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The merits factor in assessing an unreasonable refusal of ADR: a critique and a proposal[1]

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Halsey v Milton Keynes General NHS Trust [2004] EWCA Civ 576; [2004] 1 W.L.R. 3002 (CA (Civ Div))

Hurst v Leeming [2002] EWHC 1051 (Ch); [2003] 1 Lloyd's Rep. 379 (Ch D)

Dunnett v Railtrack Plc [2002] EWCA Civ 303; [2002] 1 W.L.R. 2434 (CA (Civ Div))

Golden Eagle International (Group) Ltd v GR Investment Holdings Ltd [2010] 3 H.K.L.R.D. 273 (CFI (HK))

Swain Mason v Mills & Reeve [2012] EWCA Civ 498; [2012] S.T.C. 1760 (CA (Civ Div))

Northrop Grumman Mission Systems Europe Ltd v BAE Systems (Al Diriyah C4I) Ltd [2014] EWHC 3148 (TCC); [2015] 3 All E.R. 782 (QBD (TCC))

J.B.L. 646 As state funding of the civil justice system continues to erode, there is unprecedented pressure on the courts to ration their limited resources in managing the high volume of civil and commercial disputes coming before them.[2] It is not surprising, therefore, that members of the senior judiciary have been enthusiastic in advocating the increasingly important role and benefits of alternative dispute resolution processes[3] (ADR), in particular mediation, as an adjunct to the formal adjudicative court process.[4] As Lord Neuberger MR made clear in his (cautious)[5] support for ADR:

"It is an important adjunct to, with potentially strongly beneficial effect, on our civil justice system and can be highly effective in securing a relatively cheap and expeditious, and often imaginative, resolution of civil disputes. ***J.B.L. 647*** " [6]

In 2015,[7] his Lordship went further by alluding to the idea of extending the compulsory MIAM (mediation information and assessment meetings) under the Children and Families Act 2014 [8] to certain, smaller civil cases; an idea which had previously been advocated by Lord Faulks, the Minister for Civil Justice.[9] More recently Briggs LJ in his Civil Court Structure Review (CCSR) has recommended the greater integration of ADR within his proposed Online Court.[10]

The governement is also becoming increasingly vocal of the need to promote more conciliatory foms of dispute resolution. In a joint report published in September 2016, "Transforming our Justice System", the Ministry of Justice and senior judiciary explained the new approach to dispute resolution which would assist ordinary people. This would involve a focusing on a number of ADR options including negotiation, conciliation and mediation.

The benefits of ADR over the traditional litigation process have been echoed throughout the ADR jurisprudence and extra-judicial pronouncements,[11] as well as being consistently reinforced by policy-makers.[12] As well as saving time and cost, a successful ADR outcome may assist commercial parties to maintain their trading relationship and this may lead to higher rates of satisfaction and greater levels of compliance with outcomes.[13] Yet a failed ADR, an ADR process which has not resulted in a settlement, may compound litigation costs because the parties must then incur further costs of engaging with the court process. A further issue of controversy, which will be considered in the second part, has been whether mandatory ADR (for example, introduced in Canada, the US and

Italy) adversely impacts on the right to a fair trial as protected by art.6 of the European Convention of Human Rights.

Despite the increased focus on ADR, certain aspects of the Court of Appeal's judgment in *Halsey v Milton Keynes General NHS*,[14] the landmark case on ADR, blunts the pro-ADR messages that began to emerge in the early jurisprudence which developed shortly after the implementation of Lord Woolf MR's reforms to the civil justice system.[15] One particular aspect of the *Halsey* decision which undermines the ADR obligations of litigating parties is the guidance given on the approach the courts should adopt when assessing whether a successful party has behaved unreasonably in refusing ADR (the refusing party). If unreasonable refusal can be shown, then a court is at liberty to exercise its discretion on the issue of costs and penalise the refusing party accordingly (for example, by depriving the ***J.B.L. 648*** successful party of a portion of his costs which he would otherwise be entitled to).[16] The Court of Appeal in *Halsey* accepted the Law Society's[17] six non-exclusive factors which the courts should consider when determining an unreasonable refusal of ADR.[18] The second of those factors is whether the refusing party *reasonably believed* that he has a strong case when rejecting ADR (the merits factor). If that party can demonstrate a reasonable belief in the merits of his case then he will not be found to have behaved unreasonably and, consequently, will escape being penalised in costs. The policy rationale underpinning the merits factor is that the party proposing mediation could use the threat of costs sanctions to obtain a nuisance-value offer and force a settlement in a case lacking merit.[19]

In formulating the merits factor, the court in *Halsey* reversed the principle established in the earlier decision of *Hurst v Leeming*,[20] in which Lightman J stated that a litigating party's belief in the merits of his case *would not* be sufficient justification for refusing mediation. However, even though the *Hurst* principle was reversed in *Halsey*, this article reveals that a review of the jurisprudence surrounding the merits factor indicates the emergence of two distinct judicial approaches to its application. The first approach is consistent with the *Hasley* decision in that it follows and applies the test of reasonable belief, a test which sets a relatively low threshold for a refusing party to satisfy. The second approach, however, departs from the *Halsey* -type approach and is consistent with that advocated in *Hurst* .[21] The policy rationale which appears to justify the *Hurst* -type approach is grounded on the practical benefits of ADR in resolving civil disputes.

Given the existence of these diverging judicial approaches to the interpretation and application of the merits factor, a number of immediate questions arise. To what extent are these diverging judicial approaches "fit for purpose" in assessing whether there has been an unreasonable refusal of ADR? Do these approaches strike a fair balance between an informed and justified decision by the refusing party to turn down ADR on the one hand and the need to penalise a refusing party in costs for unreasonably refusing ADR on the other? And are the policy reasons underpinning both approaches (the need to guard against unmeritorious claims and the emphasis upon the potential benefits of engaging with ADR) justifiable, and do they hold weight?

This article critically reviews the merits factor and analyses the two diverging judicial approaches. It will be argued that the *Halsey* approach of "reasonable belief" not only sets an artificially low threshold which most refusing parties are capable of satisfying, but the policy rationale upon which the merits factor rests is unsound because it places disproportionate emphasis upon the potential dangers posed to a refusing party in having to make a nuisance payment. The focus on the need to protect "vulnerable" public bodies from being potentially forced into a settlement has the effect of potentially allowing those organisations to invoke the ***J.B.L. 649*** merits factor in their defence to an otherwise justifiable costs penalty. This article will assert that the *Hurst* -type approach also has a number of shortcomings. It is too dismissive of the potential relevance of the merits factor in circumstances in which a refusing party may be justified in turning down ADR, and places disproportionate emphasis upon the practical benefits of ADR in resolving the dispute between the parties. It will be argued that a reformulation of the merits factor is necessary.

The first part of this article provides the theoretical underpinnings to judicial approaches towards ADR within the English civil justice system. The second part will critically analyse the merits factor and its underlying policy rationale. The third part examines the jurisprudence surrounding the merits factor and will explore the application of the *Halsey* approach and the emergence of a *Hurst* -type approach. The third part will also adopt a comparative perspective by considering judicial approaches to the merits factor in Hong Kong. Finally, the fourth part concludes by reflecting upon the potential for reform.

Judicial perceptions of ADR within the English civil justice system

Lord Woolf provided ADR with an enhanced role within the court rules and, as a consequence, ushered in a more formal and structured approach to the promotion and encouragement of consensual settlement within the English civil justice system. However, Lord Woolf's philosophy of encouraging the early settlement of civil disputes was not novel. The authors of the Heilbron-Hodge Report,[22] who were commissioned to investigate the implementation of previous civil justice reforms,[23] had already sown the seeds for Lord Woolf's reforms on the issue of settlement and ADR some three years prior to the Woolf reforms. It was the Heilbron-Hodge report which first advocated the need for a radical change in approach to civil justice. It did so by breaking away from the approaches taken by previous, failed, reforms which had concentrated primarily upon recommending structural changes to the system. Unlike previous reforms, the Heilbron-Hodge Report focused on recommending a change in litigation *culture*. In doing so the authors of the Report proposed an alternative aim of the justice system, from a system which existed for the vindication and enforcement of rights to one which also encouraged the early settlement of disputes.[24] But this did not mean that the encouragement of early settlement would somehow rank in priority or indeed equally to the need for the civil justice system to provide substantive justice (by which we mean the application of right law to the true facts).[25] The overarching aim of the civil justice system would remain, according to the Heilbron-Hodge report, the dispensation of substantive justice as it had done since the reforms introduced by the Judicature Act 1873 and 1875. ***J.B.L. 650*** [26]

The Heilbron-Hodge Report's recommendations, that a change in the method in which litigation should be conducted, was swiftly embraced and taken further by Lord Woolf. Consistent with his predecessors, he did not advocate that early settlement should in any way replace the principal aim of the justice system; it did not seek to replace or diminish the constitutional role of the courts in providing substantive justice, although now the purpose of civil justice was not simply to achieve substantive justice. According to Lord Woolf, the aim of the civil justice system included an equal commitment to procedural justice.[27] Procedural justice dictates that substantive justice can only be dispensed by the use of *proportionate* court and litigation resources and within a reasonable time. The defining feature of the new Woolfian procedural landscape was the overriding objective of enabling the courts to deal with cases justly.[28] As Sorabji remarks, the Woolfian overriding objective was truly innovative because it introduced a new concept of justice which was "committed to proportionality rather than … an unalloyed commitment to the achievement of what Woolf described as substantive justice …".[29]

Despite his enthusiasm for ADR, Lord Woolf did not recommend that ADR be made compulsory.[30] This was so because of the strongly held belief that citizens should never be denied their right to access the courts, nor should obstacles be placed in their way which might endanger that right. All are considered to be equal before the law and all should be allowed equal access to the law. As Lord Diplock put it in *Bremer Vulcan v South India Shipping Corp Ltd*,[31] "every citizen has a constitutional right to access". The Heilbron-Hodge Report expressed it in the following manner:

"[F]undamental to the basic precepts of any civilised society that no section of the community should be excluded from their just entitlement to equality before the law, whether or not circumstances necessitate their using the courts …." [32]

In a similar vein but from a human rights perspective, Lord Dyson's obiter comments in *Halsey* ruled out the possibility that the court has jurisdiction to compel parties to engage in ADR: "to oblige truly unwilling parties to refer their disputes to mediation would be to impose an unacceptable obstruction on their right of access to the court."[33] Such an obstruction would contravene art.6 of the European Convention on Human Rights. However, this aspect of *Halsey* has been widely criticised for a number of reasons, and primarily for its incompatability with the European Court of Justice decision in *Alassinin v Telecom Italia SpA*. In that case, the ECJ held that a statutory obligation requiring the claimant to attempt ADR as a condition precedent to bring a claim in an Italian court *was* compatible ***J.B.L. 651*** with European law, and therefore with art.6 of the ECHR.[34] Indeed, more recently, Lord Dyson MR expressed his agreement with the ECJ decision in *Alassini* but contended that compulsory mediation was less efficient than voluntary mediation—compulsory mediation would add to the costs of the dispute.[35]

The message of caution in respect of ADR and the need to contain its expansion within the civil justice system has been voiced by Lord Neuberger. His Lordship has forcefully argued that ADR, a system which provides private benefits to individuals, is not, nor should it be, considered as a branch of the government. Although ADR has a part to play in the civil justice system it cannot provide the

formal adjudicative role in administering equity and the law. That can only be provided by the courts. ADR exists and provides private justice because it exists within the framework of law and its formal adjudication without which "there would be mere epiphenomena". [36]

Nevertheless, Lord Woolf's efforts in formally incorporating the encouragement of ADR within the Civil Procedure Rules greatly enhanced the role and importance of consensual settlement though ADR. ADR would no longer remain on the periphery of the civil justice landscape. It would now occupy a central role within Lord Woolf's new procedural "landscape" of judicial case management. Parties would be required, by virtue of specific provisions of the CPR, to seriously consider engagement with ADR both before and after proceedings are issued.[37] Lord Woolf made this clear in his *Final Report* when he explained that

"the court will encourage the use of ADR at case management conferences and pretrial reviews, and will take into account whether the parties have unreasonably refused to try ADR or behaved unreasonably in the course of ADR".[38]

And where parties had failed to discharge their "ADR obligations", the courts were given powers to penalise those parties through the making of adverse costs orders.[39]

The three major civil justice reforms which followed the Woolf reforms, the Jackson Review of Civil Litigation Costs, the Briggs Chancery Modernisation Review,[40] and more recently the Briggs CCSR also reinforced the importance of ADR. Consistent with Lord Woolf's philosophy that litigation should be concerned with the encouragement of early settlement,[41] Briggs LJ in his Chancery Modernisation Review Final Report[42] recommended a culture change in the Chancery Division's management of disputes so that courts managed disputes in the widest possible sense, which would include not only the determination and enforcement of rights via court adjudication but also through the consensual ***J.B.L. 652** settlement of disputes.[43] Remaining consitent with his philosophy of introducing a culture change, Briggs LJ in his CCSR stated that stage two of his proposed Online Court is "mainly directed to making conciliation a culturally normal part of the civil court process rather than, as it is, at present, a purely optional and extraneous process".[44]

There is a final important yet increasingly controversial ADR point to consider before proceeding to an analysis of the merits factor, and that is the status of tiered ADR clauses[45] (i.e. clauses requiring the parties to undertake one or more forms of ADR (typically negotiation or mediation) before commencing formal litigation or arbitration proceedings.). These types of clauses are becoming increasingly common in commercial contracts. Although it has been established that ADR clauses are legally binding,[46] the recent High Court decision in *Emirates Trading v Prime Mineral Exports* [47] has gone further in holding that a dispute resolution clause requiring the parties to seek to resolve a dispute by "friendly discussions" within a limited time period and in good faith before the dispute could be referred to arbitration was enforceable. The decision marks a clear departure from the general principle in English law that an agreement to negotiate is unenforceable.[48] The judge, Teare J, placed reliance on the use of the word "shall" in the clause, which he found to have created a mandatory, legally binding condition. In the judge's opinion such a binding requirement was consistent with public policy to give effect to dispute resolution clauses which require the parties to seek to resolve disputes before resorting to arbitration or litigation. However, the decision has been criticised on a number of grounds, including the potential adverse impact it may have (if followed in subsequent cases) on the practice of arbitration. [49] The decision can also be criticised for going too far and at the cost of certainty in requiring parties to comply with tiered ADR clauses before reverting to arbitration or the court process, and this can be seen by comparing *Emirates Trading* with the decision in *Cable & Wireless Plc v IBM UK Ltd*. In *Cable & Wireless* the court upheld an ADR clause in which the parties had agreed to negotiate in "good faith" and to resolve their dispute through a method recommended by a specific ADR provider. This was all sufficiently certain to make the clause enforceable. By contrast, the wording used in the tiered clause in *Emirates Trading* was too uncertain, but despite this Teare J appeared to have over-emphasised the policy of promoting settlement over the need to require parties to engage in ADR, but then to have the right to revert to the court or arbitral process.

Despite the consistent judicial support and encouragement of ADR, the landmark ADR case of *Halsey* has been perceived by some as raising unnecessary obstacles in the development and further integration of ADR within the civil justice system. ***J.B.L. 653** [50]

The merits factor—a critique

The previous section provided the background to the increased recognition and integration of ADR processes within the civil justice system. It presented the development of an increased judicial awareness of the nature of ADR and the potential benefits it could bring to the courts and the litigating parties. However, the Court of Appeal's decision in *Halsey* is a restraining force on the continued development of ADR within the civil justice system. One aspect of that restraining force is the merits factor, which, in its current form, is no longer a viable criterion to assess a party's unreasonable refusal to engage in ADR. This part will critically analyse the merits factor as it was dealt with in the *Hurst* decision, its "modification" by the Court of Appeal in *Halsey*. It will also critically consider the underlying policy rationale for its existence and consider judicial approaches to the merits factor in Hong Kong.

Hurst, Halsey and the merits factor

Hurst was one of the earliest ADR decisions following the Woolf reforms. It concerned an action brought by the claimant against his barrister for professional negligence. The claimant and defendant both applied for summary judgment. At the hearing of the summary judgment application, the claimant conceded that his claim was without merit but he contended that the defendant was not entitled to recover his costs in the usual manner because he had refused the claimant's suggestion to proceed to mediation. Lightman J dismissed the claimant's application and made a number of significant comments in his judgment regarding the role and growing significance of ADR within the civil justice process. According to Lightman J, although mediation was not compulsory, ADR was "at the heart of today's civil justice system",[51] and any failure by the parties to give proper attention to it would result in adverse cost consequences. He dismissed the relevance of the party's belief in the merits of his case when it came to assessing whether the refusing party had been justified in rejecting mediation. Lightman J said:

"The fact that a party believes that he has a watertight case again *is no justification* for refusing mediation. That is the frame of mind of so many litigants." [52]

Although accepting that a party may refuse mediation if there was no real prospect of success, Lightman J stressed that a refusal would be "a high risk course to take". He placed particular emphasis upon the practical benefits of mediation when making an objective assessment of the prospects of mediation:

"*[T]he starting point must surely be the fact that the mediation process itself can and does often bring about a more sensible and more conciliatory attitude on the part of the parties* than might otherwise be expected to prevail before the mediation, and may produce a recognition of the strengths and weaknesses ***J.B.L. 654*** by each party of his own case and of that of his opponent, and a willingness to accept the give and take essential to a successful mediation. *What appears to be incapable of mediation before the mediation process begins often proves capable of satisfactory resolution later*." [53]

It was only on the exceptional facts of the case in *Hurst* that the defendant was found not to have behaved unreasonably in refusing mediation. This was so because the claimant had lost all of his previous actions against the defendant and other parties and was, as the judge put it, "a person obsessed with the injustice which he considers has had been perpetrated on him and is incapable of a balanced evaluation of the facts".[54]

Lightman J's dictum made clear that whether a party's belief that he had a watertight case was reasonable or not was no justification for refusing mediation. Lightman J's dictum is not only consistent with the pro-ADR stance adopted by the senior judiciary shortly after the Woolf reforms, but it appeared to go further by explicitly dismissing the relevance of a party's belief in assessing an unreasonable refusal: what is significant is the need to give proper consideration to ADR regardless of whether a party's belief in the strengths of his case was reasonable or not. As a consequence, Lightman J elevated the requirement to give proper attention to ADR above and beyond any other factors which may justify a refusal, and this approach is consistent with his earlier bold and rather unorthodox pronouncement that ADR was at the heart of the civil justice system. Another interesting feature is the formulation of the policy rationale to justify his approach to the merits factor. That policy is based entirely on the potential practical benefits of mediation and its potential in resolving the dispute between the parties. Where ADR provides a realistic prospect of success but is not pursued, then, as Lightman J makes clear, "there is a real possibility that adverse consequences may be attracted",[55] one of which is to penalise the refusing party in costs. The basic logic goes that had the

refusing party considered ADR and engaged with it, then the parties would have benefited in a number of ways, including the possible settlement of the case.

Halsey concerned two personal injury cases that were heard together in the Court of Appeal. In both cases the claimant had, in the course of proceedings, invited the defendants to mediate their dispute and in both cases the defendants had refused but went on to win at first instance. The first instance judges awarded costs to the defendants despite the fact that the defendants refused to mediate earlier on in the proceedings. The claimants appealed on the issue of costs. The critical question for the Court of Appeal was this: when should the court impose a costs sanction against a successful litigant on the grounds that he has refused to take part in an ADR process?

Dyson LJ (as he then was), giving the leading judgment of the court, upheld the decisions at first instance and dismissed the claimants' appeals. His Lordship was of the opinion that the defendants should not be deprived of any of their costs on the ground that they had refused to accept the claimants' invitations to agree to mediation. The general rule that costs follow the event (i.e. the loser pays the ***J.B.L. 655*** winner's costs) should not be departed from unless it is shown that the successful party acted unreasonably in refusing to agree to ADR. He went on to explain that, in assessing an unreasonable refusal, the court will consider all of the circumstances of the case including the following six non-exclusive factors:

1. the nature of the dispute;

2. the merits of the case;

3. whether other settlement methods have been attempted;

4. whether the costs of mediation would be disproportionately high;

5. whether any delay in setting up and attending ADR would have been prejudicial;

6. whether the ADR process has a reasonable prospect of success.

Dyson LJ explained the relevance of the merits factor:

"The fact that a party *reasonably believes* that he has a strong case is relevant to the question whether he has acted reasonably in refusing ADR. If the position were otherwise, there would be considerable scope for a claimant to use the threat of costs sanctions to extract a settlement from the defendant even where the claim is without merit. Courts should be particularly astute to this danger. Large organisations, especially public bodies, are vulnerable to pressure from claimants who, having weak cases, invite mediation as a tactical ploy. They calculate that such a defendant may at least make a nuisance-value offer to buy off the cost of a mediation and the risk of being penalised in costs for refusing a mediation even if ultimately successful … In *Hurst v Leeming [2003] 1 Lloyd's Rep 379, 381* Lightman J said: 'The fact that a party believes that he has a watertight case again is no justification for refusing mediation. That is the frame of mind of so many litigants.' In our judgment, this statement should be qualified. The fact that a party *unreasonably* believes that his case is

watertight is no justification for refusing mediation. But the fact that a party *reasonably believes* that he has a watertight case may well be sufficient justification for a refusal to mediate." [56]

The test of "reasonable belief"

The merits factor and its underlying policy raise a number of concerns which cast serious doubts as to whether, in its present form, it should continue to be a factor which the courts may consider when determining an unreasonable refusal. One of the principal weaknesses of the merits factor is that it does not accord with the realities of litigation; that is to say, it fails to appreciate that the vast majority of those who commence and defend proceedings do have at least a *reasonable belief* that they have a watertight case, otherwise why would they incur the substantial cost and time of engaging with the court process? Thus, the threshold set by the merits factor of reasonable belief in a watertight case is artificially low and can easily be met by most litigants who may escape cost penalties which would otherwise apply. Further, the policy rationale appears to overstate the potential risk of a party being forced into an ADR procedure and having to make a nuisance payment. As such it fails to appreciate the very nature of ADR procedures, as being ***J.B.L. 656*** consensual processes from which either party is free to withdraw from before a settlement is concluded: there is no compulsion to settle. These concerns will now be considered in detail.

Dyson LJ's "qualification" of Lightman J's dicta in the earlier case of *Hurst* had the effect of reversing the principle that a litigating party's belief in the merits of his case *would not* be sufficient justification for refusing mediation. The diverging approaches towards the merits factor as propounded by Dyson LJ and Lightman J is illustrative of the opposing judicial attitudes towards the extent to which litigating parties must consider ADR. As noted previously, Lightman J's approach dismissed any consideration of a party's belief that his case is watertight: parties should consider ADR. Further, Lightman J's approach to the merits factor was consistent with the approach advocated by the Court of Appeal in the case of *Dunnett v Railtrack*,[57] which was decided not long before *Hurst*.[58] However, the Court in *Halsey* failed to deal with Lightman J's dictum in the light of the decision in *Dunnett*, a case which placed greater emphasis on the parties' obligation to pay careful attention and to consider ADR as an option in settling their dispute rather than simply dismissing it on the basis of the parties' belief in the merits of their respective cases.

In *Dunnett* the Court of Appeal dealt with the issue of the defendant's unreasonable refusal to consider mediation. The defendant had been successful in defending an appeal by the claimant and sought its costs of the appeal, but had previously rejected an invitation by the claimant to seek a settlement through mediation, an invitation which had also been recommended by the judge granting permission to appeal. In the Court of Appeal, the defendant argued that it did not engage in mediation because it was not willing to offer more than what it had previously offered the claimant by way of settlement. Brooke LJ rejected the defendant's arguments and penalised it by refusing to award its costs. He observed that the defendant had been wrong in rejecting mediation out of hand even though it did not consider that it would bring about a settlement of the matter. In Brooke LJ's opinion, this was a misunderstanding of the purpose of ADR. He emphasised the need for the courts to further the overriding objective through active case management, which included encouraging the parties to consider ADR procedures and for the parties to also further the overriding objective in this respect. In disallowing the defendant's costs, he concluded with this warning:

"It is to be hoped that any publicity given to this part of the judgment of the court will draw the attention of lawyers to their duties to further the overriding objective in the way that is set out in CPR Pt 1 and to the possibility that, *if they turn down out of hand* the chance of alternative dispute resolution when suggested by the court, as happened on this occasion, they may have to face uncomfortable costs consequences." [59]

Brookes LJ's reference to an invitation of ADR being turned down "out of hand" indicates that litigating parties would, at least after *Dunnett*, be required to carefully consider ADR, regardless of their views on the merits of their case. Therefore, ***J.B.L. 657*** although Railtrack, the defendant, had been successful on the merits at first instance and therefore would have been justified in its confidence in success on appeal, it was still obliged to give careful consideration to ADR. Thus, Lightman J's subsequent dictum in *Hurst* is consistent with the approach taken by the Court of Appeal in *Dunnett*: although a party may consider it has a watertight case, he must continue to give proper consideration to ADR and its potential in resolving the dispute.

It is also submitted that the merits factor threshold is questionable in light of the Court of Appeal's

recent judgment in *PGF II SA v OMFS Co1 Ltd*.[60] In that case the court formally endorsed the advice given in the *ADR Handbook* [61] that silence in the face of invitations to participate in ADR is, as a general rule, unreasonable. Briggs LJ, giving the leading judgment of the court, held that

"this case sends out an important message to civil litigants, requiring them to engage with a serious invitation to participate in ADR, *even if they have reasons which might justify a refusal*, or the undertaking of some other form of ADR, or ADR at some other time in the litigation. To allow the present appeal would, as it seems to me, blunt that message." [62]

The decision is significant because it formally extends the *Halsey* guidelines by recognising that a party cannot simply consider a call to ADR and remain silent; if he did, then this would be deemed as an unreasonable refusal and would justify that party being penalised in costs.[63] It follows that a party *must* actively engage with a call to ADR and to respond in a constructive manner to that call. Silence in the face of a call to engage in ADR is counter to the very nature of ADR, which is perceived as a mechanism which breaks down the adversarial barriers between litigating parties and one which promotes an atmosphere of co-operation which may assist the parties in settling their dispute. Although in the previous case of *Rolf v De Gerin* [64] Rix LJ made reference to the claimant's offer of mediation being "spurned" by the defendant (the defendant had failed to provide any reasons for rejecting mediation), which was unreasonable, *PGF* was the first case in which the Court of Appeal *officially* recognised that silence to a call to ADR *will be* considered as unreasonable behaviour and will attract adverse costs consequences.

The decision in *PGF* is also significant for other reasons. Briggs LJ places a strict obligation on the parties to consider ADR. His Lordship made clear that a party who has been invited to engage in ADR will be expected to *seriously engage* with that invitation regardless of whether that party has valid, justifiable reasons to refuse the invitation. By endorsing the principle that silence can amount to unreasonable refusal, Briggs LJ placed the burden on the "silent" party to ensure that he has adequately discharged his ADR obligations. Here parallels can be drawn ***J.B.L. 658*** between Briggs LJ's decision in *PGF* on the issue of silence and the approach adopted by the courts in *Dunnett* and *Hurst* on the issue of a party's belief in the merits of his case. *Dunnett* and *Hurst* were consistent in making clear that a party was under a strict obligation to pay proper attention to ADR, this obligation being rationalised on the grounds that the practical benefits meant that a dispute could be resolved with the assistance of a neutral third party. Similarly, *PGF* places a strict obligation on the silent party to positively engage with an ADR invitation regardless of any reasons to the contrary, which would include the silent party's conviction that he has a watertight case.

Policy rationale of the merits factor

The policy rationale which underpins the merits factor—the policy of avoiding a party being forced into a settlement by unmeritorious claims—is weak. The idea that a party, whether it be a public body, an individual or a corporation, is in need of being protected from potential unmeritorious claims gives the misleading impression that a party proposing ADR will, in all cases, be seeking a financial settlement. Although it is true to say that the majority of civil disputes that engage ADR, whether it be negotiation, mediation or any other type of ADR process, will involve some form of financial payment in resolving the dispute, this is not true of all cases. It may be that a claimant simply wishes for an apology or he may be satisfied with a settlement such as the restoration of trading relations which does not necessarily involve the payment of money by way of settlement.

Brooke LJ in *Dunnett* highlighted the wider benefits which mediation could offer the parties when he said:

"A mediator may be able to provide solutions which are beyond the powers of the court to provide. Occasions are known to the court in claims against the police, which can give rise to as much passion as a claim of this kind where a claimant's precious horses are killed on a railway line, by which an apology from a very senior police officer is all that the claimant is really seeking and the money side of the matter falls away." [65]

Further, the policy rationale fails to appreciate the very nature and function of ADR processes such as mediation and negotiation, the most common forms of ADR procedures that are utilised in civil disputes. Those procedures are non-adjudicative and purely consensual, and as such the disputing parties are at liberty to engage in those procedures. If the parties decide to refer their dispute to an ADR procedure, then they are free to withdraw from that procedure at any time before a final

settlement is concluded. Thus, the (misleading) impression given by the merits factor policy is that "vulnerable" parties will be forced to engage with ADR *and to settle*, by making a monetary payment, to an unmeritorious claimant. ***J.B.L. 659***

The merits factor in Hong Kong

Shortly after the implementation of the Woolf Reforms, Hong Kong conducted an extensive investigation into its civil justice system and drew on some of the practices in England, including ADR. The Chief Justice of Hong Kong established the Working Party on Civil Justice Reform which was, similarly to Lord Woolf's terms of reference, tasked with reviewing "the civil rules and procedure of the High Court and to recommend changes thereto with a view to ensuring and improving access to justice at reasonable cost and speed".[66] The recommendations of the Working Party were finally published in the Civil Justice Reforms Final Report in 2004. As part of its proposals for reform, it recommended continued judicial encouragement of ADR with the use of costs sanctions for an unreasonable refusal to engage with ADR.[67] In 2010 a new court rule on mediation, Practice Direction 31,[68] was introduced, which applies to all civil proceedings in the Court of First Instance and the District Court. The Hong Kong courts have referred to *Halsey* when considering Practice Direction 31 and, although *Halsey* is not binding on the courts in Hong Kong,[69] it continues to remain relevant when the courts are required to consider the issue of potential cost sanctions in circumstances where there may have been an unreasonable refusal to consider ADR.[70]

The merits factor was considered by the High Court of Hong Kong in the case of *Golden Eagle International (Group) Ltd v GR Investment Holdings Ltd*.[71] In that case the defendant had, on two occasions, refused to engage in mediation. Eventually the parties agreed on the judgment sum and costs in favour of the claimant. The agreed sum was higher than the sum which the claimant had previously offered the defendant to settle the matter, and this led to the claimant applying to the court for enhanced interest on the damages and costs on an indemnity basis. The defendant contended, inter alia, that it had refused to engage with mediation because it reasonably believed that it had a strong case and that it had based its decision on commercial considerations. The court rejected the defendant's arguments. Having cited the relevant passage from Dyson LJ's judgment in *Halsey*, Lam J doubted whether the policy rationale of the merits factor would be relevant to Hong Kong cases. Lam J argued that the costs sanction was only applicable if a party refuses to mediate. There was no costs sanction if the parties cannot reach settlement after making a reasonable effort in mediation. The judge went on to note that, pursuant to Practice Direction 31, a party may avoid being penalised in costs after they have participated in mediation up to the agreed minimum level of participation. Further, the costs involved in such participation in Hong Kong would usually not be high enough to encourage such ***J.B.L. 660*** nuisance claims. Finally, Lam J observed that in Hong Kong the costs of mediation can be included as part of the legal costs and recoverable by the successful party if the mediation were unfruitful.[72]

In the subsequent case of *Goodtry Investments Ltd v Easily Development Ltd*,[73] Tracy Chan J followed Lam J's reasoning in *Golden Eagle* in rejecting the claimant's contention that it did not participate in mediation because it had a strong case. He found that liability was not a "clear cut matter" and therefore he was not convinced that the claimant had a good reason to refuse mediation.

There are two interrelated issues which should be noted when comparing the Hong Kong approach to the English approach to the merits factor. First, the Hong Kong approach is similar to the *Hurst* -type approach in that it is dismissive of a refusing party's arguments in rejecting ADR, even though there may exist strong reasons, including commercial considerations, for that rejection. Secondly, although Practice Direction 31 of the Hong Kong court rules *encourages* ADR, judicial approaches in both *Golden Eagle* and *Goodtry Investments* appear to adopt a strict and rigid approach to ADR and one which fails to appreciate the potential wasted costs to the parties in circumstances in which it was reasonable to refuse to engage with ADR.

The jurisprudence—diverging judicial approaches

This part critically considers the development of the jurisprudence surrounding the merits factor. As will be shown, an analysis of the jurisprudence reveals the emergence of two distinct judicial approaches to the application of the merits factor. First, the jurisprudence which developed immediately after *Halsey* demonstrates a consistent judicial approach to the application of the merits factor. The second pattern which emerges from more recent jurisprudence indicates judicial

willingness to adopt an approach which is similar to that advocated by Lightman J in *Hurst* by dismissing a party's belief in the strengths of his case (even though the facts may justify the party's belief) and placing greater emphasis on the practical benefits of ADR and the potential it offers in resolving disputes when assessing an unreasonable refusal.

It will be recalled that in *Dunnett* Brooke LJ made an order which deprived Railtrack of its costs of the appeal owing to its unreasonable behaviour in refusing to engage with mediation. The court penalised Railtrack despite the fact that the claimant had twice lost on the merits. In arguing that Railtrack should have taken part in mediation, Brooke LJ emphasised the beneficial role a mediator could play in resolving a matter when he stated that

"skilled mediators are now able to achieve results satisfactory to both parties in many cases which are quite beyond the power of lawyers and courts to achieve … But when the parties are brought together on neutral soil with a skilled mediator to help them resolve their differences, it may very well be that *the mediator is able to achieve a result by which the parties shake hands* ****J.B.L. 661*** *at the end and feel that they have gone away having settled the dispute on terms with which they are happy to live*".[74]

Therefore, regardless of the party's belief in the strengths of its case, the policy of early settlement, as advocated by Lord Woolf and the Heilbron-Hodge Report before him, and the need to properly consider mediation, which *could* bring about a resolution of the matter, took precedence over a party's belief in the merits of his claim. And, as discussed earlier, Lightman J's dictum in *Hurst* in dismissing the relevance of a party's belief in the strengths of his case is in line with the approach in *Dunnett*. Stressing the benefits which mediation presented to the parties in resolving their disputes, Brooke LJ went on to explain that Railtrack's belief in the strengths of its case appeared to show

"a misunderstanding of the purpose of alternative dispute resolution. Skilled mediators are now able to achieve results satisfactory to both parties in many cases which are quite beyond the power of lawyers and courts to achieve".[75]

It should be noted that there have been occasions, shortly after the Woolf reforms took effect, in which the courts have decided *not* to penalise a refusing party in costs for failing to engage with ADR. However, the facts of those cases are unusual and distinguishable. They indicate that the party proposing mediation had acted in an intimidatory and aggressive manner and that this was a major factor which had led the courts in finding that the refusing party had not acted unreasonably.

The first case is *Society International de Telecommunications Aeronautiques SC v Wyatt Co (UK) Ltd*.[76] In that case the defendants had settled with the claimant and then sought a contribution from its subcontractor via a Pt 20 claim which failed. On the issue of costs the defendants contended that the subcontractor ought to be deprived of its costs for declining to participate in mediation on three occasions before the case came to trial. The defendants relied on *Dunnett* and *Hurst* in support of its arguments. The judge, Park J, dismissed the defendant's submissions and, having carefully dissected the correspondence which had passed between the parties on the issue of mediation, set out five detailed reasons which justified the subcontractors' refusal to engage in mediation. Of particular importance was Park J's finding that the defendants were only interested in mediation in order to obtain a large financial contribution, and that they had failed to show that they would be interested in resolving the dispute. The manner in which the defendants were inviting the subcontractors to mediation was, as Park J put it, "disagreeable and off-putting", and this distinguished this case from *Dunnett* and *Hurst*.

In *Allen v Jones*,[77] a dispute over a right of way, the court awarded a successful defendant's costs in full. The judge found that the claim had been without merits and there was no issue of conduct or question that the defendant's decision was anything other than proportionate. In such cases, the judge held, the failure to submit to a request for mediation by the unsuccessful party ought not, as a matter of principle, of itself result in the successful party being deprived of the normal order for costs. Although *Allen* may be viewed as a *Halsey* -type case in that it ****J.B.L. 662*** places weight in favour of a successful party relying on the merits factor, one aspect of the judgment makes particularly interesting reading, and that is the conduct of the party proposing mediation. In *Allen* the judge found that the claimant's correspondence in which mediation was proposed was "highly intimidatory" and, relevant to the court's assessment of costs under the CPR, "its intimidatory nature and the fact that the claimants did not seek mediation before issuing proceedings calls into question in my mind whether the change in attitude … was genuine rather than tactical".[78]

A divergence from the pro-ADR judicial stance can be seen to emerge shortly after *Halsey* and the impact of the decision on judicial approaches to the application of the merits factor. The courts appear

to adopt a more relaxed position in respect of the merits factor, with the consequence that a refusing party can escape cost sanctions on the grounds that, adopting a wider interpretation of the merits factor, he has a reasonable belief in the strengths of his case. This is well illustrated by the Court of Appeal case of *Reed Executive Plc v Reed Business Information Ltd*.[79] The defendant had been successful in its appeal and the claimants applied for 70 per cent of their costs at first instance and in the Court of Appeal on the basis that the defendant had unreasonably refused ADR. The court dismissed the claimant's application and found that the defendant had not acted unreasonably in refusing ADR because it had a reasonable belief in the strengths of his arguments. Jacob LJ, giving the leading judgment, emphasised the significance of the merits factor in reaching his decision when he said:

"Far from being unreasonable I think it was entirely reasonable for RBI to pursue the appeal. They had at least a reasonable (and as it turned out justified) belief in their prospects. For all I know they had been advised they had a very good or even watertight case. They had ongoing disputes in other jurisdictions to consider. It may be that an ADR process would have worked, but the prospects did not look good given the wide disparity between the parties. Moreover the case was full of novel points … this would have made it much trickier to formulate any deal." [80]

Although Jacob LJ took account of the prospect of success of mediation, he particularly focused on the merits factor. However, on the issue of the court's application of the merits factor, the decision in *Reed* is unsound for a number of reasons. The first is an obvious one: the court's decision indicates a failure to appreciate the practical benefits of involving a trained mediator to resolve complex disputes to the satisfaction of the parties. It too readily assumes that cases with novel points, complex issues and where parties are too far apart are not suitable for ADR. The benefits of ADR over the adjudicative court process have been discussed earlier in this article.[81]

These benefits were recognised and reiterated by a number of important Court of Appeal authorities. In *Cowl v Plymouth City Council*,[82] a case involving a dispute between a public body and an individual, Lord Woolf MR stressed that disputing ***J.B.L. 663*** parties must be conscious of the contribution ADR can make to resolving disputes in a manner which both meets the needs of the parties and the public, and saves time, expense and stress. If litigation is necessary, then, Lord Woolf MR argued, the courts should deter the parties from adopting an unnecessarily confrontational approach to the litigation. Further, in *Burchell v Bullard* [83] Ward LJ did not hesitate in expressing his strong opposition to the contention that the defendant had a strong case and that, in any event, the issues were far too complex to be resolved through mediation. The defendants had only escaped from not being penalised in costs because their unreasonable refusal of mediation had pre-dated *Halsey*. Ward LJ nevertheless expressed his disapproval of the defendants' arguments in the following manner:

"[T]he merits of the case favoured mediation. *The defendants behaved unreasonably in believing, if they did, that their case was so watertight that they need not engage in attempts to settle*. They were counterclaiming almost as much to remedy *some* defective work as they had contracted to pay for the whole of the stipulated work. *There was clearly room for give and take. The stated reason for refusing mediation that the matter was too complex for mediation is plain nonsense*".[84]

More recently, the courts have been, in some instances, generous in giving weight to the merits factor. In *ADS Aerospace Ltd v EMS Global Tracking Ltd* [85] the court, when applying the *Halsey* factors, found that the defendant had not behaved unreasonably in refusing the claimant's invitation to mediate. The claimant's $16 million claim, which was for breach and repudiation of an agreement between the parties for the exclusive distribution of satellite tracking devices for aeroplanes or helicopters, was dismissed. The court was required to decide on the issue of costs.

The parties provided the court with information about what was going on behind the scenes with regard to trying to settle the case. The defendant's solicitors had proposed that the parties engage in settlement discussions, but the claimant wanted to wait until the exchange of witness statements. The defendant later offered to settle the claim on a without-prejudice basis but the claimant failed to provide a response and later, during a telephone discussion with the defendant, the claimant did not demonstrate any intention to settle the matter. Later, the claimant rejected the settlement offer which had been made and suggested that the parties engage in mediation. The defendant wrote back and referred to the previous history and stated that: it did not feel that mediation would be worthwhile and that both parties were now aware of each other's case; the time and cost of mediation would be wasted; and that the claimant was not likely to accept less than $16 million.

Despite this, the defendant indicated that it would consider any reasonable offer which the claimant might make on a without-prejudice basis. The claimant replied by stating that there was a reasonable prospect of settling the claim and that a skilled mediator would be capable of settling the matter. The defendant wrote back reiterating its previous position that a formal mediation was not necessary, especially given the fact that it was now three weeks before the commencement ***J.B.L. 664*** of the trial. The claimant then offered to settle the matter and repeated its invitation for the parties to engage in mediation. The defendant replied with a counter-offer which was substantially less than the claimant's offer. Neither of the offers was accepted and the matter proceeded to trial.

The claimant accepted that prima facie the defendant is entitled to its costs, but said that the defendant acted unreasonably in refusing its request to attempt to settle the dispute in mediation. The defendant said that it acted reasonably in all the circumstances. Akenhead J agreed with the defendant. In applying the *Halsey* factors, Akenhead J held that the defendant did not act unreasonably in believing that it had a very strong case both on liability, causation and quantum. There were very real difficulties apparent in the claimant's case on repudiation and the damages claim was demonstrably overstated (worth no more than about $400,000 rather than the $16 million claimed). Akenhead J was of the opinion that:

"It might be said that a good mediator would have been able to 'work on' the Claimant to accept what would in effect be a nuisance offer but, in the context of this case, with the sensible solicitors and counsel (who the Claimant did engage in this case), I have no doubt that without prejudice discussions would probably have achieved the same result or at least got to the same stage." [86]

Swain Mason v Mills & Reeves (A Firm) [87] involved a protracted professional negligence dispute against solicitors which eventually failed. However, the unsuccessful claimants had, in fact, succeeded on a number of issues. Therefore, on the issue of costs the trial judge awarded the successful defendant 50 per cent of its costs. Although the judge had made reference to the defendant's failure to engage in mediation which had been suggested by the claimant during the proceedings, he failed to mention the extent to which this had impacted on his assessment of costs. The defendant appealed. The second ground of appeal, which is of relevance to this article, concerned the judge's discretion in awarding costs. The defendant contended that the judge had wrongly found that it had acted unreasonably in refusing mediation. Davies LJ, giving the leading judgment of the court, emphasised that where a party reasonably believes that he has a watertight case, that may well be sufficient justification for a refusal to mediate. Turning to the claimant's arguments that it had succeeded in some of its arguments and therefore the defendant could not be considered as having a "clean sweep" of the issues, Davies LJ simply stated that it was rare for a party to win on every point. His Lordship overturned the trial judge's estimate of where the reasonableness and unreasonableness of the defendants' refusal to mediate lay and increased the defendant's award of costs by 60 per cent.

Davies LJ's decision in *Swain Mason* is highly questionable. On the facts of the case the unsuccessful claimant had actually succeeded in some of its points and therefore the defendant did not have a watertight case. This meant that the defendant did not have a strong enough case to justify refusing to engage in mediation. Davies LJ's consideration of this issue failed to appreciate that this case would have been suitable for mediation because there were strengths and weaknesses in both parties' cases. This argument is consistent with a number of significant authorities. In ***J.B.L. 665*** *Leicester Circuits Ltd v Coates Brothers Plc*,[88] for instance, the Court of Appeal disapproved of the defendant's decision to withdraw from a mediation that the parties had arranged and rejected its argument that it would have been pointless to participate in it. Judge LJ was strongly of the conviction that, although it could not be assumed that the mediation would have succeeded, "there [was] a prospect that it would have done if it had been allowed to proceed". More recently, H.H. Judge Waksman QC in *Phillip Garritt-Critchley v Ronnan* [89] granted an indemnity costs order against the defendants for unreasonably refusing to engage in mediation. He rejected the defendant's contention that the claim did not provide any middle ground between the parties and that the defendants were confident that an agreement could not be reached by engaging in the mediation process: "To consider that mediation is not worth it because the sides are opposed on a binary issue, I'm afraid seems to me to be misconceived." It was only by sitting down and exploring a settlement that the parties could really ascertain how far apart they really were.

Recently, a pro-*Hurst* approach to the merits factor has emerged, an approach which diverts from that of *Halsey* and takes as its focus the (overly) optimistic view that the matter would have settled if the parties had engage with ADR. Thus, this pro-*Hurst* approach reverts to the exercise of dismissing out of hand the potential relevance of a party's belief in the strengths of his own case. Take, for example,

the recent Technology and Construction case of *Northrop Grumman v BAE Systems*,[90] which came before Ramsey J.

Northrop concerned Pt 8 proceedings in the court upheld BAE's contention that on a true construction of a licence agreement, BAE was entitled to terminate that agreement for convenience. In relation to costs, NGM accepted the principle that BAE was entitled to its costs to be assessed on a standard basis if not agreed, but contended that those costs should be reduced by 50 per cent by reason of BAE's unreasonable refusal to mediate the dispute.

BAE had previously, through the exchange of "without prejudice save as to costs" correspondence, offered to settle on the basis of no payment, with each party bearing their own costs. This offer was rejected by NGM, which referred to its offers of mediation.

In support of its contentions, NGM submitted, inter alia, that the dispute was suitable for mediation and the fact that the dispute involved matters of contractual construction did not make it unsuitable for mediation. The emphasis on, and the perceived benefits of, ADR had strengthened over the years and there was no objective reason why construction issues should not be amenable to mediation so that a skilled mediator could "hold up a mirror" to the parties respective arguments, and identify the risks and merits involved as in any other case. More importantly, NGM submitted that it is the reasonableness of a party's belief that it has a strong case which is of importance. NGM submitted that this was a case where the merits weighed in favour of ADR. Finally, NGM argued that the cost of litigation in the matter outweighed any costs which would have been incurred in engaging in mediation. ***J.B.L. 666***

BAE argued that it was a sophisticated commercial client with in-house counsel who considered mediation and its likelihood of achieving settlement, saving time, costs and obviating risks and the possibility that a skilled mediator could achieve a solution. In relation to the *Halsey* factors, BAE contended that NGM's case involved a relatively short point of contract interpretation on which a claim totalling more than £3 million depended. In relation to the merits of the case, BAE submitted that it reasonably concluded that this was not a borderline case. BAE and its external lawyers considered that BAE was correct as a matter of law and also had commercial merits of not paying for licences it did not require. It felt that by suggesting mediation, NGM were attempting to put pressure on them to settle a claim for which NGM had no prospect of success. However, Ramsey J held that, in itself, this was insufficient, and placed emphasis upon the practical benefits offered by mediation when he said:

"The authors of the *Jackson ADR Handbook* properly, in my view, draw attention at paragraph 11.13 to the fact that this seems to ignore the *positive effect that mediation can have in resolving disputes even if the claims have no merit*. As they state, a mediator can bring a new independent perspective to the parties if *using evaluative techniques* and not every mediation ends in payment to a claimant… *[On] the merits of the case, I consider that BAE's reasonable view that it had a strong case is a factor which provides some but limited justification for not mediating*." [91]

This was, Ramsey J stated, a case which was appropriate for mediation and where mediation had reasonable prospects of success. Was it unreasonable for BAE, which considered it had a strong case, to reject NGM's offer to mediate? Ramsey J concluded that it was:

"Where a party to a dispute, which there are reasonable prospects of successfully resolving by mediation, rejects mediation on grounds which are not strong enough to justify not mediating, then that conduct will generally be unreasonable. I consider that to be the position here." [92]

However, BAE's "without prejudice save as to costs" letter was a relevant factor to be taken into account, and this was an offer which NGM was not successful in bettering. NGM's conduct in not accepting that offer was similarly a matter to be taken into account. Ramsey J reasoned that a refusal to mediate means that the parties have lost the opportunity of resolving the case without there being a hearing. A failure to accept the offer had equally meant that the parties had lost the opportunity of resolving the case without a hearing. He took the view that, while mediation at an earlier stage might have avoided costs, if BAE had mediated even at a later stage its conduct would not have been unreasonable.

The decision in *Northrop* stands in contrast to that in *Swain Mason*. In *Swain Mason* the claimant had succeeded in some of its arguments but was unsuccessful in persuading the Court of Appeal that its offer to mediate should be given consideration in depriving the defendant of some of its costs. In fact, the court increased the defendant's costs recoverability by 10 per cent. *Northrop* takes the ***J.B.L. 667*** opposite approach, akin to that advocated by Lightman J in *Hurst*, an approach which pays little

or no regard to the merits factor but focuses on the parties' strict ADR obligations. And the policy upon which this approach rests is the same as the policy developed by the courts in *Dunnett*, *Hurst* and related cases, a policy which takes as its focus the potential practical benefits offered by ADR in resolving disputes. It assumes that had a dispute been referred to ADR then it would have settled.

Proposal and conclusion

This article has revealed a number of concerns in respect of the merits factors. The test of reasonable belief is far too lenient towards the refusing party, with the potential of enabling that party to escape being penalised in costs. The underlying policy rationale is also questionable. It appears to exaggerate the potential threat to refusing parties in the face of unmeritorious claims. It incorrectly assumes that a claimant will, in all cases referred to ADR, be seeking only a financial settlement. And the focus on "vulnerable" public bodies needing some form of enhanced protection is flawed and illustrates a misunderstanding of the legal and practical nature of ADR procedures and the rights of the parties before and during engagement with those ADR processes.

The *Hurst* -type approach and, similarly, the Hong Kong approach, of disregarding any consideration of the merits factor and the potential relevance it may have in the court's assessment of an unreasonable refusal, also has its shortcomings. The justification for the *Hurst* approach in giving weight to the practical benefits of ADR without adequately considering the possible relevance of the merits factor is unacceptable. It too readily dismisses the potential importance of a party's belief that he may have a watertight case and too readily assumes that ADR *would have* produced a resolution of the dispute.

Thus there is a clear need to strike a balance between the obligations of litigating parties to properly consider ADR as a potential means of resolving their disputes (thereby saving themselves and the court valuable time and cost) and the need for courts to consider and, in appropriate circumstances, give due weight to the merits factor when assessing an unreasonable refusal of ADR. This need is particularly significant in the light of Briggs LJ's proposed Online Court which further integrates ADR within the civil justice process and attempts to make ADR a cultural norm.[93] To achieve this balance, the merits factor and judicial approaches to its application must be reformed in three fundamental respects. First, explicit reference to the merits factor within the *Halsey* guidelines should be removed and should form part of the "all the circumstances of the case" element of the guidelines. Secondly, the merits factor should be modified so that the threshold of "reasonable belief" is replaced with a higher threshold of "strong belief". Finally, the "protection" offered to "vulnerable" public bodies should be removed.

The first element to reform would involve removing the merits factor from the list of *Halsey* factors but allowing the courts the discretion, when assessing an unreasonable refusal, to consider it as part of the "all the circumstances of the case" element of the *Halsey* guidelines. This change should be led by the Court ***J.B.L. 668*** of Appeal providing guidance and leadership in any future case on ADR and the interpretation and application of the *Halsey* factors. The effect of this approach would be that the merits factor would continue to be relevant to the issue of unreasonable refusal but in a less explicit manner than it is currently. This would mean that where there is a case in which a successful party has maintained a genuine and *strong belief* in the merits of his arguments against a very weak or unmeritorious claim, then the courts may still take that factor into account when assessing an unreasonable refusal. This would also mean that unmeritorious claims and those cases in which the party proposing ADR has done so in an intimidatory or aggressive manner (as was the case in *Société Internationale de Télécommunications Aéronautiques* and *Allen*) will be factors which the courts should take into account as part of assessing "all the circumstances of the case".

The first element has a number of benefits. Completely removing explicit reference to the merits factor would mean that it would no longer be a focal point for a refusing party and the courts when dealing with the issue of an unreasonable refusal. It will ensure that litigating parties do not attempt to invoke the merits factor by trying to meet a low threshold of "reasonable belief" to avoid having to consider and engage with ADR.

As well as removing explicit reference to it, the second element to reform of the merits factor would be to modify the test of "reasonable belief". The current threshold fails to accord with the realities of litigation, that parties who have engaged the adversarial process have, in the vast majority of cases, done so because they possess at least a reasonable belief that they have a watertight case. Therefore, to avoid the majority of refusing parties from meeting a low threshold, the test of

"reasonable belief" should be modified by replacing it with a higher test of "strong belief". Thus, a party seeking to rely on the merits factor would be obliged to meet a higher threshold in satisfying a court that its refusal to go to ADR was reasonable. Further, by maintaining a higher threshold of "strong belief", judicial approaches to the interpretation and application of the merits factor will be modified so that a narrower and more restricted approach is adopted when assessing an unreasonable refusal to ADR rather than the wider, more lenient approach which currently exists and has been taken up by the courts in cases such as *Reed* and *Swain Mason*.

Finally, an alternative approach should be taken when dealing with the merits factor and cases involving public bodies. The policy of protecting public bodies from unmeritorious claims has, as discussed earlier, the effect of indirectly permitting those parties in litigation to easily invoke and rely upon the merits factor and thereby avoid their obligations to properly consider ADR. To avoid this outcome, public bodies should not be afforded "protection" as provided by the current policy underpinning the merits factor. This is particularly so given the fact that cases involving public bodies incur public funds when participating in the litigation process. By their very nature, public funds should be conserved for the provision vital services to the public and to improve those services. Litigation is expensive and the complex and time-consuming adversarial system compounds the issue of expense. Support for this approach can be taken from *Cowl*, in which Lord Woolf MR stressed the need for public money to be saved through engagement with ADR and the avoidance of litigation: ***J.B.L. 669**

"The importance of this appeal is that it illustrates that, even in disputes between public authorities and the members of the public for whom they are responsible, insufficient attention is paid to the paramount importance of avoiding litigation whenever this is possible. Particularly in the case of these disputes *both sides must by now be acutely conscious of the contribution alternative dispute resolution can make to resolving disputes in a manner which both meets the needs of the parties and the public and saves time, expense and stress*." [94]

Removing any exceptions for public bodies would place them on an equal footing with other litigants who would have to demonstrate a strong belief that they have a watertight case. This approach would also be in line with the Government's commitments for its departments to resolve disputes through ADR.[95] In 2011 the Coalition Government renewed its "ADR Pledge" of 2001 with the publication of its "ADR Commitment", which requires

"government departments and agencies to be proactive in the management of disputes, and to use effective, proportionate and appropriate forms of dispute resolution to avoid expensive legal costs or court actions … This includes adopting appropriate dispute resolution clauses in all relevant government contracts".[96]

Both the *Hurst* - and *Halsey* -type approaches to the merits factor are unsatisfactory and both rest on weak policy grounds. As such, they pull in opposite directions on the ADR spectrum: dismissing any justification for refusing ADR on the one hand and setting a low threshold for refusing ADR on the other. It is only when the merits factor is fundamentally reformed that the courts can apply it in a more consistent and a fairer manner.

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1. I am very grateful to Dr John Sorabji and Professors Janet Ulph and Robert Merkin for their helpful and interesting comments on earlier drafts of this article. The usual disclaimer applies.

2. In June 2015, in his maiden speech as Justice Secretary, Michael Gove announced the planned closure of courts in an attempt to save costs and streamline the system; see http://www.lawgazette.co.uk/news/gove-admits-more-courts-will-close-in-efficiency-drive/5049558.article. For a detailed an interesting discussion of the effect of austerity-induced public spending cuts on the English civil justice system see J. Sorabji, "Austerity's Effect on English Civil Justice" (2015) 4 E.L.R. 159–173.

3. For example Briggs LJ spoke of the limited court resources now available in resolving disputes through formal adjudication and the need for parties to consider ADR in *PGF II SA v OMFS Co 1 Ltd [2013] EWCA Civ 1288: [2014] 1 W.L.R. 1386*. At [27] of his judgment, Briggs LJ held that "the constraints which now affect the provision of state

resources for the conduct of civil litigation (and which appear likely to do so for the foreseeable future) call for an ever-increasing focus on means of ensuring that court time, both for trial and for case management, is proportionately directed towards those disputes which really need it, with an ever-increasing responsibility thrown on the parties to civil litigation to engage in ADR …".

4. Sir Rupert Jackson in his review of civil litigation costs explained the importance of ADR when he stated: "ADR is relevant to the present Costs Review in two ways. First, ADR (and in particular mediation) is a tool which can be used to reduce costs. At the present time disputing parties do not always make sufficient use of that tool. Secondly, an appropriately structured costs regime will encourage the use of ADR." *Sir Rupert Jackson, Review of Civil Litigation Costs Final Report (14 January 2010), Ch.36, p.355*. See also Sir Rupert's recent book, *The Reform of Civil Litigation* (London: Sweet & Maxwell, 2016) and the comments of B. Rix, "The Interface of Mediation and Litigation" (2014) 80 Arbitration 21.

5. See the discussion of Lord Neuberger's opinions in the first part of this article.

6. *Lord Neuberger, "Equity, ADR, Arbitration and the Law: Different Dimensions of Justice", Fourth Keating Lecture, Lincoln's Inn (19 May 2010)*; *Lord Neuberger, "Has Mediation Had Its Day?", Gordon Slynn Memorial Lecture (10 November 2010)*. Also see the comments of Lord Phillips of Worth Matravers, "Alternative Dispute Resolution: an English Viewpoint" (2008) 74 Arbitration 406; Lord Clarke, "The Future of Civil Mediation" (2008) 74 Arbitration 419; and *G. Lightman, "Mediation: An Approximation to Justice" (28 June 2007), S.J. Berwin*, http://www.judiciary.gov.uk/Resources/JCO/Documents/Speeches/berwins_mediation.pdf [Accessed 11 August 2015].

7. *Lord Neuberger, "A View from on High", Civil Mediation Conference 2015 (12 May 2015)*, https://www.supremecourt.uk/docs/speech-150512-civil-mediation-conference-2015.pdf [Accessed 10 October 2016].

8. Children and Families Act 2014 s.10. Section 10 makes it mandatory for any party wishing to make a family application to attend a family mediation, information and assessment meeting. At this meeting the parties are provided with information regarding the mediation of family applications, ways in which such matters may be resolved other than through the courts, and to assess whether the particular matter is suitable for mediation.

9. See *Lord Faulks, "Mediation and Government" (19 June 2014)*, https://www.gov.uk/government/speeches/mediation-and-government [Accessed 10 October 2016].

10. Briggs LJ, Civil Court Structure Review: Interim Report (2015), Judiciary of England and Wales; Briggs LJ, Civil Court Structure Review: Final Report (2016), Judiciary of England and Wales.

11. *Jackson, Review of Civil Litigation Costs Final Report (14 January 2010), Ch.36, p.355*; and see the Briggs Review, discussed later. Also, see later for a detailed discussion of the jurisprudence.

12. *Lord Faulks, "Mediation and Government" (19 June 2014)*, https://www.gov.uk/government/speeches/mediation-and-government [Accessed 10 October 2016].

13. *N. Vidmar, "Procedural Justice and Alternative Dispute Resolution" in K. Rohl and S. Machura (eds), Procedural Justice (Aldershot: Ashgate, 1997), pp.121–136*.

14. *Halsey v Milton Keynes General NHS [2004] EWCA Civ 576; [2004] 1 W.L.R. 3002*.

15. *Lord Woolf, Access to Justice Interim Report (Lord Chancellor's Department, 1995) (Interim Report)*; and *Lord Woolf, Access to Justice Final Report (Lord Chancellor's Department, 1996), (Final Report)*.

16. There are two main principles which dictate which party should pay the costs of the proceedings. The first is that the costs payable by one party to another are at the discretion of the court; there is no automatic right to the recoverability of costs (Senior Courts Act 1981 s.51 and CPR 44.3(1)). The second principle is that the unsuccessful party will usually be ordered to pay the costs of the successful party; sometimes referred to as the usual costs order (also known as "costs follow the event").

17. The Law Society had intervened as an interested party and provided detailed submissions to the court.

18. Costs are dealt with under the Civil Procedure Rules Pt 44.

19. *Halsey v Milton Keynes General [2004] EWCA Civ 576; [2004] 1 W.L.R. 3002* at [18] (Dyson LJ).

20. *Hurst v Leeming [2002] C.P. Rep. 59 Ch D*.

21. Such as *Dunnett v Railtrack [2002] EWCA Civ 303; [2002] 1 W.L.R. 2434*.

22. *H. Heilbron and H. Hodge, "Civil Justice on Trial—A Case for Change", Joint Report of the Bar Council and Law Society (1993)*.

23. In particular the implementation of the recommendations of the *Civil Justice Review—The Report of the Review Body on Civil Justice (1988), Cmd 394*.

24. For a detailed and interesting account of the history of previous civil justice reforms, see *J. Sorabji, English Civil Justice after the Woolf and Jackson Reforms: A Critical Analysis (Cambridge: Cambridge University Press, 2014)*.

25. *J. Bentham, Rationale of Judicial Evidence in Bowring (ed.), The Works of Jeremy Bentham, Vol.6 (Edinburgh: William Tait, 1843), pp.212–213*.

26. Judicature Act 1873; Judicature Act 1875 Sch.1; SI (unnumbered) of 1883; SI 2145/1962; and SI 1776/1965.

27. *Lord Woolf, Interim Report (1995)*.

28. The pre-Jackson Overriding Objective under Civil Procedure r.1.1 (1) stated: "These rules are a new procedural code with the Overriding Objective of enabling the court to deal with cases justly."

29. Sorabji, "The Road to New Street Station: Fact, Fiction and the Overriding Objective" (2012) 86 European Business Law Review 77.

30. Although it is interesting to note that Lord Woolf alluded to the possibility of revisiting the idea of compulsory mediation when discussing his reforms in Hong Kong in 1996. Lord Woolf noted that, although he had not gone so far as to recommend compulsory mediation in the English system, he was "encouraged to think that that is something which I should look at again": *Lord Woolf, "A New Approach to Civil Justice", Hong Kong lecture (1996)*.

31. *Bremer Vulcan v South India Shipping Corp Ltd [1981] A.C. 909 HL* at 917.

32. *Heilbron and Hodge, "Civil Justice on Trial" (1993), paras 4–5*.

33. *Halsey v Milton Keynes General [2004] EWCA Civ 576; [2004] 1 W.L.R. 3002* at [9] per Dyson LJ.

34. *Rosalba Alassini v Telecom Italia SpA (C-317/08, C-318/08, C-319/08, C-320/08) EU:C:2010:146; [2010] 3 C.M.L.R. 17* at [37].

35. *Lord Dyson's Key Note Speech (delivered by Brian Speers) at the Belfast Mediation Conference (9 May 2014), "Halsey 10 Years On—the Decision Revisited", reported in The Writ, The Journal of the Law Society of Northern Ireland (May/June 2014)*, http://www.lawsoc-ni.org/publications/the-writ-magazine-/ [Accessed 11 August 2015].

36. *Lord Neuberger, "Equity, ADR, Arbitration and the Law" (19 May 2010)*.

37. At the pre-action stage as well as part of their general duty to further the overriding objective.

38. *Lord Woolf, Final Report (1996)*.

39. CPR 44.2 sets out the court's powers to make costs orders and the types of orders it can make.

40. Available at https://www.judiciary.gov.uk/wp-content/uploads/JCO/Documents/CMR/cmr-final-report-dec2013.pdf [Accessed October 31, 2016].

41. *Lord Woolf, Interim Report (1995), Ch.2, para.7(a)*.

42. *Lord Justice Briggs, Chancery Modernisation Review: Final Report (December 2013)*.

43. Lord Justice Briggs, *Chancery Modernisation Review: Final Report* (December 2013), p.68, para.5.11.

44. *Interim Report* p.78, fn.10.

45. Also known as "stepped" or "escalation" clauses.

46. *Cable & Wireless Plc v IBM UK Ltd [2002] EWHC 2059 (Comm); [2002] 2 All E.R. (Comm) 1041*; followed subsequently in *Holloway v Chancery Mead Ltd [2007] EWHC 2495 (TCC); [2008] 1 All E.R. (Comm) 653*.

47. *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd [2014] EWHC 2104 (Comm); [2014] 2 Lloyd's Rep. 457*.

48. *Walford v Miles [1992] 2 A.C. 128 HL*.

49. For an in-depth analysis of the case, see Louis Flannery and Robert Merkin, "Emirates Trading, good faith, and pre-arbitral ADR clauses: a jurisdictional precondition?" (2015) 31 Arbitration International 63.

50. In arguing that mediation can provide an approximation to justice for those who cannot afford the cost and risk of litigation, Sir Gavin Lightman was critical of the *Halsey* decision on the issue that the courts cannot compel a party to mediation and the Court of Appeal's decision that the burden was on the unsuccessful party (who had invited the successful party to mediation) to show that the refusal was unreasonable. See *Lightman, "Mediation: An Approximation to Justice" (28 June 2007), S.J. Berwin*, http://www.judiciary.gov.uk/Resources/JCO/Documents/Speeches/berwins_mediation.pdf [Accessed 11 August 2015]. See also *H. Genn, Judging Civil Justice (Cambridge: Cambridge University Press, 2010), p.101*.

51. *Hurst [2002] C.P. Rep. 59* at [9].

52. *Hurst [2002] C.P. Rep. 59* at [9] (emphasis added).

53. *Hurst [2002] C.P. Rep. 59* at [10] (emphasis added).

54. *Hurst [2002] C.P. Rep. 59* at [10].

55. *Hurst [2002] C.P. Rep. 59* at [8].

56. *Halsey v Milton Keynes General [2004] EWCA Civ 576; [2004] 1 W.L.R. 3002* at [16] (emphasis added).

57. *Dunnett [2002] EWCA Civ 303; [2002] 1 W.L.R. 2434*.

58. In fact, a few months before.

59. *Dunnett [2002] EWCA Civ 303; [2002] 1 W.L.R. 2434* at [15] (Brookes LJ).

60. *PGF II v OMFS [2013] EWCA Civ 1288; [2014] 1 W.L.R. 1386*. For a discussion of various aspects of this case see M. Ahmed, "Silence in the Face of Invitations to Mediate" (2014) 73 C.L.J. 35; G. Meggitt, "PGF II SA v OMFS Co and Compulsory Mediation" (2014) 33 C.J.Q. 335; P. Taylor, "Failing to Respond to an Invitation to Mediate (2014) 80 Arbitration 470; Rix, "The Interface of Mediation and Litigation" (2014) 80 Arbitration 21; J. McQuater, "The Future of Part 36 (Part 8)" (2015) 1 J.P.I.L. 49; and E. Suter, "Unreasonable Refusal to Mediate and Costs" (2015) 81 Arbitration 2.

61. *S. Blake, J. Browne and S. Sime, The Jackson ADR Handbook (Oxford: Oxford University Press, 2013)*.

62. *PGF II v OMFS [2013] EWCA Civ 1288; [2014] 1 W.L.R. 1386* at [56] (Briggs LJ) (emphasis added).

63. See Meggitt, "PGF II SA v OMFS Co and Compulsory Mediation" (2014) 33 C.J.Q. 335 for a discussion of whether the decision in *PGF* means that mediation is compulsory in England.

64. *Rolf v De Guerin [2011] EWCA Civ 78; [2011] C.P. Rep. 24*.

65. *PGF II v OMFS [2013] EWCA Civ 1288; [2014] 1 W.L.R. 1386* at [14] (Briggs LJ).

66. *Civil Justice Reform: Final Report Chief Justice's Working Party on Civil Justice Reform (2004), section I, para.1*. On 21 November 2001, the Working Party published an Interim Report and Consultative Paper containing 80 proposals for consultation. The recommendations for reform were published in the Final Report.

67. *Civil Justice Reform: Final Report Chief Justice's Working Party on Civil Justice Reform (2004)*. The recommendations in the Final Report were broadly implemented by the HK Civil Justice (Miscellaneous Amendments) Ordinance 2008 and reflected in the Rules of the High Court (Amendment) Rules 2008 and the District Court (Amendment) Rules 2008.

68. Available at http://www.judiciary.gov.hk/en/legal_ref/prac_directn.htm [Accessed 10 October 2016].

69. *Halsey* was decided after the handover of sovereignty from the UK to the People's Republic of China in July 1997. For a comparative discussion of *Halsey*, see A. Koo, "Halsey Ten Years On" (2015) 34 C.J.Q. 77.

70. *Golden Eagle International (Group) Ltd v GR Investment Holdings Ltd [2010] 3 HKLRD 273; [2010] 5 HKC 317*.

71. *Golden Eagle v GR Investment Holdings [2010] 3 HKLRD 273; [2010] 5 HKC 317*.

72. *Chun Wo Construction & Engineering Co Ltd v China Win Engineering, HCCT 37 of 2006 (12 June 2008)*.

73. *Goodtry Investments Ltd v Easily Development Ltd, DCCJ 3346 of 2011*.

74. *Dunnett [2002] EWCA Civ 303; [2002] 1 W.L.R. 2434* at [14] (emphasis added).

75. *Dunnett [2002] EWCA Civ 303; [2002] 1 W.L.R. 2434* at [14].

76. *Société Internationale de Télécommunications Aéronautiques SC v Wyatt Co (UK) Ltd [2002] EWHC 2401 (Ch); (2003) 147 S.J.L.B. 27*.

77. *Allen v Jones [2004] EWHC 1189 (QB)*.

78. *Allen v Jones [2004] EWHC 1189 (QB)* at [33].

79. *Reed Executive Plc v Reed Business Information Ltd [2004] EWCA (Civ) 887; [2004] 1 W.L.R. 3026*.

80. *Reed Executive v Reed Business Information [2004] EWCA (Civ) 887; [2004] 1 W.L.R. 3026* at [46].

81. See "Introduction" above.

82. *R. (on the applicsation of Cowl) v Plymouth City Council [2001] EWCA Civ 1935; [2002] 1 W.L.R. 803*.

83. *Burchell v Bullard [2005] EWCA Civ 358; [2005] C.P. Rep. 36*.

84. *Burchell v Bullard [2005] EWCA Civ 358; [2005] C.P. Rep. 36* at [41] (emphasis added).

85. *ADS Aerospace Ltd v EMS Global Tracking Ltd [2012] EWHC 2904 (TCC); 145 Con. L.R. 29*.

86. *ADS Aerospace v EMS Global Tracking [2012] EWHC 2904 (TCC); 145 Con. L.R. 29* at [8].

87. *Swain Mason v Mills & Reeves (A Firm) [2012] EWCA Civ 498; [2012] S.T.C. 1760*.

88. *Leicester Circuits Ltd v Coates Brothers Plc [2003] EWCA Civ 290*.

89. *Phillip Garritt-Critchley v Ronnan [2014] EWHC 1774 (Ch); [2015] 3 Costs L.R. 453*.

90. *Northrop Grumman v BAE Systems [2014] EWHC 3148 (TCC); [2015] 3 All E.R. 782*.

91. *Northrop Grumman [2014] EWHC 3148 (TCC); [2015] 3 All E.R. 782* at [59]–[60]. (emphasis added).

92. *Northrop Grumman [2014] EWHC 3148 (TCC); [2015] 3 All E.R. 782* at [72].

93. See fn.10.

94. *Cowl v Plymouth City Council [2001] EWCA Civ 1935; [2002] 1 W.L.R. 803* at [1] (emphasis added).

95. In 2001, the Government introduced the ADR Pledge, which was a significant step forward in terms of support for ADR as it made a commitment that all government departments and their agencies would use alternative forms of dispute resolution, where appropriate and with the consent of the other party in dispute; see Ministry of Justice, "Solving disputes in the county courts: creating a simpler, quicker and more proportionate system. A consultation on reforming civil justice in England and Wales" (2011). See also the comments of the then Justice Minister and Attorney General in support of the government's "pro-active" approach to ADR: https://www.gov.uk/government/news/djanogly-more-efficient-dispute-resolution-needed.

96. See http://www.justice.gov.uk/courts/mediation/dispute-resolution-commitment.

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