PGF II SA V OMFS Company 1 Limited [2013] EWCA Civ 1288

Or

Yet another reason to mediate (or is mediation now mandatory?)

On 23rd October, the Court of Appeal handed down this important judgment which extends the previously understood principles governing the costs consequences of a failure to mediate. It is an important judgment for litigators as it puts the conduct of litigation when offers to mediate are made firmly in the spotlight when it comes to recovery of a client's costs, and may very well render mediation, and/or raise a perception that mediation is, effectively mandatory whenever one side (or the court) invites it.

The actual point of principle

The appeal raised for the first time the question of what the court's response should be to a party which, when invited to mediate, simply failed to reply. It has long been established that an unreasonable refusal to mediate should be penalised in costs, but what should the court do if a party simply doesn't respond to an offer? The conclusion was that this too is an instance where a court can deprive a party of costs to which it might otherwise be entitled. The court went further and found that in some circumstances, it might even justify a reversal of the liability for costs; and also made significant pronouncements as to how the courts should now approach a refusal to engage in alternative dispute resolution (ADR).

The facts in brief

The Claimant was a landlord of a substantial office block and the Defendant a former tenant of part of that block. At the end of the tenancy, the Claimant had a claim for dilapidations against the Defendant. The fact of wants of repair was not in dispute, although the Defendant's liability to pay for them and quantum was in dispute (because of the operation of statute (s18 Landlord and Tenant Act 1927)). The claim was for £1.9m and the defence denied liability entirely. Shortly after proceedings commenced, the Claimant made a part 36 offer that it would accept £1.125m. After disclosure, this was increased to £1.125m plus interest. At the same time a reasoned letter inviting the Defendant to mediate was sent. It acknowledged that the Defendant would wish to see the Claimant's disclosure and proposed a meeting between experts in advance of the mediation as well as offering the Defendant sight of the Claimant's s18 valuation. It proposed dates and possible mediators.

Coincidently, on the same day, the Defendant made a part 36 offer to pay £700,000. No reply to the invitation to mediate was sent. Nor did the Defendant reply to a chaser letter.

Some months later and a few weeks before trial, the Claimant made a further part 36 offer to accept £1.05m plus interest. Then, the day before trial, the Defendant gave notice of its intention to amend its Defence to take the point that the air conditioning (in respect of which c£250,000 was claimed) was outside the demise (and so that there was no duty to repair it). The Claimant replied by accepting the Defendant's original Part 36 offer of £700,000. In the letter of acceptance the Claimant argued that the normal cost consequences (i.e. payment by the Claimant of the Defendant's costs from 21 days after the offer) should not apply because of the late amendment to the Defence, an argument that did not find favour in court the next day (and no appeal was brought as to that).

However by the next day, the Claimant had thought of a further argument, namely that the normal cost consequences should not apply because of the Defendants' silence in the face of an offer to mediate. The Claimant argued that rather than it being liable for the Defendant's costs, the Defendant should pay its costs.

The judgment at first instance

The court found that many civil disputes were suitable for mediation based on encouragement in the Woolf reforms, the CPR and the Division practice guides and on support from Government. It also found that the focus on the Jackson report on litigation costs and on the need for proportionality was further support for mediation as was the constraints on the provision of state resources for the conduct of civil litigation.

The court found that the Defendant's silence did amount to a refusal to mediate notwithstanding its submissions to the contrary and further that the refusal was unreasonable; and concluded that it would be "unjust" (for the purposes of CPR36.14(4)) for the Claimant to pay any of the Defendant's costs for the period following the 21 days after the Defendant's Part 36 offer, and so that the usual Part 36 consequence in the Defendant's favour would not apply .

The Court of Appeal's view

The Court of Appeal gave an unequivocal endorsement to the view given in the ADR Handbook that silence in the face of an invitation to participate in ADR is, as a general rule, of itself unreasonable. That is so even if a refusal to mediate might have been reasonable if the receiving party had engaged with the request in a meaningful way.

The court found that the *Halsey* test for unreasonableness of a refusal to mediate was not purely objective but was properly coloured by the party's (reasonable) perceptions at the time the offer was made.

Further, a failure to provide reasons for a refusal was unhelpful to the real objective of encouraging the parties to consider and discuss ADR. The court pointed out that discussions between legal advisors and experts at various stages in the litigation process are now an accepted part of the litigation landscape. However, it expressed scepticism as to "reasons" for refusing to engage in ADR which were only first formulated when the parties came to argue costs.

Additionally the court considered that a discussion around ADR may fully settle a case, partially settle it or lead to some other conclusion for the more efficient and cost effective way to progress litigation which would result in the better allocation of valuable court resources.

The court was unsympathetic to the suggestion that having made a part 36 offer, which ultimately was accepted, the defendant had shown its belief in its case and that the subsequent acceptance illustrated that belief was reasonable.

The court also rejected the idea that the parties were too far apart for mediation to be successful saying that the point about the air conditioning, discovered by the parties at the last moment was "*precisely the sort of insight which a trained and skilled mediator, experienced it the relevant field, can bring to an apparently entrenched dispute".*

The court did however agree with the Defendants that a refusal to engage in a discussion about mediation does not produce an automatic costs penalty. It is simply part of the balancing exercise for the court. In particular it rejected the Claimant's submission that it should be paid its costs (i.e. the consequences of the acceptance of the part 36 should be reversed) saying that this should be reserved for the most serious cases, for example where one party refuses to engage even after an indication from the court that it should do so.

On the other hand, the court held that the decision "*sends out an important message to civil litigants, requiring them to engage with a serious invitation to participate in ADR, even if they have reasons which might justify a refusal, or the undertaking of some other form of ADR, or ADR at some other time in the litigation*." It went on to say that the "*court's task in encouraging the more proportionate conduct of civil litigation is so important in current economic circumstances*" that while the sanction chosen by the first-instance judge was "*a little more vigorous than I would have preferred*" it "*operates pour encourager les autres*."

Accordingly it did not disturb the discretion of the trial judge that each party should bear their own costs (for the Post Part 36 offer period).

Practice points

The first and most obvious is that a party in future ignores, or refuses, an offer to mediate at its peril. Whilst the Court was clear that there would be occasions where simply not responding might be appropriate, these are likely to be few and far between. Although the court may have implied that a more common order would have been a deprivation of some of the costs of the successful party, the words "pour encourager les autres" are very significant.

Secondly, the Court did agree with the Defendant that one would have expected the Claimant to complain about the silence, suggesting in correspondence that it amounted to a refusal or raising the matter at the directions hearing before the court. Doing so can be seen as good practice in the future.

Thirdly, the court itself may state that the dispute appears to be suitable for mediation, and if mediation is then refused the relevant refusing but successful party may even have to pay its losing opponent's costs (or some of them).

Fourthly, if mediation (or other ADR) is to be refused (or its consideration is to be deferred), then the refusing party needs to be careful to craft and supply persuasive reasons for the refusal (or deferment) without delay. It is not sufficient to raise those points much later, for example when arguing costs after judgment at trial.

Fifthly, the court did refer to other forms of ADR such as early neutral evaluation and financial dispute resolution. Apart from the family law context (where judicial financial dispute resolution is a mandatory element of the judicial process), it is suspected that these are not and will not be much used. The court's thought that mediators will raise their own points has perhaps not been the usual perception of a mediator's role to date, although there is currently much debate about whether a more evaluative element should enter the mediation process. This is perhaps a judicial suggestion that it would be useful for this to be more commonly used. Obviously, mediators' raising their own points has long formed a helpful part of "reality testing" and provided it does not detract from the important perception of the mediator's neutrality, the authors can see the advantages in using this technique. However, what is most important is whether this decision will lead to a further shift in (i) litigators' and (ii) the court's approach to proposals to mediate. The court of appeal appears to have decided that the default option is now to impose sanctions in the event of a refusal to mediate. It is likely that there will be a further psychological shift in litigators' perceptions towards regarding mediation as effectively becoming a mandatory part of a full litigation process.