Will this new matrix control litigation costs?

Natalia Siabkin and Suzanne Farg discuss the impact of the reforms five months after implementation

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'It remains to be seen whether the new rules will reduce the costs of litigation by curbing unnecessary costs or will have the more detrimental effect of preventing litigants from pursuing their claims fully (or at all).'

The new Jackson toolkit for reining in litigation costs arrived on 1 April 2013, as set out in the Civil Procedure (Amendment) Rules 2013 and accompanying Practice Directions. 'Costs Management' is the new concept. Proportionality and compliance, backed by the courts' powers to give relief from sanction, have been with us for some considerable time but have now received transformative makeovers.

How are lawyers to interpret the changes to be able to continue acting in the best interests of their clients and will these changes serve the intended purpose of controlling litigation costs?

Proportionality: value trumps all?

Proportionality features as a pervasive approach within the rules, but also provides a specific basis for assessing the extent to which litigation costs can be recovered. It is part of the usual standard basis of assessment between the parties. New 'proportionality' applies to cases issued from 1 April 2013 onwards (CPR 44.3(7)). Where cases involve work undertaken prior to 1 April, costs incurred for such work will be assessed under the previous concept of proportionality and only work undertaken from 1 April will be assessed under the new proportionality provisions. This means that detailed assessment bills for cases issued from 1 April will have to be partitioned with pre-1 April work in one part and work from 1 April in another. Within one bill, costs could be assessed under the different concepts of proportionality with different outcomes, though it is difficult to envisage how new proportionality could avoid affecting the overall cost recovery.

'Old-style' proportionality was the subject of guiding principles in practice directions (previous CPR 44PD.5), which stated that:

- the relationship between total costs incurred and the financial value of the claim may not be a reliable guide;
- there would be costs inevitably incurred which are necessary for the successful conduct of the case;
- solicitors should not be required to conduct litigation at uneconomic rates; and
- in a modest claim the proportion of costs are likely to be higher than in a large claim such that they may even equal or possibly exceed the amount in dispute.

This guidance has disappeared and instead CPR 44.3 confirms that:

- proportionate costs will bear a reasonable relationship to the value of what is in issue, the complexity of the case, additional work caused by the conduct of the paying party and wider factors such as reputation or public importance; and
- costs that are disproportionate may be disallowed or reduced, even if they were reasonably or necessarily incurred.

Does the change suggest an expectation that overall costs should

not ordinarily exceed the value of what is in issue?

As an example of the 'modest' claim envisaged by the previous practice direction this could be a mid-value multi-track clinical negligence claim where the complexity requires the involvement of a number of experts. Depending on how far steps have to be taken to establish liability and quantum, the recovery of damages in the region of £75,000 could quite possibly generate overall costs of £140,000. While CPD44.5 would have provided a more circumspect response to the paying party's challenge for proportionality, the new overriding object of dealing with cases at proportionate cost is likely to make these costs a more open target. All the more so, if the 'sums in issue in proceedings' mentioned in CPR 44.3 are interpreted as referring to the final award and not to a reasonable valuation of the likely damages made at the outset.

In addition to the April 2013 changes, the Civil Justice Council Costs Committee is under direction to conduct a comprehensive evidence-based review of the nature of the guideline hourly rate and to recommend new (and not necessarily increased) guideline rates specific to different areas of civil litigation. These recommendations are expected by the end of March 2014.

When presented with an argument of proportionality under the previous rules, the court in *Lownds v Home Office* [2002] first considered whether the total costs were disproportionate to the value of the claim, before going on to look at whether individual costs items had been both reasonably and necessarily incurred. This was propounded as a two-stage approach so that, if globally the costs indicated disproportion, individual items had to satisfy the test of necessity as a higher bar than reasonableness. If, in the example mentioned, the outcome of a review of necessity of the items claimed in a bill resulted in costs reduced to £115,000 there would have been no further enquiry. Now, in the name of proportionality, the rules enable the court to disallow or reduce reasonably or necessarily incurred costs. Could there be a '*Lownds* plus one' or three-stage approach whereby, once the filter of necessity has been applied, another global view is taken of what is proportionate and the £115,000 is further reduced with possibly some recognition of the complexity involved?

The risk is that where costs exceed the value of the claim, recovery from the paying party is going to be more closely aligned to the claim value or the amount recovered and it remains to be seen how this is mitigated by the other mentioned factors of complexity, conduct of the parties and public importance. At the time of preparation of this article there are no reported decisions to shed more light on how proportionality will be interpreted in practice. While uncertainty is likely to breed more caution, there is the spectre of further potential costs to be incurred in order to establish what the new concept of proportionality will really mean for clients, lawyers and their costs.

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Compliance/relief from sanction: fewer second chances

CPR 3.9, which confirms the court's powers to provide relief from sanction, is still based on consideration of all the circumstances. However, the previous 'shopping list' of factors to be taken into account, which included matters such as relative prejudice, intention and explanation, has been reduced to two factors namely, the need:

- for litigation to be conducted efficiently and at proportionate cost; and
- to enforce compliance with rules, practice directions and orders.

Judges are being exhorted to take a tougher approach in respect of issues of compliance and it is no longer clear that balancing relative prejudice between the parties will be as important as the new imperative to control litigation costs and enforce compliance to this end.

In *Fred Perry (Holdings) Ltd v Brands Plaza Trading Ltd* [2012] Jackson LJ struck out a defence for non-compliance and said 'there is a concern that relief against sanctions is being granted too readily', and 'Litigants who substantially disregard court orders or the requirements of the Civil Procedure Rules will receive significantly less indulgence than hereto'.

While Coulson J permitted the amendment of a cost budget under one of the cost management schemes in *Murray v Neil Dowlman Architecture Ltd* [2013] , he restricted the basis of his decision to the 'unusual facts' and confirmed that it would:

> ... no longer be possible in the ordinary case for parties to avoid the consequences of their own mistakes simply by saying that the other side has not suffered any prejudice as a result.

After 1 April 2013, HHJ Pelling QC sitting as a High Court judge in *Fons HF v Corporal Ltd* [2013] came very close to refusing an extension of time to both parties who had failed to file and serve witness statements in breach of an Order, stating that if the witness statements had been served in time it would have become clear that the trial listing of five days was far too long. He warned that:

> ... the wider litigation world should be aware that all courts at all levels are now required to take a very much stricter view of the failure by parties to comply with directions, particularly where the failure to comply is likely to lead into a waste of the limited resources available to those with cases to litigate.

The *Solicitors' Journal* also highlighted a case headlined as a victory by defendants' solicitors ('Weightmans claims first post-Jackson relief from sanctions victory', May 2013) where relief from sanction was refused, denying the claimant an extension of time to serve particulars of claim. The judge referred to radical amendment of CPR 3.9 and indicated he was taking

a stricter approach to non-compliance commenting that 'the claimant has taken quite long enough to bring these proceedings and enough is enough'.

Costs management: controlling costs and providing certainty?

The creation of specific costs management rules provides a framework for the court to actively manage the costs of litigation. The new rules can be found at CPR 3.12-3.18, together with associated practice direction 3E, and will apply to most types of multi-track cases commenced on or after 1 April 2013, including personal injury and clinical negligence claims. The rules require all parties to the litigation to file a budget of their estimated costs. A prescribed format (Precedent H) and guidance notes regarding completion of the budget (split into phases of litigation from pre-action to settlement) are annexed to the practice direction. The sanction for failing to file a budget is intentionally draconian: any party that does not file a budget as directed will be treated as having filed a budget comprising only the applicable court fees.

It is notable that the court's costs management powers are not intended to be retrospective and only those costs to be incurred after the date of the budget can be approved by the court. However, the court may record its comments on costs already incurred and take them into account when considering the reasonableness and proportionality of future costs.

The importance of preparing a comprehensive and realistic budget at this stage cannot be overestimated. On considering an overspend by the receiving party in the recent costs-budgeted case of *Elvanite Full Circle Ltd v AMEC Earth Environmental (UK) Ltd* [2013] in the Technology and Construction Court, Coulson J commented that:

> ... proper practice requires the budget to be prepared on the basis that all of the pleaded issues are in dispute... In the absence of any stated qualification in the costs budget, the court is entitled to assume the comprehensive nature of the figures put forward.

It is likely to be difficult to remedy, at a later stage, mistakes or omissions in the budget and therefore, it is necessary for the parties to carefully plan their case strategy at an early stage and include in the budget accurate estimates of all anticipated costs, including experts' fees, counsel's fees and other disbursements. While not specifically referred to, it would appear that in appropriate cases this may also include any potentially recoverable additional liabilities (such as an ATE insurance premium in connection with the cost of experts' liability reports in a clinical negligence claim).

While uncertainty is likely to breed more caution, there is the spectre of further potential costs to be incurred in order to establish what the new concept of proportionality will really mean for clients, lawyers and their costs.

Once the parties' budgets have been exchanged and filed, the court is likely to make a 'costs management order' (CMO). The sections of the budgets which are agreed between the parties will be recorded in the CMO and the court will review and revise any parts which are not agreed and then record its approval in the CMO. The court is not required to make a CMO in every case but, if it does so, the court will thereafter control the parties' budgets in respect of recoverable costs.

The key question is how the court will set the level of the budget. The practice direction indicates that the intention is not for the court to undertake a detailed assessment in advance. However, it is also acknowledged that judges may have to drill down to the constituent elements of the costs in order to set the budget. Therefore, it is likely to be necessary for parties to provide to the court details of how the total estimated costs of each phase have been reached. It is not yet clear whether the court will look at overall costs per phase or more detailed information such as estimated time, hourly rates and disbursements. However, it is notable that in *Troy Food v Manton* [2013] (to which a costs budgeting pilot scheme applied) HHJ Kaye QC gave consideration to factors including the hourly rate of counsel when setting the budget.

Subsequently, the court will take into account the parties' budgets before making any case management decisions and will not give a direction if, by doing so, it will make the costs of a particular phase of the proceedings disproportionate. This may mean that a party's ability to take essential steps in their claim could be subject to greater restrictions under the court's new costs management powers.

On assessment of costs at the conclusion of a case under a CMO, the court will have regard to the receiving party's last approved or agreed budget and will not depart from the budget unless satisfied that there is good reason to do so (specifically taking into account costs proportionality). It remains to be seen whether this will lead to a decreased requirement for detailed assessment, for example if courts become more able to summarily assess costs simply by reference to a budget. However, detailed assessment may still be required in connection with costs which predate the budget and is likely to be required if the receiving party has overspent and seeks to argue that there is good reason to depart from the budget.

The effect of costs budgeting will gradually become clearer as claims are litigated under the new costs management rules. Currently, guidance regarding the approach to be taken by the court in implementing these rules is scarce and the available authorities come from similar (but not identical) cost management pilot schemes.

In *Henry v News Group Newspapers Ltd* [2013] (a case litigated under the defamation pilot costs management scheme) the Court of Appeal found that there was a good reason to depart from the approved costs budget. However, this authority is likely to have limited application going forwards as the court also distinguished the provisions of the pilot scheme from the new costs management rules. Moore-Bick LJ

warned that the court would in future be slow to deviate from an approved budget and commented that there should be a 'particular emphasis on the function of the budget as imposing a limit on recoverable costs'.

Conversely, in *Troy* permission to appeal has recently been granted in respect of a costs management order, where the defendant's grounds of appeal include an argument that the judge has been too generous in approving parts of the claimant's budget. The appeal in this case is likely to consider issues surrounding the way in which a budget is set and the scope for departing from the approved budget at detailed assessment.

In the recently decided case of *Elvanite Full Circle Ltd v AMEC Earth Environmental (UK) Ltd* [2013] (also litigated under a costs management pilot scheme), Coulson J provided guidance that is likely to be applicable to claims falling within the new costs management rules. The parties had exchanged amended costs budgets just prior to trial. However, no application had been made for the previous CMO to be amended and the trial judge was unaware of the updated budgets. The defendant's amended budget was approximately double their earlier approved budget. On winning the claim, the defendant argued that:

- indemnity costs should apply;
- that their amended budget should be approved; and
- that if the amended budget was not approved, the court should find, for the purposes of costs assessment, that they had good reason for departing from their earlier approved budget.

Although Coulson J decided that indemnity costs were not applicable in this case, he commented that the starting point for assessing indemnity costs should still be the CMO, as this would provide a measure of certainty for parties going into litigation. The application of indemnity costs may be a good reason to then depart from the budget at assessment but this would be 'fact-specific' and the costs assessment should begin by reference to the approved budget.

The sanction for failing to file a budget is intentionally draconian: any party that does not file a budget as directed will be treated as having filed a budget comprising only the applicable court fees.

Secondly, Coulson J considered whether an application could be made to amend a CMO following judgment. He commented, in *Elvanite*, that an

application to revise a CMO 'ought to be made immediately it becomes apparent that the original budget costs have been exceeded by a more than minimal amount'. In this case a formal application should have been made to the court before trial and, furthermore, the judge indicated that he would not normally expect a CMO to be amended after judgment, as this would detract from the intention of the new rules to provide more certainty as to costs.

In *Elvanite*, the most significant increase in the defendant's costs was in respect of experts' fees. The sum of £30,500 was allowed for these fees in the approved budget, however fees of more than £200,000 had been incurred by the conclusion of the trial. Coulson J considered this to be 'an astonishingly high figure', and suggested that 'it is precisely this sort of unjustified expenditure which the costs management regime was designed to prevent'. This highlights the need to consider costs alongside case strategy at the outset and to provide justification for apparently high estimates at the time at which the budget is prepared.

Thirdly, Coulson J found that (with the possible exception of one issue which arose late in the litigation and required some additional evidence) he could see no good reason to depart from the budget at subsequent assessment, in respect of the increase in the experts' fees. The case had progressed as expected and it was felt that the defendant's overspend arose in large part from problems with the initial preparation of the budget. In accordance with his previous decision in *Murray*, Coulson J considered that it would be difficult to persuade a court to later rectify inadequacies or mistakes in the initial preparation of a budget.

Finally, on considering the defendant's entitlement to an interim payment of costs, Coulson J found that the defendant's costs were likely to be assessed overall at around the level of their approved budget and therefore ordered an interim payment of slightly less than the total budgeted amount.

How will the changes impact on legal practice and costs?

Lawyers and clients will have to focus more on time limits, compliance with rules, orders and practice directions, and aim to seek to agree extensions in good time. This could conceivably generate more work and costs. However, if faced with a time-wasting opponent, the positive aspect is that courts are likely to be more prepared to use their power to enforce compliance with unless orders and striking out, where appropriate, which could make case conduct sharper with some cost saving.

The starting point for assessing indemnity costs should be the CMO, as this would provide a measure of certainty for parties going into litigation.

Cost budgeting and the new test for proportionality will require early assessment of case strategy and detailed consideration of the available and required evidence, alongside considering the potential value of the claim. Once a budget is approved, the conduct of the case, including the division of work between different levels of fee-earner, the extent to which expert evidence is obtained, and reliance on counsel, will be led by the budgeted costs.

All of the focus on planning for case conduct and costs from the beginning of a case has the potential to make lawyers think more carefully about which matters they will take on and how these cases can be run cost effectively; the intention is that the costs will lead the work as opposed to the work leading the costs. However, it remains to be seen whether the new rules will reduce the costs of litigation by curbing unnecessary costs or will have the more detrimental effect of preventing litigants from pursuing their claims fully (or at all). This is of particular concern in complex claims where the damages are likely to be relatively modest but the claim is of the utmost importance to those pursuing it, for example a clinical negligence claim involving the death of a person, such as a child, who has no dependents.

Although the new rules promote increased certainty about costs, there is likely to be a period of significant uncertainty while we learn more about how the rules will be implemented. This may involve two to three years of satellite litigation to pin down 'proportionality' and possibly longer to check the parameters for compliance and assess how costs management will take effect in practice.

In some cases, costs budgets may reduce or replace the need for detailed assessment, effecting savings in the costs generated by the costs recovery process itself, and the reduction of such costs is the intention behind the new provisions for provisional assessment of costs up to £75,000.

There may also be unintended or unforeseen consequences, which surface when new rules are applied and interpreted in different contexts. There are already some 'what if' questions thrown up by the changes, such as what if the client wants to pay for further experts or work outside an approved budget – will the court allow such evidence to be used? Uncertainty itself generates costs and increases risks for lawyers advising clients but we can only know whether the pain and investment of time and cost involved in implementing the changes will achieve the intended purpose of controlling litigation costs after we have passed through the adjustment process to come in the next few years. ■

Elvanite Full Circle Ltd v AMEC Earth Environmental (UK) Ltd [2013] EWHC 1643 (TCC)

Fons HF v Corporal Ltd [2013] EWHC 1278 (Ch)

Fred Perry (Holdings) Ltd v Brands Plaza Trading Ltd & anor [2012] EWCA Civ 224

Henry v News Group Newspapers Ltd [2013] EWCA Civ 19

Lownds v Home Office [2002] EWCA Civ 365

Murray & anor v Neil Dowlman Architecture Ltd [2013] EWHC 872 (TCC)

Troy Food Ltd v Manton [2013] EWCA Civ 615