THE PERILS OF IGNORING FAULTY OFFERS TO SETTLE: EXPANDED DISCRETION UNDER RULE 49

Posted on March 12, 2015

Categories: Insights, Publications

A variety of considerations go into deciding whether to accept an offer to settle a business dispute. One of the less obvious of these considerations relates to cost consequences. Under Rule 49 of the *Rules of Civil Procedure* rejecting an offer to settle in a civil proceeding may lead to significant consequences when it comes time for the court to award costs: if it turns out that the party that rejected the offer to settle would have been in the same position or better if it had accepted the offer, a higher rate of costs may be awarded to penalize that party for unnecessarily lengthening the proceeding. The purpose of Rule 49 is to encourage settlement and, whenever possible, avoid a trial.

To trigger the cost consequences under Rule 49.10, an offer to settle must meet strict requirements: (1) the plaintiff or defendant must make its offer at least seven days before the commencement of the hearing; (2) the offer must not be withdrawn or expire before the commencement of trial; (3) the offer must not have been accepted by the other side; and (4) the judgment must be as favourable or more favourable than the terms of the settlement offer. The offer must also be fixed, certain and capable of clear calculation in order to attract Rule 49 cost consequences.

Under Rule 49.10, if the plaintiff makes an offer to settle and then obtains a judgment that is as favourable as or more favourable than its own offer, the plaintiff is entitled to partial indemnity costs to the date of its offer, and then its substantial indemnity costs from that date forward, unless the court orders otherwise. If the defendant makes an offer to settle and the plaintiff obtains a judgment that is as favourable as or less favourable than the defendant's offer, the plaintiff is entitled to partial indemnity costs to the date the offer was served. The defendant is then entitled to partial indemnity costs from that date forward, unless the court orders otherwise.

Despite the strict requirements under Rule 49.10, the court does have discretion when it comes to applying cost consequences under the Rule. Courts also have discretion when it comes to applying cost consequences to settlement offers that do not conform to the strict Rule 49 requirements.

A recent Ontario Court of Appeal decision, *Elbakhiet v. Palmer*,[1] provides helpful new guidance on the extent to which the court will apply its discretion to non-compliant offers to settle under Rule 49.

Residual Discretion Under Rule 40.10(1) and (2)

The cost consequences under Rules 49.10(1) and (2) are to be applied "unless the court orders otherwise." This discretion allows the court a degree of latitude in applying Rule 49.10 cost consequences in each case. However, as discussed in McMillan's practice guide, The *Essential Guide to Settlement in Canada*,[2] the Rule 49 purpose of inducing settlement and avoiding trial can only be realized upon if the provisions on cost consequences are applied consistently to ensure a reasonable predictability in cost awards.[3] If the court's residual discretion is used too frequently, this would result in the uneven application of the rule, or its dilution to the point where there is effectively no longer a general rule.[4]

***Elbakhiet v. Palmer* and Discretion Under Rule 49.13**

Rule 49.13 gives the court the discretion to consider any offer to settle, regardless of whether the offer meets the requirements of Rule 49.10. For example, in a case where the offer to settle was served only 5 days before trial, the court relied on Rule 49.13 to exercise its discretion to award the plaintiff substantial indemnity costs from the date of their offer. This was the case despite the fact that the court expressly found that Rule 49.10 did not apply in the circumstances.[5]

The Ontario Court of Appeal recently held in *Elbakhiet v. Palmer* that a court not only can consider using discretion under Rule 49.13, but had the obligation to do so when the defendant made an offer to settle that almost met the requirements of Rule 49.10, but was a "near miss."

In awarding costs, the trial judge in *Elbakhiet* held that the defendant's second offer to settle did not exceed the judgment awarded by the jury, which is one of the requirements of a Rule 49.10 offer. The question of whether the offer to settle exceeded the judgement was not clear cut in this case, because the parties had not explicitly set out the interest rate that would apply to the offer.

The Court of Appeal upheld the trial judge's finding in this regard. However, the Court of Appeal also held that the trial judge erred by not giving proper consideration to Rule 49.13. The fact that the offer to settle was a "near miss" was not a factor in rule 49.10 considerations, but it ought to be a factor in applying Rule 49.13. The Court of Appeal explained: "given that the offer to settle was virtually the same as the Judgment, this was a case where the court had to consider the impact of rule 49.13."6 When the settlement offer complies with the "spirit" of Rule 49, even if it does not technically qualify as a Rule 49.10 offer, Rule 49.13 gives the court the discretion, and in fact the obligation, to give the settlement offer considerable weight when arriving at a costs award.[7]

Accordingly, the Court of Appeal overturned the trial judge's cost ruling, taking into account Rule 49 and Rule 57. Rule 57 asks the court to consider the amount claimed and the amount recovered in the proceeding,

among other issues. The Court of Appeal concluded that the trial judge made an error in failing to give any consideration to the offer to settle and by failing to give any consideration to what amount would be fair and reasonable.[8]

Conclusion

Rule 49.10 remains narrow in its application and courts are to depart from its requirements "only in exceptional circumstances" where the interests of justice require it.[9] However, litigants must be cautious when deciding whether to reject a Rule 49 settlement offer that may not be strictly compliant with Rule 49.10, so as to avoid unexpected cost consequences.

Simply because a settlement offer does not comply with the strict Rule 49.10 requirements does not mean that the offer will not trigger significant cost consequences. If the settlement offer nearly complies with Rule 49.10, or complies with the "spirit" of Rule 49, the Court of Appeal has made clear that courts are under an obligation to use their discretion and give weight to the settlement offer when awarding costs. Litigants who choose to ignore faulty offers to settle now do so at their own peril.

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1 *Elbakhiet v. Palmer*, 2014 ONCA 544 (Elbakhiet).

2 This practice manual is focused exclusively on the subject matter of settlement. It is a practical guide for in-house and external lawyers offering an overview of the basic principles of settlement law, guidance on how to implement a settlement, and a collection of forms and precedents.

3 *Essential Guide to Settlement*, p. 51.

4 *Essential Guide to Settlement*, p. 51.

5 *Kagal v. Tessler*, 2003 OJ No. 630.

6 *Elbakhiet*, para. 32.

7 *Elbakhiet*, para. 33.

8 *Elbakhiet*, para. 36.

9 *Elbakhiet*, para. 31.

A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against

making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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