costs counsel before agreeing the costs order.

2. What sort of conduct will lead to a penalty in costs?

- Failure to comply with the pre-action protocol
- Unreasonable failure to mediate
- Other misconduct

Failure to comply with the pre-action protocols

Note that the terms of the Practice Direction on Protocols are mandatory:

Practice Direction on Protocols

2.2 The court will expect all parties to have complied in substance with the terms of an approved protocol.

2.3 If, in the opinion of the court, non-compliance has led to the commencement of proceedings which might otherwise not have needed to be commenced, or has led to costs being incurred in the proceedings that might otherwise not have been incurred, the orders the court may make include:

(1) an order that the party at fault pay the costs of the proceedings, or part of those costs, of the other party or parties;

(2) an order that the party at fault pay those costs on an indemnity basis;

...

2.4 The court will exercise its powers under paragraph 2.1 and 2.3 with the object of placing the innocent party in no worse a position than he would have been in if the protocol had been complied with.

...

3.2 *A defendant may be found to have failed to comply with a protocol by, for example:*

(a) *not making a preliminary response to the letter of claim within the time fixed for that purpose by the relevant protocol;*

(b) *not making a full response within the time fixed for that purpose by the relevant protocol.*

Note that it is necessary to show causation - the court is required to put the innocent party in no worse a position than it would have been in if the Protocol had been followed.

Unreasonable refusal of mediation

Definitive guidance has been given by the Court of Appeal in Halsey v Milton Keynes [2004] EWCA Civ 576: the onus is on the unsuccessful party seeking to avoid the conventional order, and that party must show that the opponent has acted unreasonably in refusing ADR.

The factors that will go to determine whether refusal to mediate was reasonable or not are:

- The nature of the dispute
- The merits of the case
- Attempts at other methods of settlement
- Costs of mediation
- Delay
- Prospects of the mediation succeeding

Other misconduct

This can encompass exaggeration of a claim, delay, failure to co-operate, persistence with a hopeless defence, breach of obligation to disclose.

3. What is the effect of misconduct?

Failure to comply with a protocol

Aegis Group Plc v Inland Revenue (Park J, 13/5/05): 15% costs penalty for successful Defendant for failing to reply to letter of claim

Daejan Investments v The Park West Club [2003] EWHC 2872 (TCC): party making fundamental change to case midway through proceedings ordered to pay costs to date on the basis that it had failed in substance to comply with Protocol.

Unreasonable refusal to mediate

Denial of costs to successful party: Dunnett v Railtrack [2002] EWCA Civ 303

Variation in costs order in favour of innocent party: Burchell v Bullard [2005] EWCA Civ 358

But note that the court will be astute to prevent parties using the offer to mediate tactically in order to squeeze an offer on an unmeritorious case: Halsey

4. What can you do if what can you do if the issue was not raised at the time of the costs order?

First: should it have been? Note the word appropriate in Jack J's formulation.

Secondly: consider whether the conduct can be characterised in some other way - was the conduct in question disproportionate or unreasonable; if so it may be possible to characterise it that way, instead of alleging misconduct.

Andrew Post