Unreasonable refusal to mediate: the need for a principled approach - PGF II SA v OMFS Co 1 Ltd

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Cases cited
PGF II SA v OMFS Co 1 Ltd [2013] EWCA Civ 1288; [2014] 1 W.L.R. 1386; [2013] 10 WLUK 734 (CA (Civ Div))
Halsey v Milton Keynes General NHS Trust [2004] EWCA Civ 576; [2004] 1 W.L.R. 3002; [2004] 5 WLUK 215 (CA (Civ Div))

***C.J.Q. 261** PGF II SA, a freehold owner of a mixed commercial and office building in London, instituted proceedings against OMFS Co 1 Ltd, its tenant of three floors, for breaches of repairing covenants. Damages totaled slightly more than £1.9 million. OMFS denied liability on the basis that the costs of repair would exceed the diminution in value of the reversion in consequence of the defects pursuant to s.18 of the Landlord and Tenant Act 1927 .

PGF attempted to settle the claim by making three Pt 36 offers: £1.25 million at the commencement of the proceedings in October 2010; £1.25 million plus interest on April 11, 2011; and £1.05 million plus interest in December 2011. None of them were accepted. On April 11, 2011 it also made a serious written invitation to participate in mediation, suggesting exchange of information between experts, provision of a copy of s.18(1) valuation, proposed dates of mediation in the next two months, additional candidates as mediators, as well as seeking OMFS's agreement to mediate, explanation for refusal, request for disclosure, dates of availability and list of proposed mediators. It offered to mediate three months later, seeking OMFS's willingness to attend a mediation, available dates and reasons for refusal if applicable. Both invitations were met with complete silence.

On January 10, 2012, one day before the trial was due to start, OMFS applied to amend their defence that the air-conditioning system, which made up about £250,000 of the total claim, did not fall within the demise and therefore it had no liability for the alleged defects. Later on the same day, PGF accepted OMFS's Pt 36 offer, of April 11, 2011, of £700,000 inclusive of interest.

Consequently the only issue that remained for determination was the award of costs from the date of expiry of the relevant period to the date of acceptance of the Pt 36 offer. PGF asked the court to depart from CPR r.36.10(5)(b) for an order that OMFS pay PGF's costs because of late amendment of defence and unreasonable refusal to mediate. [1] OMFS resisted the application on the ground that silence did not amount to refusal and that any deemed refusal was not unreasonable due to the parties' conduct at a previous mediation for an unrelated matter, the absence of expert evidence on diminution in value and no reasonable ***C.J.Q. 262** prospect of a successful mediation. [2] Mr Recorder Furst QC held that silence amounted to a refusal to mediate and such refusal was unreasonable. [3] The judge deprived OMFS of its costs but stopped short of ordering it to pay PGF's costs during the contested period.

The Court of Appeal affirmed the decision of the lower court. Briggs L.J., delivering the judgment, summarised the principles laid down in *Halsey v Milton Keynes NHS Trust* [4] as follows:

> (i) the court should not compel parties to mediate even if it was within its power to do so. This would risk contravening art.6 of the Human Rights Convention, and would conflict with a perception that the voluntary nature of most ADR procedures is a key to their effectiveness;
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> (ii) nonetheless the court may need to encourage the parties to embark upon ADR in appropriate cases, and that encouragement may be robust;
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> (iii) the court's power to have regard to the parties' conduct when deciding whether to depart from the general rule that the unsuccessful party should pay the successful party's costs includes power to deprive the successful party of some or all of its costs on the grounds of its unreasonable refusal to agree to ADR; and
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> (iv) for that purpose the burden is on the unsuccessful party to show that the successful party's refusal is unreasonable. There is no presumption in favour of ADR. [5]

His Lordship then referred to a list of non-exhaustive factors identified in *Halsey* , which are relevant for the court to decide whether a party acted unreasonably to refuse ADR: (a) the nature of the dispute; (b) the merits of the case; (c) the extent to which other settlement methods have been attempted; (d) whether the costs of the ADR would be disproportionately high; (e) whether any delay in setting up and attending the ADR would have been prejudicial; and (f) whether the ADR had a reasonable prospect of success. [6] Despite the fact that their applicability to the facts was hotly debated, not one was useful to determine the issue on appeal: whether silence in face of a serious invitation to engage in ADR is itself unreasonable on the basis that silence amounts to a deemed refusal. As such, his Lordship made a new addition to the *Halsey* guidelines:

"Silence in the face of an invitation to participate in ADR is, a general rule, of itself unreasonable, regardless whether an outright refusal, or a refusal to engage in the type of ADR requested, or to do so at the time requested, might have been justified by the identification of reasonable grounds. I put this forward as a general rather than invariable rule because it is possible that there may be rare cases where ADR is so obviously inappropriate that to characterise silence as unreasonable would be pure formalism. There may also be cases where the failure to respond at all was a result of some mistake ***C.J.Q. 263*** in the office, leading to a failure to appreciate that the invitation had been made, but in such cases the onus would lie squarely on the recipient of the invitation to make that explanation good." [7]

He spelt out two practical reasons for this extension:

"The first is that an investigation of alleged reasons for refusal advanced for the first time, possibly months or even years later, at the costs hearing, where none were given at the time of the invitation, poses forensic difficulties for the court and the inviting party including, in particular, the question whether the belatedly advanced reasons are genuine at all …

Secondly, a failure to provide reasons for a refusal is destructive of the real objective of the encouragement to parties to consider and discuss ADR, in short to engage with the ADR process. There are many types of reasonable objection to a particular ADR proposal which, once raised, may be capable of being addressed. Mediation may be resisted on the basis that some other type of ADR, such as early neutral evaluation, may be equally suitable and preferred by the objecting party. A proposed mediation may be expensive to the other party if, as is usual, the mediator's fees are shared equally. In such a case it is not unknown for the proposing party to offer to bear the whole fee, or for some cheaper form of ADR, including judicial early neutral evaluation or financial dispute resolution, to be provided more cheaply by the court. ADR may be proposed before the other party has the requisite information, a difficulty capable of being addressed either by limited voluntary disclosure, or by ADR at a later date than that proposed.

Difficulties of this kind constantly arise in civil litigation, and the culture is now well-established under which the parties should discuss these difficulties, and seek to narrow their differences, before those which are irreconcilable are put to the court for determination …". [8]

He added:

"This second reason is partly a matter of practicality, but also serves the policy of proportionality. A positive engagement with an invitation to participate in ADR may lead in a number of alternative directions, each of which may save the parties and the court time and resources." [9]

Another novel point that Briggs L.J. decided in this case concerned the exercise of discretion on costs sanctions. In rejecting PGF's cross-appeal for an order that its costs during the relevant period be paid by OMFS, his Lordship qualified principle (iii) as follows:

"the proper response in any particular case may range between the disallowing of the whole, or only a modest part of, the otherwise successful party's costs.

There appears no recognition in the Halsey case that the court might go further, and order the otherwise successful party to pay all or part of the unsuccessful party's costs. While in principle the court must have that power, ***C.J.Q. 264*** it seems to me that a sanction that draconian should be reserved for only the most serious and flagrant failures to engage with ADR, for example where the court had taken it upon itself to encourage the parties to do so, and its encouragement had been ignored." [10]

It is 11 years since the Court of Appeal in *Dunnett v Railtrack Plc* [11] ordered the successful party to bear its own costs in the appeal, because it turned down out of hand the chance of ADR when suggested by the court at a stage before the costs started to flow. Yet litigants continued to express reservation as to the practical benefits of mediation, reluctance to initiate the process and even outright rejection to engage in it. Despite the unpredictability of costs which may well exceed the value of the subject matter in dispute in the civil courts, they were prepared to argue against adverse costs consequences.

The rule of law demands clarity and consistency as to what constitutes unreasonable refusal to mediate. Otherwise court users who came with clean hands or became involved in disputes that are not suitable for mediation may well be deterred from vindicating their rights before a judge for fear of getting worse off as a result of litigation. The *Halsey* guidelines allow flexibility for application in a variety of factual situations. But it also comes with some unavoidable shortcomings. First, no single factor will trump the others. The applicability of all relevant criteria to the particular facts of each case will be heavily contested at the costs stage of litigation. [12] Secondly, the non-exhaustive list is subject to infinite extension, such as unreasonable conduct within a mediation [13] and silence in face of invitation to participate in mediation.

Briggs L.J.'s judgment, in developing the *Halsey* principles and guidelines, emphasised the importance of a principled approach to explain the interrelationship among different factors and justify future amendments. The starting point rests on the costs shifting principle. It requires the court to order the unsuccessful party to pay the successful party's litigation expenses, so that disputants do not become worse off as a result of having to seek court adjudication to assert or defend their civil rights. Logically, the burden lies on the unsuccessful party to justify a departure from the general rule that costs follow event by showing that the successful party acted unreasonably in refusing to agree to ADR. [14]

The extent of costs sanctions is subject to the indemnity principle. Bramwell B. said in *Harold v Smith* :

"Costs as between party and party are given by the law as an indemnity to the person entitled to them: they are not imposed as a punishment on the party who pays them, nor given as a bonus to the party who receives them. ***C.J.Q. 265*** " [15]

In line with the restorative nature of this common law principle, [16] the amount awarded must be no more than not what the successful party is liable to pay his or her legal representatives. By parity of reason, it makes perfect sense to cap the maximum of a costs penalty to the whole of the successful party's costs. [17] However, ordering the successful party to pay all or part of the unsuccessful party costs in case of "the most serious and flagrant failures to engage with ADR, for example where the court had taken it upon itself to encourage the parties to do so, and its encouragement had been ignored" does not sit well with the indemnity principle. It reflects the goal to achieve proportionate justice in the reformed English civil justice system to which we next turn.

The Woolf reforms unveiled a prominent policy to encourage and facilitate disputants to use ADR for earlier settlements, which then formed part of the court's duty of actively managing cases for achieving accuracy limited by the both aspects of the proportionality principle. [18] All the *Halsey* factors and the extension in *PGF* primarily relate to proportionate costs as between the parties. The additional pointer in *Halsey* , the impact of any encouragement that the court may have given in a particular

case,[19] is uniquely relevant to proportionate allocation of judicial resources among all litigants. The court's encouragement may take different forms, ranging from suggestion to one of the parties as in *Dunnett*[20] to the less robust Ungley Order[21] and the strongest order set out in *Appendix 7 to the Admiralty and Commericial Court Guide 2013*.[22] The Court of Appeal in *PGF* could not have intended to award costs to unsuccessful parties if the successful parties merely disregarded the weakest form of the court's encouragement. Such an outcome does not reconcile with *Dunnett* and risks getting too close to compelling truly unwilling parties to refer to their disputes to ADR if imposed. Briggs L.J.'s second novel point demands focus on the conduct of the successful parties and a balancing exercise with other relevant *Halsey* criteria.

In order to effect culture change to embrace ADR more readily in the English civil justice system, it is equally important to inform litigants and their legal representatives of what amounts to reasoned refusal. This principled approach to *Halsey* and its modifications in this ruling aims to do just that.

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Footnotes

1 *PGF II SA v OMFS Co 1 Ltd [2012] EWHC 83 (TCC)* at [25].
2 *PGF II SA [2012] EWHC 83 (TCC)* at [29]–[32].
3 *PGF II SA [2012] EWHC 83 (TCC)* at [43]–[46].
4 *Halsey v Milton Keynes NHS Trust [2004] EWCA Civ 576; [2004] 4 All E.R. 920* .
5 *PGF II SA v OMFS Co 1 Ltd [2013] EWCA Civ 1288* at [22].
6 *PGF II SA [2013] EWCA Civ 1288* at [22].
7 *PGF II SA [2013] EWCA Civ 1288* at [34].
8 *PGF II SA [2013] EWCA Civ 1288* at [35], [37]–[38].
9 *PGF II SA [2013] EWCA Civ 1288* at [39].
10 *PGF II SA [2013] EWCA Civ 1288* at [51]–[52].
11 *Dunnett v Railtrack Plc [2002] EWCA Civ 303; [2002] 2 All E.R. 850* .
12 See, for example, *Daniels v Commissioner of Police of the Metropolis [2005] EWCA Civ 1312* (merits of the case); *Hickman v Black Lapthorn (Costs) [2006] EWHC 12 (QB)* (merits of the case); *Rolf v De Guerin [2011] EWCA Civ 78* (nature of the dispute); *Swain Mason v Mills & Reeve [2012] EWCA Civ 498* (merits of the case); *ADS Aerospace Ltd v EMS Global Tracking Ltd [2012] EWHC 2904* (Other settlement methods attempted, delay and merits of the case).
13 *Carleton (Earl of Malmesbury) v Strutt & Parker (A Partnership) [2008] EWHC 424 (QB)* .
14 *Halsey [2004] EWCA Civ 576; [2004] 4 All E.R. 920* at [13].
15 *Harold v Smith [1850] 5 H. & N. 381* at 385.
16 Adrian Zuckerman, "The Costs Indemnity Principle - From Restoration to Blame" (2008) 27(3) C.J.Q. 281, 282.
17 *Halsey [2004] EWCA Civ 576; [2004] 4 All E.R. 920* at [13]; *PGF II SA v OMFS Co 1 Ltd [2013] EWCA Civ 1288* at [51].
18 John Sorabji, "Prospects for Proportionality: Jackson Implementation" (2013) 32(2) C.J.Q. 213, 223–224.
19 *Halsey [2004] EWCA Civ 576; [2004] 4 All E.R. 920* at [29].
20 *Dunnett [2002] EWCA Civ 303; [2002] 2 All E.R. 850* at [7].
21 *Halsey [2004] EWCA Civ 576; [2004] 4 All E.R. 920* at [32].
22 *Halsey [2004] EWCA Civ 576; [2004] 4 All E.R. 920* at [30].

