LET'S BE REASONABLE

EFFECTIVE CALDERBANK OFFERS

Unreasonable rejection of a Calderbank offer risks an adverse costs order, but the offer must itself be reasonable and allow the offeree time to consider it and to assess their chances of success. **By Nigel Watson**

It has become increasingly common for a court to entertain an application for special costs orders arising out of the rejection of a Calderbank offer not bettered on judgment when that rejection can be demonstrated to be unreasonable. While Calderbank offers may prove to be a powerful tool in triggering favourable cost sanctions, the question of costs remains a discretionary matter, and recent judgments continue to highlight the importance of having regard to the various factors that determine unreasonableness in rejecting an offer.

CALDERBANK OFFERS

An offer of compromise pursuant to O.26 of the *Supreme Court (General Civil Procedure) Rules* 2005 (a formal offer) has virtually automatic cost consequences. Those consequences are an award of costs to the party making the offer, on a party and party basis from the expiry of the offer. The court does, however, retain discretion to award costs on a more favourable basis.

A Calderbank offer is an offer of compromise made on a "without prejudice" basis, save as to the question of costs. The offer is made in accordance with the principles of *Calderbank v Calderbank*,[1] subsequently applied in the Supreme Court of Victoria by Byrne J in *Mutual Community Ltd v Lorden Holdings Pty Ltd & Ors*.[2]

The Calderbank offer may provide greater flexibility than a formal offer and will, at times, assist in encouraging the court to award costs on a more favourable basis. It is important to emphasise that there is no prima facie presumption for an award for indemnity costs where a party rejects a Calderbank offer on terms more favourable than judgment.[3] Rather, the making of a Calderbank offer is just one factor that may trigger a court's general discretion, under s24 of the *Supreme Court Act* 1986 (Vic), to award a more favourable costs order.[4]

HAZELDENE – THE TEST OF UNREASONABLE REJECTION

The Court of Appeal in *Hazeldene's Chicken Farm Pty Ltd v Victorian WorkCover Authority (No 2)*[5] (*Hazeldene*) conveniently offered a summary of the policies and principles governing the use of Calderbank offers.

The Court noted (at [21]) the established competing policy objectives of providing an incentive for parties to settle their litigation early, but at the same time not discouraging potential litigants from bringing their dispute to the court by ensuring that an order for special costs should only be made in special circumstances. The Court of Appeal observed (at [23]) that:

"[T]hese competing considerations are sufficiently accommodated by applying a test of (un)reasonableness. The critical question is whether the rejection of the offer was unreasonable in the circumstances."

Acknowledging that it is "neither possible nor desirable to give an exhaustive list of relevant circumstances", the Court of Appeal detailed a number of factors that should be taken into account when considering a submission that the rejection of the Calderbank offer was unreasonable. A court "should ordinarily have regard at least to the following matters:

ILLUSTRATION **GREGORY BALDWIN**

- the stage of the proceeding at which the offer was received;
- the time allowed to the offeree to consider the offer;
- the extent of the compromise offered;
- the offeree's prospects of success, assessed as at the date of the offer;
- the clarity with which the terms of the offer were expressed;
- whether the offer foreshadowed an application for an indemnity costs in the event of the offeree's rejecting it" (at [25]).

Whether it is necessary for an offer to include with sufficient particularity the reasons why the offer should be accepted is the subject of varying judicial opinion[6], and was considered further in *Hazeldene*. Despite holding that it was "neither necessary nor desirable to lay down any general rule in this regard",[7] the Court of Appeal did not completely discount the relevance of the extent to which the reasoning behind the offer should be explained in a Calderbank letter.

While it is not a mandatory requirement to trigger the court's discretion, it would be prudent to explain in some detail the terms and consequences of the offer, particularly where, on its face, it may appear to be a modest offer. Importantly, sufficient explanation surrounding the terms of the offer may assist in the consideration of the degree of compromise and lend to justifying why it was unreasonable in all the circumstances for the offeree to have rejected the offer.

ASSESSING PROSPECT OF SUCCESS

The issue of whether or not it was unreasonable to reject the offer was raised in two cases where the party rejecting the offer argued that it was not in a position at the time the offer was made to properly assess the prospect of success.

In *Pepe v Platypus Asset Management Pty Ltd (No 2)*[8] (*Pepe*), the Supreme Court entertained a claim by the defendant for costs on an indemnity basis; alternatively, on a solicitor and client basis. The basis of the claim was that the unsuccessful plaintiff had failed to better its offers, or had abandoned certain claims. The defendant had made two formal offers and two Calderbank offers.

In exercising his discretion, Almond J considered the factors in assessing reasonableness set out by the Court of Appeal in *Hazeldene*. His Honour accepted that the offers were made at an early stage in the proceedings, allowed sufficient time to accept the offers and were expressed in "sufficiently clear terms" (at [12]). Further, his Honour accepted the defendant's submission that "properly advised, the potential cost consequences of rejecting the offer would have been known to the plaintiff" (at [12]).

The dispute in *Pepe* turned on the proper construction of an employment contract. In particular, the facts surrounding changes to the contract were in dispute and arose out of discussions at a critical meeting held between the parties. The defendant submitted that the plaintiff should be taken to have known his own narrative of events and therefore have been in a position to assess his prospects of success. Almond J disagreed, holding that:

"Whilst the plaintiff must be taken to have known of the narrative of events and his own evidence, in my view it does not follow that the plaintiff was necessarily in a position to adequately assess his prospects of success as at the date of the respective offers. The plaintiff submits that the first time he was apprised of the defendant's evidence relating to the . . . meeting was when Mr Bryant gave evidence in Court. Based on the evidence before me there is force in this submission" (at [13]).

Almond J noted that the outline of evidence of Mr Bryant was "uninformative" and "without descending into the content of the discussion" (at [14]). His Honour also noted that the amounts offered, being $65,000 and $90,000, were relatively small compared to the claim of in excess of $1 million.

In exercising his discretion, his Honour considered the rejection was not unreasonable in these circumstances and declined to make any special costs order against the plaintiff.

In *Mackie Group Pty Ltd v Reading Properties Pty Ltd (No 2)*,[9] a formal offer and a number of Calderbank offers were exchanged between the parties throughout the course of the litigation. The relevant Calderbank letter sought to be relied on by the plaintiff was rejected by a counter offer served by the defendant. Having identified the relevant test of unreasonableness, Byrne J went on to say:

"[T]he focus of the question in this case is whether Reading Properties, and those advising it, were then able at that time to form an assessment of their prospects of resisting the Mackie Group claim" (at [10]).

The defendant submitted that it was not in a position to make such an assessment due to the "confusing state of the plaintiff's pleadings" and "irrelevant and inadmissible content" of the plaintiff's affidavits (at [11]). Noting that the plaintiff's case was a straightforward one and that the factual contest in the matter arose from issues raised by the defendant and therefore within the knowledge of the defendant, Byrne J rejected the protests by the defendant that it was not in a position to assess the strength of the plaintiff's case (at [12], [17]–[19]). He ordered the defendant to pay the costs of the plaintiff on a party/party basis up to the date the Calderbank offer was rejected and thereafter on an indemnity basis.

THE TIME FACTOR

Both the time at which the offer is made and the time allowed for the party to consider the offer are critical in determining the reasonableness of rejecting the offer.

As a minimum, the Calderbank offer would normally be left open for acceptance after service for at least the time provided by a formal offer. Nevertheless, where the offer is not time critical it would be sensible to err on the side of caution and nominate a longer time period for acceptance of the offer, preferably 21 to 28 days. If time is critical, however, a Calderbank offer provides flexibility which cannot be provided by a formal offer. For example, in *Primus Telecommunications Pty Ltd v CCP Australian Airships Ltd*,[10] Habersberger J held that a Calderbank offer made during trial and open for acceptance for less than 24 hours was sufficient for him to award indemnity costs against the defendant.

EXTENT OF COMPROMISE AND EXPLANATION

In the decision of *Kermani v Gaylard & Ors (No 2)*[11] (*Kermani*), the extent of the compromise offered by two separate Calderbank letters served by the defendants, and the explanation given for the Calderbank offers, played a crucial role in informing the judge whether or not it was reasonable in all the circumstances for the plaintiff to have rejected the offer.

There were two relevant Calderbank offers and one formal offer. The first of the Calderbank offers was made at an early stage of the proceedings, in which the defendants offered $30,000 to the plaintiff with each party bearing its own costs (the 2007 offer). The second Calderbank offer was for $120,000 plus costs (the 2009 offer) and a formal offer was made in similar terms.

Sifris J held that the plaintiff did not act unreasonably in failing to accept the 2007 offer because "the offer was too low and was in effect a demand to capitulate" (at [25]).

The plaintiff, in opposing the award for solicitor and client costs, submitted, inter alia, that it was not unreasonable to reject the 2009 offer, as it was significantly less than the amount of claim. His Honour considered the plaintiff was unreasonable in rejecting that offer because that "offer did not amount to a demand to capitulate but rather represented a serious endeavour to resolve the proceedings and was by no means a token amount" (at [23]).

Sifris J also noted that the relevant matters set out in the 2009 offer, explaining why the offer was considered to be reasonable, were

highly relevant so far as inviting the plaintiff to accept the offer, and noted that the plaintiff failed to beat the formal offer which "provides a further reason for awarding solicitor and client costs".[12] His Honour was therefore prepared to award solicitor and own client costs based on the 2009 offer.

LESSONS

The issue of costs and the basis on which costs will be awarded is always within the discretion of the court. The Court of Appeal in *Hazeldene* identified a number of factors which should be weighed up by a court in considering whether or not it should order costs on a basis which is more favourable than the usual party and party costs order. The recent decisions continue to emphasise that a key element underlying every factor is whether or not the offeree was unreasonable in rejecting that offer.

It is apparent that a practitioner preparing a Calderbank offer must turn their mind to the question of reasonableness in all of the surrounding circumstances, and provide an explanation for that offer, if they wish the court to attach any weight to that offer in the exercise of its discretion to award special costs. ●

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1. [1975] 3 All ER 333.
2. Unreported decision, Byrne J, 28 April 1993.
3. See *Jones v Bradley (No 2)* [2003] NSWCA 258 at [5] per Meagher, Beazley and Santow JJ, where the court rejected an earlier line of authority that had suggested a prima facie presumption to an award for indemnity costs in these circumstances.
4. See *Colgate Palmolive Co v Cussons Pty Ltd* (1993) 46 FCR 225 per Sheppard J for a list of circumstances and authorities thought to warrant the exercise of the court's discretion on the question of costs.
5. (2005) 13 VR 435.
6. See *Macquarie Bank Ltd v National Mutual Life Association of Australasia Ltd* (unreported decision, Supreme Court of New South Wales, 27 July 1994) at [4] where the Court held: "There is no obligation upon a party making an offer of settlement in a Calderbank letter to specify with precision the reasons why the opposing party will fail, or should accept the offer in the letter"; *Wenzel v Australian Stock Exchange Ltd* [2002] FCA 353 at [8] per Sundberg J, who held that: "The extent to which a Calderbank letter draws an applicant's attention to the weakness of its case is a consideration relevant to the making of an indemnity order. The letter must descend to particularity"; *NMFM Property Pty Ltd v Citibank Ltd (No 11)* [2001] FCA 480 at [87] per Lindgren J, holding that: "No doubt where a party puts *with sufficient particularity* to the opposing party the reasons why the latter *must fail*, yet the latter does not recognise the inevitable, this will be a factor pointing to an award of indemnity costs".
7. Note 5 above, at [27], where the Court endorsed the words of Redlich J in *Oversea-Chinese Banking Corporation v Richfield Investments Pty Ltd* [2004] VSC 351 at [87] that: "Any attempt to prescribe the reasoning which must accompany an offer should be resisted. Whether there is a need for the offer or to descend to specificity as to why the offer should be accepted must depend upon a consideration of all the circumstances existing at the time of the offer. The extent to which the weakness of a party's position is exposed through the pleadings, affidavits and the various communications between the parties during the course of the litigation may bear upon the significance of the absence of specificity in the informal offer."
8. [2011] VSC 21. The author understands that an application for leave has been filed to appeal from the decision and costs order made by Almond J in the Supreme Court of Victoria. The leave application and any subsequent appeal should not alter the factors set down in *Hazeldene* but may provide further guidance as to the application of these factors.
9. [2010] VSC 205.
10. [2003] VSC 141.
11. [2011] VSC 143.
12. Note 11 above, at [26]. The inclusion of a statement of reasons in a Calderbank offer was subsequently endorsed in *Mediterranean Olives Financial Pty Ltd & Ors v Gita Lederberger & Ors (No 2)* [2011] VSC 333 at [10], where Pagone J held that: "By including such a statement in an offer, the recipient of the letter can be informed of why it might be in their interests to accept the offer. The statement of a reason why an offer should be accepted is a material factor in deciding whether an offer ought reasonably to have been accepted".