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Nik Ivanov,
Vice President, SKULD North America Inc. 757 Third Avenue, New York, NY 10017

PART 36 / Sealed offers – the English Law experience

1. Introduction

A **Part 36 offer** (a settlement offer made under Part 36 of the Civil Procedure Rules) **in** English litigation and the largely equivalent sealed offer (or **"WPSATC"** offer) in London arbitration are formal settlement offers made by an offeror in a specific form which will attract specific consequences in circumstances where the offeree does not accept the offer and subsequently fails to beat the offer in litigation/arbitration.

A Part 36 offer has been described as "*one of the most, if not the single most, effective tool in promoting settlement of disputes*" available to parties in legal process.

It has become so valued a tool that English solicitors will make such offers as a matter of course in handling disputes. They are common and very effective. However, they are also a concept that apparently mystifies many US lawyers and which seems to still be viewed with mistrust by much of the US maritime bar.

Benefits of a Part 36 / Sealed offer

(1). The promotion of settlement (equal measures *carrot* and *stick*). The costs consequences arising from rejection are a powerful incentive for the offeree to seriously consider a settlement.

(2). Effective tool for initiating or re-igniting reasonable settlement dialogue ("*the fear factor*").

(3). No prejudice for making the settlement offer. The confidential nature and non-disclosure of the offer helps protect the parties' respective positions in the legal process.

(4). Preventing (or at least discouraging) over-ambitious claims by claimants or entrenched "all or nothing" thinking by defendants.

(4). A means of costs protection for defendants whereby defendants can guard against costs liability in circumstances where a claimants' claim is over-stated or excessive.

(5). A means of costs protection for claimants (given the emergence of more complicated costs orders) whereby a claimant can guard against adverse costs consequences where multiple claims are advanced with varying degree of merit. For example, claimant may be prepared to settle for less but does not want to abandon claims with unilaterally

(6). Insurance perspective: Liability insurers (for example FDD insurers providing support for legal costs) may be more inclined to support an assured claim on the basis that effective costs protection can be put into place prior to proceeding in litigation/arbitration.

2. What is necessary for the process to be effective.

Essentials to the process:

(1) Certainty of Process

– both parties MUST understand the required process (- i.e. what is necessary to ensure an *effective* offer).

(2) Certainty of Consequence

- both parties MUST understand the consequences of accepting or ignoring/rejecting the offer. The offeror must be able to rely on the consequences affixed to the offer in order to pitch the offer correctly and the offeree must understand the risks in not accepting the offer. Effectiveness of the process requires each party to understand the risks and rewards tied to the offer.

(3) Uniformity and consistency of application

- Judges and arbitrators generally understand that the consequences following an offer must be applied consistently (with some, but limited, flexibility) in order for the process to be effective.

The underlying common law principle: "Costs follow the event"

The successful party in legal proceedings is entitled to recover its legal costs on a reasonable and proportionate basis (**standard basis**) from the losing party. The general rule is that a successful party is a party that is adjudged or awarded a recovery from the other party.

3. English Courts: Part 36 Offers in Practice.

Governed by Part 36 of the Civil Procedure Rules

(1) Certainty of Process:

- Can be made by a claimant or a defendant.
- Can be made at any stage, including before commencement of proceedings **(CPR 36.7).**
- The settlement must be a genuine offer to settle (as opposed to a tactical offer made purely to attract Part 36 costs consequences)
- The offer must be made in accordance with the strict requirements of Part 36 **(CPR 36.5, CPR 36.6).**
  - In writing;
  - It must state that it is made under Part 36 of the CPR
  - Must state a period of acceptance not less than 21 days ***(the relevant period)***. **(CPR 36.5.1)**

Prior to 2015, an offer that specified it was open for acceptance only for a certain period, after which it would automatically expire, was considered invalid under Part 36. However, the CPRs were amended in April 2015 to allow Part 36 offers to automatically expire in not accepted by a certain date (after *the relevant period*).

- Interest: To be effective, a Part 36 offer must include interest up to the date on which *the relevant* period expires, and also include future interest up to payment. This is usually presented as part of the settlement figure: ***King v City of London*** [2019] EWCA Civ 2266 and subsequent amendments to the CPRs from 2015 **(CPR Rule 36.5(5)).**

- Costs: To be effective, a Part 36 Offer must include an offer to pay the other side's costs (in an amount to be assessed by the Court if not agreed) up to the date of acceptance or expiry of the relevant period (whichever is sooner).

(2) Certainty of Consequence:

(i). **The settlement offer is accepted** - no order for costs **(CPR Rule 36.13)**

(ii) **Defendant makes an offer and claimant fails to accept offer** (three possible scenarios):

- Defendant is successful in defending the claim:
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  - Defendant recovers its costs from claimant on a standard basis.

- Claimant fails to accept the defendant's offer and the claimant obtains a judgment "more advantageous" than the offer. Claimant "beats the offer" and recovers a sum that is more than the offer (i.e. the claimant was justified in not accepting the defendants offer)

  - Claimant entitled to recover its costs from defendant on a standard basis.

- Claimant fails to accept the defendant's offer and the claimant obtains a judgment "less advantageous" to it than the offer. Claimant fails to "beat the offer" and recovers a sum that is less or equal to the offer (i.e. the claimant should have accepted the defendants' offer)

  - Claimant entitled to its costs on a standard basis up to the expiry of the *relevant period*.
  - Thereafter, claimant is responsible to pay its own costs and cannot recover these from defendant (even though the claimant made a recovery in the proceedings)
  - Defendant is entitled to recover from the claimant its legal costs on a standard basis from the date on which *the relevant period e*xpired and
  - Defendant is entitled to standard interest on those costs.
    (CPR Rule 17)

In short: if the claimant make a recovery, but the recovery is not enough to "beat" the offer, Part 36 effectively reverses the general costs rule and the defendant is treated as the "successful party" from the date of expiry of the relevant period.

(iii) **Claimant makes an offer and defendant fails to accept offer** (three possible scenarios)

- Defendant is successful in defending the claim

  - Claimant is responsible for paying defendant's costs on a standard basis.

- Defendant fails to accept the claimant's offer and the claimant obtains a judgment in its favor but one that is "less advantageous" than the offer. Defendant has "beaten the offer" (i.e. the defendant was justified in not accepting the claimant's offer but is still the losing party in the litigation).

  - Claimant entitled to recover its costs from defendant on a standard basis (general rule of "costs following the event" applies)

- Defendant fails to accept claimant's offer and the claimant obtains a judgment "equal to or more advantageous than the offer. Defendant fails to "beat the offer" (i.e. the defendant should have accepted the claimants' offer).

  - Claimant entitled to its costs on a standard basis up to the expiry of the *relevant period* plus interest on those costs.
  - Claimant entitled to its costs **on an indemnity basis** for the period starting after expiry of *the relevant period*.
  - Claimant entitled to interest on the sum awarded to the claimant at an enhanced (penalty) rate **up to 10% above base rate** from the date of expiry of the relevant period;
  - Claimant entitled to interest on the indemnity costs awarded at an enhanced (penalty) rate **up to 10% above base rate**.
  - Claimant entitled to an additional amount (effectively a fine) capped at £75,000, calculated by applying a prescribed percentage on the amount of damages/costs awarded by the Court **(CPR 36.17(7))**

At first glance Part 36 appears quite generous. However, it is designed to provide claimants with an incentive for settlement given that claimants would recover costs on a standard basis anyway if their claim is wholly or partially successful.

General

The English Court will generally approach the above costs consequences as automatic, but may vary the application of above rules if it considers it would be "***unjust to do so***". For example the Court may take into account the conduct of the parties, other settlement offers etc when considering the appropriate consequences that should be applied.

Examples

Shah v Shah [2021] EWHC 1668 (QB)

Global Energy Horizons Corporation v Gray [2021] EWCA Civ 123

> *"Where a defendant is faced with an exorbitant claim which he wishes to defend vigorously but where he is vulnerable to a finding that he is liable for a much smaller amount, there is a clear process provided by CPR Part 36 which he can follow to protect his position"*

Other Considerations

- Multiple and/or competing Part 36 offers can be (and often are) made by parties;
- Circumstances when Part 36 offers may not be appropriate:
  - All or nothing cases – no effective costs protection to be gained.
  - Parties want to settle for a single lump sum – and avoid lengthy costs assessments.
  - Multiple defendants
  - Flexible / non-monetary resolutions – e.g. deals on future business / set offs etc.
  - Complicated claims/counterclaims

4. London Arbitration : Sealed offers (WPSATC / Calderbank offers)

CPR Part 36 is not directly applicable or binding on arbitration but provides *general principles* and *useful guidance* to an arbitral Tribunal. A Tribunal has a broad discretion under Section 61 of the Arbitration Act 1996 to assess costs taking into account the circumstances and taking into consideration what was reasonable and proportionate:

> Section 61
> *(1) The tribunal may make an award allocating the costs of the arbitration as between the parties, subject to any agreement of the parties.*
>
> *(2) Unless the parties otherwise agree, the tribunal shall award costs on the general principle that costs should follow the event except where it appears to the tribunal that in the circumstances this is not appropriate in relation to the whole or part of the costs.*

In practice, LMAA generally followed the form of Part 36 with two clear distinctions:

1. The LMAA does not have the power under its Rules to award "fines" or penalty interest (at 10% above base);

2. The LMAA were keen to preserve a greater measure of flexibility in the Tribunal exercising is discretion on costs issues.

Therefore, in respect of the consequences the consequence following a Claimants sealed offer, when considering sanctions Tribunal's are generally limited to ordering indemnity costs.

The dilemma

Prior to 2017 there was an increasing tendency for English solicitors to frame their WPSATC offers in LMAA arbitration as "Part 36 offers" (and referencing Part 36 sanctions) as a matter of course and rather blindly assume that they applied to arbitration when they did not.

The LMAA were acutely aware of the need to distinguish LMAA practice from formal Part 36 offer Procedure. At the same time they recognized the benefit in preserving the general system offered by Part 36, in particular the consistency and certainty of practice which provided an *"extremely effective and necessary tool in the armoury for efficient dispute resolution*".

Solution and current approach

The LMAA considered it important to make it clear that, while there might be some generally parallel scheme in arbitration, it was not Part 36.

To address this, in 2017 the LMAA revised its terms to include the following:

> LMAA Rules 2017 (Second Schedule):
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> *19. ….For the avoidance of doubt, the English High Court procedure as to Part 36 offers is not applicable to arbitrations conducted under these Terms, and paragraph (b) above is not intended to limit the matters which may be considered by a tribunal in the exercise of its discretion.*

The amended terms provide no guidance as to the applicable practice when awarding costs and simply leave this as a matter of discretion.

However, the intention was not made to signal any major change in practice – rather to clear up misunderstandings and ensure that the LMAA were not constrained by Part 36 procedure, and instead reserved a measure of flexibility.

As a consequence, there has not been a significant change in approach by the LMAA since the 2017 revision to the Terms. The upshot now is that Part 36 procedure is generally followed in principle, with the sanction for claimants' offers being indemnity costs (rather than penal interest and fines). There has been, perhaps, a general reluctance to award indemnity costs too readily (although that reluctance may be changing as several LMAA arbitrators have confirmed that they are now more readily willing to award indemnity costs). The LMAA now rarely see offers referring to Part 36. What happens instead is that routine correspondence is headed WPSATC.

5. Sealed offers in Hong Kong arbitration.

Starting point is that an arbitral Tribunal can include in its award directions as to the costs of arbitral proceedings (Arbitration Ordinance *section 74(1),*): The Tribunal will generally follow the approach that costs follow the event.

However, the Tribunal will give regard to "all relevant circumstances" and the Tribunal is empowered with a broad power in respect of how it approaches/awards costs. The principles it applies broadly reflect the same principles and approach adopted by English arbitral proceedings. In particular:

- Whether a written offer of settlement has been made (*section 74(2), AO*).
- Whether parties were successful on all or some of its claims,
- Whether the offeree should have accepted the earlier offer made in light of the outcome of the arbitration – i.e. the concept of whether the offer has been "beaten"

En Po Kwong v Chinney 2005: This Judgement sets out in some detail how costs should be dealt with given a sealed offer situation in domestic Hong Kong arbitration. It acknowledges that sealed offers / Calderbank offers are widely accepted as valid in international and maritime arbitration, and that the same principles and consequences should apply in Hong Kong arbitration. There are some variances in procedure. However, essentially the main takeway is that Caderbank offers are generally supported in Hong Kong but will depend on all the facts and should be considered by the Tribunal.

https://jusmundi.com/en/document/decision/en-po-kwong-marble-factory-ltd-v-chinney-construction-company-ltd-judgment-of-the-high-court-of-hong-kong-2005-hcct-7-2005-friday-8th-july-2005

For more detail, a useful article is below:
https://www.lexology.com/library/detail.aspx?g=02d13304-4148-4d8b-8fe8-487bf88b3589

6. Sealed offers in Singapore arbitration.

Morgan Lewis' Brief Guide to Singapore Arbitration (2018):
https://www.morganlewis.com/-/media/files/supplemental/2018/international-arbitration-guide_singapore_180640.pdf?rev=e447a0ef8f74436e8ee83dfff8a031eb&hash=2ABDC34092BB2875D8CCD664966F459A

> *'Calderbank' or 'Sealed' offers are commonly used in arbitration where the terms of a settlement offer are made on a without-prejudice basis. If the tribunal subsequently awards the offeree an amount which is less favourable than the Calderbank Offer, the offeror may disclose the existence and terms of the Calderbank Offer to the tribunal for an order that the offeree pays the offeror's costs incurred from the date of the offer on the basis that the offeree should have accepted the Calderbank Offer when it was made. Had the offeree accepted the Calderbank Offer, the costs of the proceedings incurred by the offeror after the date of the Calderbank Offer would have been saved.*
>
> *Although commonly encountered in arbitration proceedings, the concept of a Calderbank Offer is not formalised in the major sets of arbitration rules, or in the IAA or AA. Arbitral tribunals are generally given the broadest discretion as to costs, subject to any other agreement by the parties. There is no reason in principle why such discretion should not extend to considering whether costs consequences should follow from the fact that a Calderbank Offer was made by one party to the other before or in the course of a proceeding. Are arbitration proceed*

In short: the concept of a Calderbank offer in English arbitration is generally adopted and accepted in Singapore arbitration, together with the resulting cost consequences. The English position is largely similar to or carries weight in the context of a Singapore arbitration. The existence of a Calderbank offer is one of the factors which a Singapore tribunal will consider in exercising its discretion on the issue of costs. The tribunal will of course take into account of all the circumstances of the case.

This factor has also been recognised recently in the Singapore Chamber of Maritime Arbitration Rules 4th Ed (2022) at Rule 39. Although it does not go so far as to set out the cost consequence, it provides for any unreasonable refusal to accept a settlement offer to be taken into account when it comes to costs.

> **39.4** When deciding which party shall bear the costs of the arbitration and the legal or other costs of the parties, and the amounts of all such costs, the Tribunal may take into account any unreasonable refusal by a party to participate in mediation and/or accept any settlement offers that were made. Any party may before a final Award is made, provide notice of any settlement offer that has been made in the course of proceedings and the disclosure of such settlement shall be made in accordance with the Tribunal's directions.