Costs Law Update
Spring 2017

Costs Budgeting Special

Budget Done, Now Monitor

Preparing a budget and having this agreed or approved by the court is just the first part of the budgeting process. Serious trouble may lie ahead if the initial budget is simply filed away until the conclusion of the matter.

The rules state that an agreed/approved budget will not be departed from on detailed assessment unless the court is persuaded that there is a good reason to do so. Although, to date, there is limited case law on the approach the court will take to whether there is a "good reason", this is likely to be interpreted narrowly. The easier route to escaping the initial approved/agreed budget is to make an application for permission to amend. PD 3E requires the parties to revise their budgets in respect of future costs "if significant developments in the litigation warrant such revisions". Even if there is otherwise a "good reason" to depart from the budget on assessment, it is unlikely a court would do so if there has been a failure to apply for an amended budget at the point of any "significant development". What amounts to a "significant development" is also likely to be interpreted narrowly.

The amended budget will only apply to future costs, not those already incurred.

The costs budgeting process therefore makes it essential that costs are carefully monitored as they are being incurred, so fee earners are alert to the danger that a budget may be exceeded. It is also crucial to understand what needs to be monitored. It is not sufficient to know that only £60,000 worth of costs have been incurred in relation to an agreed/approved budget of £100,000. This is because PD 3E para.7.10 states:

> "The making of a costs management order under rule 3.15 concerns the totals allowed for each phase of the budget."

A court on detailed assessment is concerned with each phase. It is not enough to be within budget overall; the costs for each phase must also be in budget. Also, costs which cause a phase to be exceeded cannot be moved over to a phase that has not been exceeded. So, for example, if there is a budget that allows £10,000 each for the Witness Statements and Disclosure phases, if £15,000 has been incurred for one phase and £5,000 for the other then you are still £5,000 over budget and unlikely to be able to recover the shortfall.

As it is only future costs that can be approved in any amended budget, it is essential that the costs spend is carefully monitored to identify any potential overspend well in advance of the limit of the budget for the relevant phase actually being exceeded.

It would be a mistake to believe that any shortfall between the costs incurred and the level of budget can automatically be recovered from the client. For such a shortfall to be recovered from the client it is likely to be necessary to show:

(i) the client was told that work was being undertaken that was in excess of the budget;
(ii) the client was informed that such work was unlikely to be recovered from the other side, even if successful;
(iii) the client expressly agreed to this.

The process of carefully monitoring costs as a case proceeds has the positive advantage of focusing fee earners' minds on the level of work that is being reasonably undertaken relative to the budget and thus reducing the risk of going over-budget in the first place. Secondly, it enables fee earners to appreciate the amount of time that they do actually spend on various phases of a case in a way that has often traditionally been lacking. This will assist enormously when it comes to the preparation of accurate future budgets in other matters.

The key points to remember are:

- Advise clients of the budget set and the consequences of the same.
- Continue to advise clients of the level of costs being incurred relative to the budget on a regular basis.
- Monitor the level of costs being incurred on a regular basis phase-by-phase.
- If there is a significant development in a case, review what impact this may have on the budget.
- If it is necessary to apply to have a budget revised, apply well before work is undertaken outside the existing budget.

Avoiding a Professional Negligence Claim

One of the problems with the costs management process is that many budgets are laboriously prepared but there is then such a reluctance, or delay, on the part of the courts to list a matter for a costs management hearing that the case settles without any actual costs management order being made. The rules state that where a costs management order has been made, when assessing costs on the standard basis, the court will not depart from such approved or agreed budget unless satisfied that there is good reason to do so. Does this mean that costs budgets can be safely ignored in the absence of a costs management order? No.

Caution is needed because the rules themselves relating to costs budgeting are somewhat confusing and inconsistent. CPR 44.4 states that at a detailed assessment hearing on the standard basis the court will have regard to the receiving party's "last approved or agreed budget". This implies that a court will not be concerned with a budget that has not been approved or agreed. However, PD 44 para.3.2 provides:

> *"If there is a difference of 20% or more between the costs claimed by a receiving party on detailed assessment and the costs shown in a budget filed by that party, the receiving party must provide a statement of the reasons for the difference with the bill of costs."*

This requirement applies to any budget filed, with there being no precondition of it being approved or agreed. Further, PD 44 para.3.4 expressly provides that the court may take into account any filed budgets which have not been approved or agreed when assessing the reasonableness and proportionality of any costs claimed.

Perhaps most important is the further provision at PD 44 para.3.6 that:

> *"Where it appears to the court that the paying party reasonably relied on the budget, the court may restrict the recoverable costs to such sum as is reasonable for the paying party to pay in the light of that reliance, notwithstanding that such sum is less than the amount of costs reasonably and proportionately incurred by the receiving party."*

This is an enormously useful tool for controlling the recoverable costs of the other side, but one that is unfortunately routinely overlooked. It potentially means, for example, that a party's recoverable costs might be limited to the £100,000 shown in a filed budget even if the court concludes £200,000 has been reasonably and proportionately incurred. The key element of this provision is being able to show reasonable reliance. This requires two things:

1. Consideration must have been given to the other side's budget when it was served. In the new litigation landscape, failure to do so is likely to amount to professional negligence.
2. The client must have been informed about the budget and advised accordingly. This should be second nature in any event (and negligent not to do so), but is also crucial to setting up a paper trail to show there has been reasonable reliance. A short file note and letter to the client may save them £10,000s or £100,000s in third party costs. It is probably not sufficient to simply show that consideration was given to the budget. What is likely to be required is evidence of decisions being made as a consequence of the budget. This does not necessarily require a major change in the conduct of the litigation. It is likely to be sufficient to advise the client along the lines of: "in light of the other side's budget of £100,000 to take the matter to trial we believe this matter should continue to be defended" or "given the other side's budget of £200,000 to take this matter to trial we would recommend that consideration should be given to the possibility of ADR". The advice may be the same as would have been given in any event but the crucial step is to establish contemporaneous evidence of reasonable reliance on the budget.

This issue can, of course, work both ways. The other side may also seek to show reasonable reliance on your budget if they are the paying party. This is yet another reason to carefully monitor your own costs expenditure as against your own budget as a case progresses. Even where there has been no approved or agreed budget, if it appears that your own served budget may be too low, it is essential that an updated one is prepared and served.

Getting the Basics Right

Having an approved court budget may be of limited benefit if work has been placed into the wrong phase when completing the budget.

Surely if work is undertaken pre-proceedings in relation to preparing witness statements this should be placed in the Precedent H budget in the Pre-Action phase? No.

The *Guidance Notes on Precedent H* state that the Pre-Action phase should not include "any work already incurred in relation to any other phase of the budget." So, for example, work done pre-proceedings on witness statements should go in the Witness Statements phase under incurred costs.

If you or your opponents' budget shows significant costs claimed in the Pre-Action phase, it has almost certainly been incorrectly completed.

What About Incurred Costs?

The costs budgeting rules as originally drafted appeared to make clear that costs management orders related to future costs only. It was therefore generally understood that parties did not need to challenge incurred costs at a costs management conference as such costs would be dealt with in the ordinary way at detailed assessment at the end of the claim.

However, this (universal) understanding was thrown into doubt by comments made by the Court of Appeal in Sarpd Oil International Ltd v Addax Energy SA & Anor [2016] EWCA Civ 120. This appeared to suggest that the first CMC was the appropriate occasion on which issues between the parties regarding the quantum of costs shown in their respective costs budgets should be debated and that this related to both future costs and those already incurred.

These observations caused considerable concern that failing to dispute an opponent's incurred costs at the CMC/CCMC stage may mean the chance is lost forever.
Fortunately, and because of these concerns, the Civil Procedure Rules have been amended to make clear that any costs management order relates to future costs only. However, the rules provide that the court

may also record the extent to which incurred costs are agreed by the parties. Further, the court itself may comment on the incurred costs, which will be a factor for the court to take into account at any future detailed assessment. These amendments came into force from 6 April 2017.

It therefore remains essential, when discussing costs budgets with opponents or at costs management conferences, to be clear whether it is incurred or future costs that are being referred to and what it is that is covered by any costs management order.

Revising Budgets Downwards

PD3E para.7.6 requires parties to revise their budgets if there is a "significant development" in the litigation. Parties have naturally tended to focus on seeking to increase their own budget if there is such a development. However, for defendants, this provision is just as important as a tool to reduce an opponent's budget downwards.

A significant factor for the court, when setting the initial budgets, will be proportionality and, more specifically, the potential value of the claim and its complexity. The budgets should be set at a level which is proportionate to reflect these factors. In this context, it is just as important to recognise that an apparently high value, complex claim can reduce in value and complexity as easily as going in the other direction.

Against this background, it is easy to see that a budget of £100,000 may have been proportionate when a claim was valued at £500,000 but would cease to be remotely proportionate if the likely value of the claim dropped to £10,000 because of medical developments.

The extent to which a change in the value of the case amounts to a "significant development" will be case specific. For example, in *Churchill v Boot* [2016] EWHC 1322 (QB) the court declined to allow an increase to the claimant's budget as a consequence of the value of the claim doubling.

Defendants need to be alert to any significant developments in a case that may provide the opportunity to try to reduce opponents' budgets downwards. Although a significant change in the value/complexity of a claim might be a "good reason" to depart from a budget on detailed assessment at the conclusion of a case, a court may doubt it satisfies that description if a party has failed treat it as being a "significant development" during the claim by applying for the budgets to be varied.

Costs Budgeting Training

GWS are currently arranging a limited number of in-house costs training sessions on the costs budgeting process.

These are designed to provide practitioners with a practical insight into this area of the law and to deliver tactical tips on staying one step ahead of the opposition.

Please contact Simon Gibbs if you would like to find out more.

Please Contact Us

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