

BRIEFING NOTE**THE INSURER'S FRIEND AND THE SHARPEST TOOL IN THE SHED:
THE OFFER TO SETTLE AKA THE CALDERBANK OFFER****Justyn Jagger****18 June 2024****Introduction**

Two of the most commonly asked questions in the claims department of any insurance company are: "How do we defend inflated claims?" and at the same time "How do we reduce legal spend on defence costs?" Claims do, of course, drive the insurance industry, because without claims there would be no need for insurance. And inflated claims, whether innocent or otherwise, are part and parcel of that industry. As indeed are aggressive plaintiff lawyers and sometimes equally aggressive panel defence lawyers, all with billable targets to achieve.

So the obvious answer would appear to be: "Vigorously defend the inflated claim placing trust in the judicial system to get the right answer whilst driving down the rates paid to the panel defence lawyers who are reliant upon repeat instructions to keep their practices solvent".

To a limited extent, that answer is correct. Yes, inflated claims have to be vigorously defended to encourage the proper presentation and support of the indemnity amount claimed. Yes, litigation, arbitration and mediation are the proper fora in which the claim must be examined. And yes, panel rates must be reviewed annually to ensure that the insurer receives best service for fair value, whilst maintaining support from a well-informed insurance defence bar.

But the better answer is: "Undertake a detailed assessment of the claim, provide the insured with a copy of that assessment, and then, if proceedings are commenced, make an Offer to Settle at an amount that encourages the insured to accept that offer rather than prosecuting the claim in court, incurring significant fees and the risk of paying the insurer's defence costs."

A Hypothetical Example

Let's take a hypothetical example. A butcher, a baker and a candlestick maker club together to buy a beautiful pea green boat. They love their boat and insure it for five million dollars. Then one day, the boat is struck by lightning. The owners are heartbroken and, brimming with all the emotion they have for their boat, bring an insurance claim for the cost of repairing the damage. Advised by their lawyer friend, Mr. Klingon, to accept not a penny less than the policy limits of five million, they elect to start an action before the Inter Galactic Council ("the IGC").

The insurer instructs a surveyor, Captain Kirk, to inspect the damage and an insurance lawyer, Mr. Spock, to review the policy. Kirk confirms that lightning has indeed struck the boat which Spock advises triggers the insurers' liability to indemnify the owners. So the issues now are the extent of the damage, the cost to replace the damaged parts and the indemnity amount.

Kirk advises that although struck by lightning, only a limited number of items on the boat were actually damaged, all of which could be replaced for two million dollars. Spock advises that the policy provides an indemnity on an actual cash value basis, in other words old for old and not new for old, such that depreciation has to apply. As the boat has a service life of twenty years and was ten years old when the lightning struck, depreciation of 50% applies. Spock advises that the indemnity amount is reduced to one million dollars. That's logical, of course.

The owners, relying on the evidence of Captain Ahab, maintain that everything attached to the boat, as well as the boat itself, was nearly new, extensively damaged and very expensive to replace. Klingon goes into warp speed and now particularises the claim at six million dollars, choosing to ignore the inconvenient wording of the policy as well as the policy limits.

Now proceedings before the IGC, that imposes a "loser pays" rule, are very expensive. Spock advises that his costs will be in the region of 500,000 dollars, the IGC's costs will run to 700,000 dollars, and that Klingon's costs could hit 800,000 dollars, all of which would have to be paid by insurers because, as the boat has been damaged, they are liable to indemnify the owners.

The insurers are baffled. The boat has sustained damage that can be repaired for two million, but the policy applies depreciation so the amount of the indemnity reduces to one million. But there's competing expert evidence suggesting that policy limits of five million may be payable. And a claim, which ignores the policy wording, has been brought for six million. And the legal costs to sort it all out could run to another two million. What on earth can they do?

The Offer to Settle / The Part 36 Offer / The Calderbank Offer

Then Spock suggests an Offer to Settle of one and a half million dollars including interest and costs. Spock explains that the Offer to Settle, also known as the Part 36 Order or the Calderbank Offer in other parts of the universe, has the potential to shift the legal and procedural costs of determining the amount of the indemnity from the defendant insurers to the plaintiff owners, incentivising the owners to settle, not fight, their claim. It works like this.

If the owners accept the offer, then the claim, interest and costs are covered and paid by the 1.5 million. This means that in paying 1.5 million, insurers have bought off the risks and costs of the claim going to trial. Even if the IGC agrees with Kirk and Spock and awards the owners 1 million in damages, interest and the costs of the IGC and Klingon could hit 1.5 million. Allowing also for Spock's costs of 0.5 million, the total cost would be 3 million. Whilst insurers have paid more than the 1-million-dollar assessment, they have saved significant costs.

If the owners do not accept the offer, the claim goes to trial and the IGC awards the owners 1.5 million (or less) in damages, interest and costs up to the date of the offer then from the date of the offer, the owners must pay Klingon's costs, Spock's costs, and the costs of the IGC. Spock's costs are deducted from the amount awarded, here reducing the amount that the insurers must pay from 1.5 million to 1 million. And from that 1 million, the owners must then pay the costs of Klingon and the IGC, another 1.5 million. So rather than receiving 1.5 million if they had accepted the offer, the owners must now pay out 0.5 million, a swing of 2 million.

If the owners do not accept the offer, the claim goes to trial and the IGC awards more than 1.5 million in damages, interest and costs up to the date of the offer then the offer does not bite and insurers must pay the damages and interest awarded, plus the costs of the IGC, Klingon and Spock. If the IGC awards damages and interest of 2 million, the insurers' total cost would be in the region of 4 million, as the costs equal the damages and interest payable.

Conclusion

The Offer to Settle, also known as the Part 36 Offer or Calderbank Offer, is a powerful tool. By raising the risk that the procedural and legal costs of both parties shift to the plaintiff if the plaintiff rejects and then fails to beat the offer, it forces the plaintiff and its counsel to examine the merits of the claim against the costs and risks of pursuing the claim to judgment.

In the above example, a plaintiff faced with a swing of 2 million, being the choice between accepting an offer of 1.5 million or rejecting that offer and paying out 0.5 million if awarded less than the offer, will often revisit the merits of the claim with the benefit of second opinions from impartial technical and legal experts. In the light of those third-party views, and perhaps a non-binding mediation, the 1.5 million, whilst below expectations, may well be accepted

If the offer is accepted, the insurer may feel that it has paid too much to settle what it considers to be an inflated claim. But it may also recognise that in buying off an inflated claim at an early stage it enjoys significant savings in defence costs and avoids the inherent risk in many insurance claims that when determining a battle of technical experts, the Court finds in the insured's favour and awards damages far in excess of the insurer's reserve.

Justyn Jagger



justyn.jagger@sjlaw.com.sg

65 6694 7281 | 65 9154 9695