New South Wales Bar ADR Workshop
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"Walk Away Offers of Compromise"

Judge Peter Johnstone

1. Introduction

1.1 The topic I propose to address is "Walk Away Offers of Compromise".

1.2 This subject has been addressed in numerous judgments in recent years, and it seems that this is an area that will continue to excite the attention of appellate courts for some time to come.

1.3 One possible explanation for this is that in the context of the administration of justice the topic brings into focus the tension between the competing demands of access to justice and the efficient disposal of litigation.

1.4 Another possible explanation is the discretionary nature of costs orders generally. In *Baulderstone Hornibrook Engineering Pty Limited v Gordian Runoff Limited (No 2)* [2009] NSWCA 12 at [19] it was said by the President of the Court of Appeal, Justice Allsop:

> "There are now many authorities on genuineness of offers. All these are fact and circumstance specific to the case and the parties. The offer need only be, or be part of, a genuine attempt to reach a negotiated settlement."

1.5 Walk away offers are but a particular species of offers of compromise designed to attract an award of costs on an indemnity basis. To put the topic in context, therefore, first requires an overview of the principles surrounding the awarding of indemnity costs. I will then discuss offers of compromise, whether made in accordance with the UCPR or by way of Calderbank letters, and then turn to discuss walk away offers in particular.

2. Indemnity costs

2.1 The starting point for any discussion as to costs is s 98 of the *Civil Procedure Act 2005* (CPA), which gives the court power to award costs as between parties to litigation. Such costs are commonly described as "party/party costs". The court has full power to determine by whom, to whom and to what extent costs are to be paid, **and on what basis.** S 98(1) of the *Civil Procedure Act 2005* provides:

> "**Courts powers as to costs**
>
> Subject to rules of court and to this or any other Act:
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> (a) costs are in the discretion of the court, and
>
> (b) the court has full power to determine by whom, to whom and to what extent costs are to be paid, and
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> (c) the court may order that costs are to be awarded on the ordinary basis or on an indemnity basis."

2.2 Party/party costs are sourced from a court order, which one party recovers from another party in litigation. Costs are only payable if an order is made to that effect: CPA s 98(2). Costs are separate from and in addition to any award of damages or other order for the payment of money, but the costs will form part of the judgment. A judgment includes an order for costs: CPA s 3.

2.3 Practitioner/client costs, on the other hand, are the costs that the practitioner charges the client: *Qantas Airways Ltd v Dillingham Corp* (unreported, NSW Sup Ct, Rogers J, 14 May 1987); *Stanley v Phillips* (1966) 115 CLR 470 at 478. Practitioner/client costs are governed by the law of contract, subject to legislative intervention and the inherent supervisory jurisdiction of the Supreme Court: *Woolf v Snipe* (1933) 48 CLR 677.

2.4 Party/party costs are compensatory, and not used to punish: *Allplastics Engineering Pty Ltd v Dornoch Ltd* [2006] NSWCA 33. Party/party costs are to be assessed on the "ordinary basis" unless the court orders otherwise: r 42.2. They are in the nature of an indemnity of a party's practitioner/client costs, although they will rarely amount to a full indemnity of the practitioner/client costs. They do not include unreasonable or unusual costs: *EMI Records Ltd v Ian Cameron Wallace Pty Ltd* [1983] Ch 59; [1982] 2 All ER 980. Nor will they include costs incurred by "an unusually fussy, hysterical, ignorant, suspicious and vindictive" client: *Huggard v Huggard* (1902) 8 ALR 178. See also *Smith v Smith* [1906] VLR 78 at 80.

2.5 Costs awarded on an indemnity basis are intended to provide a more complete indemnity than costs awarded on the ordinary basis: *Milosevic v Government Insurance Office (NSW)* (1993) 31 NSWLR 323 at 324; *Rosniak v Government Insurance Office* (1997) 41 NSWLR 608; 26 MVR 204.

2.6 The purpose of the next part of my paper is to discuss the circumstances in which the court might award costs on an indemnity basis. The indemnity basis is defined in r 42.5(b):

> **"Indemnity costs**
>
> If the court determines that costs are to be paid on an indemnity basis:
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> (b) …all costs (other than those that appear to have been unreasonably incurred or appear to be of an unreasonable amount) are to be allowed."

The nature of indemnity costs

2.7 The important difference between the assessment of costs on the ordinary basis and assessment on an indemnity basis is the change in the onus of proof, it being incumbent on the paying party to satisfy the costs assessor as to unreasonableness of any costs claimed: *Singleton v Macquarie Broadcasting Holdings Ltd* (1991) 24 NSWLR 103, unlike an assessment on the ordinary basis where the claiming party carries the onus: *Kumagai Australia Finance v Avarton Ltd* (unreported, NSW Sup Ct, Bryson J, 7 June 1991). The essence of the effect of the reversal of onus has been described as "a question of who gets the benefit of the doubt": *EMI Records Ltd v Ian Cameron Wallace Pty Ltd* [1983] Ch 59; [1982] 2 All ER 980 at 989; *Bouras v Grandelis* (2005) 65 NSWLR 214; [2005] NSWCA 463 at [118].

2.8 Indemnity costs are distinct from practitioner/client costs: *Bouras v Grandelis* (2005) 65 NSWLR 214; [2005] NSWCA 463 at [125]; but in assessing party/party costs on an indemnity basis a costs assessor may have close regard to the actual practitioner/client costs: *Singleton v Macquarie Broadcasting Holdings Ltd* (1991) 24 NSWLR 103. Nevertheless, the practitioner/client costs must not be "blindly and uncritically" equated to the party/party costs: *Nieborak v Piper* (unreported, NSW Sup Ct, Young J, 11 December 1990). For example, a success premium under a costs agreement has been disallowed on assessment of party/party costs, even where the costs were awarded on an indemnity basis: *Madden v NSW Insurance Ministerial Corp* [1999] NSWSC 196. Indemnity costs may be akin to a penalty: *Lamesa Holdings BV v Federal Commissioner of Taxation* (1997) 74 FCR 416 at 419, but they remain compensatory, and the costs allowed must not offend the indemnity rule: *Petrotrade Inc v Texaco Ltd* [2001] 4 All ER 853 at 856.

2.9 The discretion to order that costs be paid on an indemnity basis, although absolute, must be exercised judicially: *Degmam Pty Ltd (in liq) v Wright (No 2)* [1983] 2 NSWLR 354; *Milosevic v Government Insurance Office (NSW)* (1993) 31 NSWLR 323. It used to be said that the court should only order indemnity costs in exceptional circumstances: *Leichhardt Municipal Council v Green* [2004] NSWCA 341. That principle, however, appears to be changing: *Chaina v Alvaro Homes Pty Ltd* [2008] NSWCA 353 at [111].

2.10 The bulk of the cases where indemnity costs have been awarded fall into certain recognised categories. But it has been emphasised that the categories are not closed: *PCRZ Investments Pty Ltd v National Golf Holdings Ltd* [2002] VSCA 24 at [35] - [36]; *Tetijo Holdings Pty Ltd v Keeprite Australia Pty Ltd* (unreported, FCA, French J, 3 May 1991); *Colgate-Palmolive Co v Cussons Pty Ltd* (1993) 46 FCR 225; 118 ALR 248 at 233-234 (FCR). It is also clear that a formal warning by one party of an intention to claim indemnity costs will make the awarding of indemnity costs more likely: *Martin v Carlisle* [2008] NSWSC 1276 at [6]; *Huntsman Chemical Co Aust Pty Ltd v International Pools Aust Ltd* (1995) 36 NSWLR 242.

2.11 It is convenient, then, to discuss the cases in the context of some these arbitrary categories, but it should be noted that the cases often overlap or fit into one or more of these categories. The categories are:

- Hopeless cases
- Abuse of process
- Fraud and other serious misconduct
- Unreasonable conduct or “relevant delinquency” in the proceedings
- Offers of compromise and *Calderbank* letters

Hopeless cases

2.12 Indemnity costs may be awarded in proceedings commenced or prosecuted in which there were no prospects of success. For example, where a limitation period applies: *Hillebrand v Penrith Council* [2000] NSWSC 1058, or the matters raised have been decided previously: *Bayne v Blake (No 3)* (1909) 9 CLR 366. Other circumstances include a claim that is “without substance”, “groundless”, “fanciful or hopeless” or so weak as to be futile. This might be the result of “wilful disregard of the known facts or the clearly established law”: *O'Keefe v Hayes Knight GTO Pty Ltd* [2005] FCA 1559; *Fountain Selected Meats (Sales) Pty Ltd v International Produce Merchants Pty Ltd* (1988) 81 ALR 397 at 401; *Frippery Pty Ltd v Booth* [2008] FCA 514.

2.13 An order will more readily be made where a letter is sent by one party pointing out the deficiencies of the other party's case or defence and giving notice of an intention to apply for indemnity costs: *McIlraith v Ilkin* [2008] NSWCA 11 at [19]. However, mere weakness of a case will not be sufficient to warrant an exercise of the discretion to award indemnity costs: see *Wentworth v Rogers (No 5)* (1986) 6 NSWLR 534. As to the dangers of assessing "hopelessness" in the "bright light of hindsight", see *Grynberg v Muller; Estate of Bilfeld* [2002] NSWSC 350 at [48].

Abuse of process

2.14 Costs may be awarded on an indemnity basis where the proceedings amount to an abuse of process: *Baillieu Knight Frank (NSW) Pty Ltd v Ted Manny Real Estate Pty Ltd* (1992) 30 NSWLR 359 at 362, such as where they were commenced other than in good faith, or for an ulterior or collateral purpose: *Hawke v Limbo* (unreported, NT Sup Ct, Kearney J, 9 August 1990), such as commencing defamation proceedings for the ulterior purpose of investigating the conduct of a royal commission: *Packer v Meagher* [1984] 3 NSWLR 486 at 500; or presenting a winding up petition against a solvent company to put pressure on it to pay money in respect of a bona fide dispute: *Re a Company (No 0012209 of 1991)* [1992] 1 WLR 351; *Polaroid Australia Pty Ltd v Minicomp Pty Ltd* (1997) 16 ACLC 529. See also *McAuliffe v Commonwealth* [2007] NSWSC 178; *Re SCA Properties Pty (in liq)* (1999) 17 ACLC 1611; *McKewins Hairdressing & Beauty Supplies Pty Ltd (in liq) v Deputy Commissioner of Taxation* (2000) 74 ALJR 1000; 171 ALR 335; [2000] HCA 27; *Fountain Selected Meats (Sales) Pty Ltd v International Produce Merchants Pty Ltd* (1988) 81 ALR 397 at 401.

Fraud and other serious misconduct

2.15 Other conduct which will ground an order for indemnity costs is misbehaviour of a serious nature, such as fraud: *Gate v Sun Alliance Ltd* (1995) 8 ANZ Insurance Cases 61-251 at 75,817 - 75,818, perjury or contempt: *Berkeley Administration Inc v McClelland* [1990] FSR 565 at 568–569; *Ivory v Telstra Corp Ltd* (unreported, Qld Sup Ct, Douglas J, 4 May 2001), and dishonest conduct: *Vance v Vance* (1981) 128 DLR (3d) 109 at 122, for example, deceptive behaviour calculated to harm the other party: *Ecrosteel Pty Ltd v Perfor Printing Pty Ltd* (1996) 37 IPR 22; or maintaining a defence which is known to be false: *Westpac Banking Corp v Ollis* [2007] NSWSC 1008 at [7] and [11], or where the rights and privileges of the other party are flouted or abused: *Ugly Tribe Co Pty Ltd v Sikola* [2001] VSC 189.

2.16 Contempt cases will usually attract indemnity costs, but not always, and it remains a matter of discretion in individual cases: *McIntyre v Perkes* (1988) 15 NSWLR 417; *Evenco Pty Ltd v Amalgamated Society of Carpenters etc Union of Employees (Qld)* [1999] QSC 53.

2.17 Other examples of sufficient dishonest conduct are breach of fiduciary duty and fabricated evidence: *Bir v Sharma* (unreported, The Times, Vinelott J, 17 December 1988); or unfounded allegations of fraud or improper conduct: *Re Bisyk (No 2)* (1980) 32 OR (2d) 281 at 287; *Maule v Liporoni (No 2)* (2002) 122 LGERA 216 at 22; *Jeans v Bruce* [2004] NSWSC 758; *Ingot Capital Investment v Macquarie Equity Capital Markets (No 7)* [2008] NSWSC 199. See also *Wentworth v Rogers (No 5)* (1986) 6 NSWLR 534 at 538; *Ronald v Harper* [1913] VLR 311.

Unreasonable conduct or "relevant delinquency" in the proceedings

2.18 But it is not only serious misconduct that will justify an order for indemnity costs. Conduct which is unreasonable or that involves a *"relevant delinquency"* may also be sufficient to justify the order.

2.19 Thus, inappropriate behaviour such as delay and unnecessarily prolonging the proceedings may be sufficient: *Spalla v St George Motor Finance Ltd (No 8)* [2006] FCA 1537 at [31]; *Re Wilcox; Ex parte Venture Industries Pty Ltd (No 2)* (1996) 72 FCR 151 at 153-154; or delay occasioned by the making of unjustified allegations: *Arian v Nguyen* (2001) 33 MVR 37; [2001] NSWCA 5 at [37]; *Degmam Pty Ltd (in liq) v Wright (No 2)* [1983] 2 NSWLR 354 at 358; *Melouhowee Pty Ltd v Steenbohm* (unreported, NSW Sup Ct, Waddell J, 6 February 1992) at 3; or disregarding a court order: *O'Keefe v Hayes Knight GTO Pty Ltd* [2005] FCA 1559 at [35]; or where the moving party fails to turn up on a motion.

2.20 Other behaviour held to have been sufficiently delinquent includes: knowingly maintaining a false defence: *Commonwealth Bank of Australia v Saleh* [2007] NSWSC 990, maintaining a cross claim on a basis that was inconsistent with the defence to the main claim: *International Advisor Systems Pty Ltd v XYYX Pty Ltd (Costs)* [2008] NSWSC 312; failings in relation to the discovery of documents: *Masha Nominees Pty Ltd v Mobil Oil Australia Pty Ltd (No 2)* [2006] VSC 56 at [17] - [21]; failing to brief expert witnesses with true and complete relevant history: *Mabbett v Watson Wyatt Superannuation Pty Ltd* [2008] NSWSC 460; or making multitudinous amendments: *Qantas Airways Ltd v Dillingham Corp* (unreported, NSW Sup Ct, Rogers J, 14 May 1987). See also *Sires v Prier* [2006] NSWSC 438; *LMI Australasia Pty Ltd v Baulderstone Hornibrook Pty Ltd* [2003] NSWCA 74; *Sydney City Council v Gatwick* [2006] NSWCA 280.

2.21 Other conduct for which courts have awarded indemnity costs includes deliberate or high handed behaviour: *Rouse v Shepherd (No 2)* (1994) 35 NSWLR 277 and other aggressive or uncooperative behaviour: *Preston v Preston* [1982] 1 All ER 41 at 58-59; *Unioil International Pty Ltd v Deloitte Touche Tohmatsu (No 2)* (1997) 18 WAR 190; wasting the court's time, such as with arguments which have no prospect of success: *Buckingham Gate International Pty Ltd v Australia & New Zealand Banking Group Ltd* (2000) 35 ACSR 411; [2000] NSWSC 946; *Asia Strategic Investment Alliances Ltd v HIH Casualty & General Insurance Ltd* [1999] NSWSC 601 at [76] - [77], or behaviour which causes unnecessary anxiety, trouble or expense, such as the failure to adhere to proper procedure: *FAI General Insurance Co Ltd v Burns* (1996) 9 ANZ Insurance Cases 77,213 (61-384). An ex parte order obtained against an innocent third party may be grounds for an order for indemnity costs: *Westpac Banking Corp v Hilliard* [2001] VSC 198.

2.22 The impugned conduct must be connected with the litigation itself, as opposed to the subject matter of the litigation, or causative of the litigation: *Mead v Watson* (2005) 23 ACLC 718; [2005] NSWCA 133 at [9] - [10], or done contemporaneously and influenced by the existence of the proceedings: *Masha Nominees Pty Ltd v Mobil Oil Australia Pty Ltd (No 2)* [2006] VSC 56 at [15] - [18] and [24]. But see also *Residents Against Improper Development Inc v Chase Property Investments Pty Ltd* [2006] NSWSC 623; *Scott v O'Riley* [2007] NSWSC 192.

Offers of compromise

2.23 Orders for costs on an indemnity basis are frequently made where a party failed to accept an offer of compromise that was more favourable than the ultimate outcome. Offers of compromise might be made under the UCPR or, alternatively, by way of a Calderbank letter. But they operate differently.

2.24 Rules 42.14 and 42.15 provide for the award of indemnity costs when parties fail to accept offers of compromise that should have been accepted: *Hillier v Sheather* (1995) 36 NSWLR 414. In this regard, the rules create a statutory exception to the presumption that costs should follow the event: *Maitland Hospital v Fisher (No 2)* (1992) 27 NSWLR 72 at 725. Although the court retains a discretion to make other orders for costs where appropriate, it is for the offeree to establish a basis for the court to do so: *Caine v Lumley General Insurance Ltd (No 2)* [2008] NSWCA 109 at [33].

2.25 The relevant rationale for the rules was first considered by the Court of Appeal in *Morgan v Johnson* (1998) NSWLR 578 at 581 - 582, per Mason P. The relevant passages are cited with approval more recently by Tobias JA in *Bennette v Cohen (No 2)* [2009] NSWCA 162 at [25].

2.26 The President, with whom Sheller JA agreed, stated the following propositions (omitting citations):

> "(1) The purpose of the rule is to encourage the proper compromise of litigation, in the private interests of individual litigants and the public interest of the prompt and economical disposal of litigation: *Maitland Hospital*; *Hillier*.
>
> (2) The aim is to oblige the offeree to give serious thought to the risk involved in non-acceptance: *Maitland Hospital*.
>
> (3) The prima facie consequence of non-acceptance will be that the rule will be enforced against the non-accepting party: *NSW Insurance Ministerial Corporation v Reeve*; *Hillier*. This is because, from the time of non-acceptance 'notionally the real cause and occasion of the litigation is the attitude adopted by [the party] which has rejected the compromise': *Maitland Hospital*; see also *Hillier*.
>
> (4) Lying behind the rule is the common knowledge that 'litigation is inescapably chancy': *Maitland Hospital*. For this reason, the ordinary provision is expected to apply in the ordinary case: ibid *NSW Insurance Ministerial Corporation v Reeve*. As Clarke JA expressed it in *Houatchanthara*:
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>> 'The rule lays down the general principle that should be applied, and the order provided for in that rule should only be departed from for proper reasons which, in general, only arise in an exceptional case.
>>
>> It is clear that if the rule operates, the plaintiff will be significantly disadvantaged, but that disadvantage flows naturally from the risks of litigation. The idea behind the rule is to encourage settlement or compromise of proceedings, and more specifically, to encourage litigants to give serious consideration to the settlement of proceedings. Where an offer is made by a defendant to a plaintiff, the latter is put on notice that unless he or she accepts that offer, there is a significant risk that the order provided for by the rule may follow. In declining to accept the offer, the plaintiff undertakes the risk and the consequences that flow naturally from that risk.'
>
> (5) The discretion to displace the rule is a judicial one, requiring the private and public purposes of the rule to be borne in mind: *Maitland Hospital*. Reasons must be given for 'otherwise ordering': *Hillier*; *Quach*."

2.27 Similar to the rules of court (but **not** identical) is the effect of the non-acceptance of an offer of settlement contained in a *Calderbank* letter: *Calderbank v Calderbank* [1976] Fam 93. Historically, there was no remedy outside the rules for a party to protect his or her position as to costs by making an offer of settlement. The modern law now recognises offers of settlement, even though made on a without prejudice basis, for the purposes of costs orders. This was recognised in *Messiter v Hutchinson* (1987) 10 NSWLR 525 by Rogers J. The principle is based on the court's discretion as to costs: see *Smallacombe v Lockyer Investment Co Pty Ltd* (1993) 42 FCR 97 at 101.

2.28 An offer of compromise which does not conform to the court rules may nevertheless be considered under the "*Calderbank*" principles: *Cook v Hawes* [2002] NSWCA 120, provided the offer discloses an intention to make a genuine offer: *Trustee for the Salvation Army (NSW) Property Trust v Becker (No 2)* [2007] NSWCA 194 at [27]. The intention must however, be made clear: *Dean v Stockland Property Management Pty Ltd (No 2)* [2010] NSWCA 141 at [34].

2.29 Hence there are a variety of circumstances in which it may be appropriate to make indemnity costs orders where a reasonable offer of settlement has not been accepted: *Nobrega v Trustees of the Roman Catholic Church for the Archdiocese of Sydney (No 2)* [1999] NSWCA 133; *LMI Australasia Pty Ltd v Baulderstone Hornibrook Pty Ltd* [2003] NSWCA 74.

2.30 There are important differences between an offer of compromise made under the UCPR and offers of compromise made by way of a Calderbank letter. These differences are addressed in detail in a comprehensive extra-curial paper by the Hon Justice Beazley AO (see the Supreme Court website at Speeches). See in particular her discussion of the advantages of an Offer of Compromise over a Calderbank offer at paras 60 - 67: see, eg, *Macquarie Radio Network Pty Ltd v Arthur Dent (No 2)* [2007] NSWCA 339.

2.31 The main distinction is that a *Calderbank* letter does not raise a prima facie presumption: per Giles JA in *SMEC Testing Services Pty Ltd v Campbelltown City Council* [2000] NSWCA 323 at [37], confirmed in *Jones v Bradley (No 2)* [2003] NSWCA 258 at [8], and *South Eastern Sydney Area Health Service v King* [2006] NSWCA 2 at [90].

2.32 Thus, the making of a *Calderbank* offer better than the result ultimately obtained does not automatically translate into an indemnity costs order: *Commonwealth v Gretton* [2008] NSWCA 117 at [43]; *SMEC Testing Services Pty Ltd v Campbelltown City Council* [2000] NSWCA 323; *Jones v Bradley (No 2)* [2003] NSWCA 258 at [8] - [9]; *East West Airlines Limited v Turner (No 2)* [2010] NSWCA 159 at [13] - [14]. Offerors bear the persuasive burden of satisfying the court to exercise its discretion in their favour: *Evans Shire Council v Richardson* [2006] NSWCA 61 at [26]; *Commonwealth v Gretton* [2008] NSWCA 117 at [46].

2.33 A second distinction is that an offer of compromise cannot be made inclusive of costs. Unlike on offer of compromise under the rules, a *Calderbank* offer may be made on an inclusive of costs basis: *Trustee for the Salvation Army (NSW) Property Trust v Becker (No 2)* [2007] NSWCA 194 at [25] - [29]. See for example: *Elite Protective Personnel v Salmon* [2007] NSWCA 322 at [7], and *Dean v Stockland Property Management Pty Ltd (No 2)* [2010] NSWCA 141 at [29].

2.34 A Calderbank offer also allows a greater degree of flexibility in the formulation of the offer. The offer may be limited to liability, or be made in the alternative: *Vale v Eggins (No 2)* [2007] NSWCA 12. It may take into account contributory negligence: *Coombes v RTA (No 2)* [2007] NSWCA 70. An offer may be made as a combined offer on behalf of a number of parties: *Monie v Commonwealth (No 2)* [2008] NSWCA 15 at [54]. See also *Manly Council v Byrne (No 2)* [2004] NSWCA 227; *Yazgi v Permanent Custodians Ltd (No 2)* [2007] NSWCA 306.

2.35 A major change was effected to the rules relating to Offers of Compromise by the UCPR, such that offers conforming with the rules may now be made at any time, including during a trial: r 20.26(7)(b). If made two months or more before trial the offer of compromise must be left open for not less than 28 days. Otherwise the requirement is that the offer be left open "for such time as is reasonable in the circumstances". This change was made to recognise the reality that *Calderbank* offers could be made at any time.

2.36 It was unclear whether an offer of compromise (as opposed to a *Calderbank* offer) must involve a real and genuine element of compromise: *The Uniting Church v Takacs (No 2)* [2008] NSWCA 172 per Basten JA at [30] - [33]. In *Hancock v Arnold (No 2)* [2009] NSWCA 19 the Court said:

> "What is required to trigger the costs consequences is an offer of "compromise". It is sometimes said that the offer must be "genuine", but this epithet probably adds little to the concept of compromise. Indeed, it may be distracting if it suggests that some assessment is required of the subjective intentions of the offeror. Whether there is an offer of compromise must be capable of objective determination by reference to the circumstances at the time the offer was made": [23].
>
> "The purpose of the cost rules is to encourage the making of offers of compromise. If the offer is designed to attract the rules, the rules are presumably having their intended effect. With a *Calderbank* offer, it is necessary to state expressly that the offer is without prejudice as to costs: such a statement provides no basis for depriving the offer of the consequences it would otherwise have, if not accepted and bettered by the offeree. The incentive to settlement will be diminished to the extent that persons receiving offers believe they can ignore them with impunity as to costs consequences": [24].

2.37 The decided cases disclose three broad categories of circumstances available to an unsuccessful plaintiff to resist an order for indemnity costs by reason of the failure to accept an offer of compromise bettered or equaled by the ultimate outcome. The first basis upon which a court might decline to award indemnity costs is that the period for acceptance was unreasonable. The second is that the offer did not involve any compromise. The third is that the rejection of the offer was not unreasonable.

3. Resisting indemnity costs orders in the context of an offer of compromise

3.1 I turn now to consider three broad categories of circumstances available to to resist an order for indemnity costs when there has been a failure to accept an offer of compromise not bettered or equalled by the ultimate outcome.

A reasonable time for acceptance

3.2 The first basis for resisting an order for costs on an indemnity basis is that the period for acceptance was unreasonable.

3.3 In *Pittorino v Yates* [2009] NSWCA 87 Tobias JA said that the offeree should not be placed under undue and unfair pressure, and should have the opportunity to make an informed and reasoned judgment whether or not to accept the offer. In *Hancock v Arnold (No 2)* [2009] NSWCA 19 the Court said:

"When offers are made and receive no response at all, let alone a counter-offer, the courts may need to be wary of accepting later suggestions that the offeree acted reasonably. For example, if the time permitted for accepting the offer is thought to be unreasonably short, a letter of response seeking an extension of time within which to consider the terms of the offer might be expected": [25]. Also in that case, Giles JA and Tobias JA said that having regard to the seriousness of the consequences, the Court should not be ungenerous in determining the question of whether the time was reasonable.

3.4 As to what is a reasonable time, see *Kooee Communications Pty Ltd v Primus Telecommunications Pty Ltd (No 2)* [2008] NSWCA 85 at [15] - [24]. Basten JA referred to three factors as relevant: The first is the extent to which the parties may reasonably be expected to have a clear perception as to the strengths and weaknesses of their positions, so that the reasonableness of a particular offer might be speedily assessed. The second factor is the stage which the proceedings have reached and because at trial costs accrue daily, even on an hourly basis, there is a heightened incentive to respond within the time permitted. And, thirdly, counterbalancing the first factor, the distraction from preparing or running a trial caused by the need to address the terms of an offer, provide advice and obtain instructions.

3.5 Other recent cases involving a consideration of the reasonableness of the period for acceptance include: *Chamma v Solima & Sons* [2008] NSWSC 382]; *Seary v White (No 5 - Costs)* [2008] NSWDC 21 at [17]ff; *Jones v Dapto Leagues Club Ltd (No 2)* [2008] NSWCA 111, *County Securities Pty Ltd v Challenger Holdings Pty Limited (No 2)* [2008] NSWCA 273 at [35].

The concept of compromise

3.6 The next factor to be considered is whether the offer represented or formed part of a genuine attempt to reach a negotiated settlement: *Baulderstone Hornibrook Engineering Pty Limited v Gordian Runoff Limited (No 2)* [2009] NSWCA 12 at [19].

3.7 In *Hancock v Arnold (No 2)* [2009] NSWCA 19 the Court of Appeal said:

> "What is required to trigger the costs consequences is an offer of "compromise". It is sometimes said that the offer must be "genuine", but this epithet probably adds little to the concept of compromise. Indeed, it may be distracting if it suggests that some assessment is required of the subjective intentions of the offeror. Whether there is an offer of compromise must be capable of objective determination by reference to the circumstances at the time the offer was made": [23].

3.8 This is an evaluative determination, as to which "judicial minds may differ": see the paper by Justice Beazley at [28]. Thus, an offer designed "merely to trigger any costs sanctions" will not be regarded as an offer of compromise: *Leichhardt Municipal Council v Green* [2004] NSWCA 341 at [21] - [24], [36] and [39]; *Russell v Edwards (No 2)* [2006] NSWCA 52 at [8]; *Jones v Bradley (No 2)* [2003] NSWCA 258 at [12]. Or, the offer involves so small a compromise as to be illusory: *Bartlett v Coomber* [2008] NSWCA 282 at [8] and [10].

The concept of unreasonable rejection

3.9 The next factor to be considered is whether the rejection of the offer was not unreasonable. The determination is also an evaluative judgment requiring a consideration of the facts and circumstance specific to the case: *Baulderstone Hornibrook Engineering Pty Limited v Gordian Runoff Limited (No 2)* [2009] NSWCA 12 at [19]. Some of the factors overlap with the first concept discussed above at to whether the offer involved a compromise.

3.10 The reasonableness of an offer may be determined on a summary basis without the need to adduce further evidence. However, sometimes material will need to be put before the court to establish the circumstances, such as the correspondence.

3.11 Relevant factors have been held to include the complexity of the issues: *MGICA (1992) Pty Ltd v Kenny & Good Pty Ltd (No 2)* (1996) 70 FCR 236; the modesty of the amount in issue: *Ofria v Cameron (No 2)* [2008] NSWCA 242; and whether any and what conditions have been placed on the offer: *Skalkos v Assaf (No 2)* [2002] NSWCA 236; *Baulderstone Hornibrook Engineering Pty Ltd v Gordian Runoff Ltd* [2006] NSWSC 583 at [73] - [74].

3.12 Another circumstance relevant to the reasonableness of rejection is where the full parameters of the dispute were still uncertain at the time of the offer: *Equity 8 Pty Ltd v Shaw Stockbroking Ltd* [2007] NSWSC 503 at [42]; or where the offeror's case changes after the offer: *South Eastern Sydney Area Health Service v King* [2006] NSWCA 2006 NSWCA 2 at [85]; *Rolls Royce Industrial Power (Pacific) Ltd v James Hardie & Co Pty Ltd* [2001] NSWCA 461; *East West Airlines Limited v Turner (No 2)* [2010] NSWCA 159 at [16].

3.13 Hence, where all the relevant evidence had not been served before the offer, the discretion to award indemnity costs might be refused: *Vale v Eggins (No 2)* [2007] NSWCA 12 at [22]. But not where the information is served early: *Elite Protective Personnel v Salmon* [2007] NSWCA 322 at [147]. Thus, putting a party on clear notice of certain facts affecting the likely outcome will weigh in favour of the offeror: *Blagojevch v Australian Industrial Relations Commission* (2000) 98 FCR 45.

3.14 In the case of a Calderbank offer, the form of the letter may also be a factor: *Elite Protective Personnel v Salmon* [2007] NSWCA 322 at [7] and [137]; *Trustee for the Salvation Army (NSW) Property Trust v Becker (No 2)* [2007] NSWCA 194 at [25] - [29], such as whether it warns sufficiently of the consequences of a failure to accept a reasonable offer: *Ng v Chong* [2005] NSWSC 385 at [14]; see also *Nobrega v Trustees of the Roman Catholic Church for the Archdiocese of Sydney (No 2)* [1999] NSWCA 133. There is, however, no set form or specific formula required: *Grace v Thomas Street Café Pty Ltd (No 2)* [2008] NSWCA 72 at [29]. An offer that does not finalise the terms upon which the matter is to be resolved and does not put an end to the negotiations is relevant to the exercise of the discretion: *Commonwealth v Gretton* [2008] NSWCA 117 at [11].

3.15 The statement of principle enunciated in *Morgan v Johnson* (see above at 2.27) to the effect that an order other than an order in accordance with an offeror's prima facie entitlement to indemnity costs should only be made in "exceptional circumstances" has been consistently affirmed: see *South Eastern Sydney Area Health Service v King* [2006] NSWCA 2 at [83]; *Caine v Lumley General Insurance Ltd (No 2)* [2008] NSWCA 109 at [35].

4. Walk away offers of compromise

4.1 I turn now to specifically consider walk away offers of compromise against the background of the general principles I have so far discussed, in particular the principle that the offer must contain a genuine element of compromise, or as Justice Allsop puts it, be part of a genuine attempt to reach a negotiated settlement.

4.2 The first point to be made is that in New South Wales the concept of walk away offers has been given express legislative recognition. Rule 20.26(2) of the UCPR provides:

"An offer must be exclusive of costs, except where it states that it is a verdict for the defendant and that the parties are to bear their own costs."

4.3 By definition, a walk away offer will involve an offer by a defendant that the plaintiff rejects, and after a hearing the plaintiff loses. The applicable rule is r 42.15A, which provides:

"**42.15A Where offer not accepted and judgment as or less favourable to the defendant**

(1) This rule applies if the offer concerned is made by the defendant, but not accepted by the plaintiff, and the defendant obtains an order or judgment on the claim concerned as favourable to the defendant, or more favourable to the defendant, than the terms of the offer.

(2) Unless the court orders otherwise:

(a) the defendant is entitled to an order against the plaintiff for the defendant's costs in respect of the claim, to be assessed on the ordinary basis, up to the time from which the defendant becomes entitled to costs under paragraph (b), and

(b) the defendant is entitled to an order against the plaintiff for the defendant's costs in respect of the claim, assessed on an indemnity basis:

(i) if the offer was made before the first day of the trial, as from the beginning of the day following the day on which the offer was made, and

(ii) if the offer was made on or after the first day of the trial, as from 11 am on the day following the day on which the offer was made."

4.4 As to whether the ultimate judgment is as favourable to the defendant, or more favourable to the defendant, there can be little doubt that where a walk away offer was made and the defendant recovers judgment on the claim concerned, that is a result as favourable to the defendant, or more favourable to the defendant, than the terms of the offer.

4.5 The effect of an outcome whereby the parties to litigation are to bear their own costs is that no party/party costs are payable: *Re Hodgkinson* [1985] 2 Ch 190; *Trikas v Rheem (Australia) Pty Ltd* (1964) 81 WN (Pt 1) (NSW) 504. Such costs as the parties may have incurred themselves, or any liability to pay practitioner/client costs, lie where they fall: *Wentworth v Wentworth* [1999] NSWSC 638. (Thus, an order that each party *pay* their own costs is inappropriate, the better order being that each party *bear* their own costs: *Liverpool City Council v Estephan* [2009] NSWCA 161 at [75].)

4.6 But the concept of success is not to be confused with the concept of compromise. In *Regency Media Pty Ltd v AAV Australia Pty Ltd* [2009] NSWCA 368 at [28] - [30] the Court of Appeal said:

> "It will rarely be the case that a decision needs to be made as to whether or not an "offer" answers the description of an "offer of compromise" within the rules. To the extent that the element of compromise is absent, the Court will be more likely to "otherwise order"… The offer… was an invitation to surrender, rather than any form of commercial compromise… Any such element of compromise was, at best, "of limited significance"… The offer can be accurately described as derisory."

4.7 Thus, an offer that is in substance an invitation to surrender, rather than a commercial compromise, will not trigger the indemnity costs mechanisms unless something more is present, such as a claim approaching the frivolous or vexatious: *Regency Media Pty Ltd v AAV Australia Pty Ltd* [2009] NSWCA 368 at [31]. "If it were otherwise, the public policy to encourage settlement would rarely be served, in an all or nothing case." What is ultimately required is that the offer contain some real benefit to a plaintiff, something more than total capitulation: see *Bennette v Cohen (No 2)* [2009] NSWCA 162 at [38]. See also *Roads and Traffic Authority of NSW v Refrigerated Roadways Pty Ltd (No 2)* [2009] NSWCA 336 at [17] - [21].

4.8 In *Regency Media Pty Ltd v AAV Australia Pty Ltd* [2009] NSWCA 368 at [32], the Court went on to discuss the concept of an "all or nothing case":

> "Whilst a marginal difference between the offer and the result may constitute a real and genuine offer of compromise in a personal injury context, that is not generally true in an all or nothing case… If a derisory offer, of the kind made in these proceedings, could result in an order for indemnity costs, then it is likely that many, perhaps most, contract interpretation disputes would result in an indemnity costs order, if the formality of an offer in accordance with the rules had been made at an early stage. If the appellant were to succeed in the present case, it is quite likely that such an offer would accompany most statements of claim as a matter of commercial practice. The purpose of the special order - to encourage settlement - would no longer be served."

4.9 This concept of an "all or nothing case", not involving a process of evaluation or assessment in which the end result could vary over a range, has found voice in other Court of Appeal decisions, to which I now turn.

4.10 In *Robb Evans v European Bank Ltd (No 2)* [2009] NSWCA 170 the Court of Appeal made a distinction between all or nothing cases and those involving evaluative judgments with a range of possible outcomes. It said this at [18]:

> "Generally, damages claims for personal injury are likely to involve evaluative judgments both in respect of liability and quantum. Cases turning upon what a reasonable person would do in particular circumstances and whether there is a sufficient causal connection between a breach of duty and an injury suffered are likely to involve evaluative judgments. The same will be true of an assessment of loss. By contrast, the outcome of a contract case may well depend upon a point of construction of a contract, the outcome of which may be uncertain, but which results in one party winning and the other losing; success or failure in such a case will not involve the selection of a point within a range of possible outcomes. This point of distinction is illustrated by the present case. Either the respondent was entitled to recover losses calculable by reference to currency movements, based upon its probable actions if it had received the money when it should have, or it was not. In practical terms, there was no range of possible outcomes."

4.11 In *Dean v Stockland Property Management Pty Ltd (No 2)* [2010] NSWCA 141 at [43] the Court of Appeal warned that care must be taken not to unduly deter parties from bringing or defending proceedings for fear that they will retrospectively be found to have not been justified in doing so:

> "Uncertainty in outcome is not enough, and what appears certain at the time of judgment does not necessarily have that character at an earlier time."

4.12 The Court went on to cite a passage from the decision of Harper J from Victoria in *Ugly Tribe Co Pty Ltd v Sikiola* [2001] VSC 189 at [11] in the context of balancing the interests of successful and unsuccessful litigants:

> "After all success can seldom be guaranteed, if only because - where the facts are in dispute, as they generally are - it is seldom possible to predict with certainty what findings of fact will be made. In these circumstances, an honest plaintiff or defendant might be discouraged from bringing or defending a claim where an adverse result to be followed by an order that the losing party indemnify, or go close to providing an indemnity to, the successful party against the latter's costs."

4.13 These concepts were taken up in *East West Airlines Limited v Turner (No 2)* [2010] NSWCA 159. In that case the Court concluded that it was not unreasonable for the appellant to refuse an offer of settlement "on the basis that the appeal be withdrawn with each party to bear their own costs". The appeal raised an important practice issue that had not previously been decided, and there were persuasive arguments supporting the position of each party.

Even though the outcome of the appeal turned substantially on the basis that it raised issues of fact, there was, however "scope for argument to the contrary". The submissions were not "so untenable" that indemnity costs should be awarded.

4.14 More importantly for present purposes, the Court went on to say that even if it were a genuine attempt to resolve the matter, the real question was whether it was unreasonable for the respondent to refuse the offer. On this question, the Court said "there were substantial matters for determination in the appeal" that "required the Court's full consideration". In refusing to award indemnity costs, the Court went on to say at [12]:

> "Although the first respondent's submissions on the appeal were found to be wrong, they were not unarguable. It should also not be forgotten that after a lengthy and hard fought trial the first respondent had been successful in obtaining judgment in its favour. In the context of assessing a "walk away" offer, these are important considerations."

5. Conclusion

5.1 As Justice Hoeben said in his judgment in *Melchior v Sydney Adventist Hospital Ltd (No 2)* [2009] NSWSC 65 at [17]:

> "It is always difficult to evaluate the genuineness of a "walk away" offer."

5.2 My conclusion is that to establish that a walk away offer involves the necessary element of compromise will require the offeror to demonstrate a saving in costs of some substance: *Dean v Stockland Property Management Pty Ltd (No 2)* [2010] NSWCA 141 at [15].

5.3 But even that may not be enough to justify indemnity costs where the case involves substantial matters for determination on hearing, especially in all or nothing cases, not involving evaluative judgments with a range of possible outcomes: *Hancock v Arnold (No 2)* [2009] NSWCA 19 at [23] -]24].

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