

Are You Being Reasonable? – Calderbank Offers and Costs Protection in Litigation

Aquagenics Pty Limited (in liquidation) v Certain Underwriters at Lloyd's Subscribing to Contract Number NCP106108663 (No 2) [2017] FCA 724

Fiona Reynolds & Melissa Liu | July 2017 | Commercial Disputes & Transactions

Summary

It is well established that failure of a party to accept a *Calderbank* offer may justify the Court exercising its discretion to award costs on an indemnity basis.

Generally a Court needs to determine, having regard to the circumstances, whether the party was acting unreasonably in rejecting the offer.

A recent case has shown that the Court will not award costs on an indemnity basis if at the time of the offer, the applicant had not pleaded certain entitlements to indemnity and the offer was a 'minimal compromise' measured against indemnity subsequently sought.

It is important that when parties make or receive a *Calderbank* offer, careful consideration is given to the offer and the pleaded case at the time the offer is made.

Background

The Federal Court of Australia decision in *Aquagenics Pty Ltd*¹ is a reminder for parties to carefully consider their options before rejecting a *Calderbank* offer as the offeror can potentially seek for its costs to be paid on an indemnity basis.

Facts

- Certain underwriters from Lloyd's ('the Insurers') were the professional indemnity insurers of Aquagenics Pty Ltd ('Aquagenics').
- In May 2014, Aquagenics gave notice to the Insurers that a third party had a claim against it and an Arbitrator had ordered that Aquagenics pay to the third party the sum of \$1,346,111.57 arising from a breach of contract concerning work for the design and construction of a wastewater treatment plant during the period of policy. This triggered Aquagenic's entitlement to be indemnified.
- The Insurers did not accept liability to indemnify under the policy.
- Aquagenics commenced proceedings against the Insurers claiming indemnity pursuant to the policy but only sought indemnity in respect of the amounts awarded by the Arbitrator for design defects (amounting to \$668,729) plus certain other expenses, costs, Arbitrator's fees and interest.
- On 9 September 2016, Aquagenics put forward a *Calderbank* offer to the Insurers to settle on the following basis:
 - a) a payment of compensation in the sum of \$600,000; plus
 - b) a further payment for costs in the sum of \$64,000;
 - c) terms of settlement be recorded in a deed of release containing a confidentiality clause;

d) the action be dismissed upon payment, on the basis that each party will pay their own costs.

- The offer was open for 28 days. The Insurers rejected the offer.
- On 13 April 2017, Aquagenics amended its pleadings to include indemnity for items with respect to pre-commissioning and commissioning, thereby increasing the total claim for indemnity to \$1,695,082.
- On 5 June 2017, the Court delivered judgment and found that Aquagenics was entitled to be indemnified under a policy of insurance pursuant to section 57 of the *Insurance Contracts Act 1984* (Cth) in the amount of \$1,695,082 plus interest.
- On or about 20 June 2017, Aquagenics applied to the Court to have its costs paid on an indemnity basis from 9 September 2016 by reason of the *Calderbank* offer.

Legal Principles

The Court, in determining whether to award indemnity costs, followed the principles set out in *Kooee Communications Pty Ltd v Primus Telecommunications Pty Ltd (No 2)* [2011] FCAFC 141 and *CGU Insurance Ltd v Corrections Corporation of Australia Staff Superannuation Plan Pty Ltd* [2008] FCAFC 173; (2009) 15 ANZ Insurance Cases 61-785.

One of the key elements for consideration by the Court was whether, having regard to the circumstances, the Insurers had acted unreasonably in rejecting the offer.

Decision

Aquagenics submitted that because it had succeeded in obtaining judgment in its favour for an amount significantly higher than the initial amount offered to the Insurers in the *Calderbank* offer, it was *prima facie* entitled to an order against the Insurers for costs on an indemnity basis.

On the question of whether it was unreasonable to reject the offer, his Honour considered the prevailing circumstances at the time of the offer.

At the time of the offer, Aquagenics' pleaded claim for indemnity was for design defects totalling \$668,729 plus expenses, costs, Arbitrator's fees and interest.

The offer however was premised on a claim for \$1,127,082, which sum represented a portion of the larger claim for indemnity that was not pleaded until well after the *Calderbank* offer had expired.

His Honour was of the view that whilst Aquagenics' offer did represent a genuine compromise of the amount ultimately claimed, it was only a minimal compromise on the claim for indemnity at the time of the offer. His Honour concluded that the Insurers had not acted unreasonably in rejecting the offer and declined to award indemnity costs on the basis of the offer.

Implications

Although the rejection of the offer was reasonable, it does not follow that it was not sensible for Aquagenics to have made the offer.

This decision serves as a reminder of the Court's approach in exercising its discretion in awarding indemnity costs in particular, considering:

1. whether there was a genuine offer of compromise?; and
2. whether it is unreasonable for the party to whom the offer is made to reject it.

The use of *Calderbank* offers and offers of compromise under the UCPR are useful tools to facilitate settlement and protect a party's position in respect of costs. It is important to keep in mind that it may not automatically follow that if an offer is declined and an outcome more favourable than the offer is achieved at final hearing, that an order for indemnity costs will be awarded. This decision is a timely reminder that it is the prevailing circumstances at the time the offer is made, not at the time of judgment, that are relevant to determining whether a decision to reject an offer is reasonable.

¹ *Aquagenics Pty Limited (in liquidation) v Certain Underwriters at Lloyd's Subscribing to Contract Number NCP106108663 (No 2)* [2017] FCA 724 (23 June 2017)

For more information,
please contact:



Fiona Reynolds

Partner

T: 02 8257 5751

M: 0417 215 703

fiona.reynolds@turkslegal.com.au



Melissa Liu

Lawyer