**IN THE DISTRICT COURT**
**AT WELLINGTON**

**I TE KŌTI-Ā-ROHE**
**KI TE WHANGANUI-A-TARA**

**CIV-2017-085-000288**
**[2020] NZDC 18318**

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| BETWEEN | VELMA ANNE HAWKINS<br>Plaintiff |
| AND | McGANNON MOTELS LIMITED<br>First Defendant |
| AND | PATRICK GANNON and CAROLINE DENISE GANNON<br>Second Defendants |

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| Hearing: | 31 July 2020 |
| Appearances: | MRC Wolff and H Dempsey for the Plaintiff<br>R Stoop for the Defendants |
| Judgment: | 30 October 2020 |

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**RESERVED JUDGMENT (No 2) OF JUDGE C N TUOHY**

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## Introduction

[1] On 12 February 2019 I issued an interim judgment on the lessor's claim for reimbursement of legal costs incurred by her pursuant to a contractual indemnity in the lease.[1] The judgment also covered the lessee's counterclaim in respect of two matters related to the lease.

[2] That judgment clarified some of the matters of principle in dispute but, for the reasons explained in the judgment, it was not possible to quantify the amount of the costs which should be reimbursed to the lessor. At the end of the judgment, I set out

1 [2018] NZDC 23829.

various options for progressing the dispute to finality. None has succeeded. The dispute has returned to the Court for a final determination.

**Pre-proceeding costs**

[3] In the interim judgment, I drew a distinction between pre-proceeding and proceeding costs. The former describes legal costs charged to the lessor by her solicitors which relate to the lease, but which are not costs in connection with this proceeding. These are contractually payable. The latter describes legal costs incurred in connection with the proceeding in relation to which the Court has an overriding discretion.

[4] In relation to pre-proceeding costs, while the Court was able to make findings about what matters were or were not covered by the contractual indemnity, it was not possible without expert evidence to quantify the lessor's entitlement.

[5] The interim judgment made certain suggestions as to how a final resolution could be reached. The experts already instructed by the parties were not able to reach an agreement as to quantum based on the findings in the interim judgment. They were, however, able to produce a joint experts' report based on the judgment.

[6] The task of the two experts was to consider the two matters identified in para [80](c) and (d) of the Court of Appeal's judgment in *Black v ASB Bank Ltd*, that is:[2]

> (c) Whether the steps undertaken were reasonably necessary in pursuance of the tasks contemplated in the contract; and
>
> (d) Whether the rate at which steps were charged was reasonable having regard to the principles normally applicable to solicitor/client relationships.

[7] The experts' report was comprehensive. The lessor's expert, John Meads, quantified the pre-proceeding costs at $48,598.79 (inclusive of GST and

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2 [2012] NZCA 384.

disbursements). The lessee's expert, Jade Aislabie, quantified them at $38,500 (inclusive of GST and disbursements), the difference amounting to $10,098.79. The report identified how the difference arises.

[8] Both counsel came to the hearing prepared to defend the position of their expert. But it is fair to say that both readily agreed during the argument that the most pragmatic approach was to split the difference. I am in full agreement with that approach. Therefore, I fix the lessor's entitlement to pre-proceeding costs at $43,549.40.

**Proceeding costs**

*Lessor's submissions*

[9] The more difficult issue is the proceeding costs. The amount sought by the lessor is $127,533.67. The lessor submits that there is no doubt that the claim is within the ambit of the relevant indemnity clause in the lease, cl. 8(1)(c), in that it plainly relates to "an attempt to enforce against the tenant the landlord's rights under the lease", specifically the right given by cl 8(1)(c) itself.

[10] The lessor submitted that all the steps taken in the proceeding itself were reasonably necessary, particularly given the lessee's "modus operandi" which, the lessor says, was to intentionally withhold payment of sums properly due until formal enforcement procedures had been undertaken. There was a continued practice of refusing or failing to make rental and insurance payments on time. There was no doubt that the taking of proceedings was necessary, therefore, so were the costs of doing so.

[11] As to the reasonableness of rates charged, the lessor points to the agreement of both experts in their report that the hourly rates charged to the lessor by her solicitors' various "operatives" were reasonable. While they were referring to rates charged during the pre-proceeding period, there was no reason to think the later rates charged were not also reasonable.

[12] As to the counterclaims, the lessor is in tentative agreement with the preliminary view expressed in the interim judgment that costs should lie where they fall. As to a deduction from the proceeding costs to account for the fact that the work charged for includes work relating to the counterclaims, the lessor submits this should be minimal, around 5 per cent. This is because they accounted for only a minimal portion of the work undertaken on behalf of the lessors. It was also submitted that overall the lessor was more successful than the lessees on the counterclaims.

*Lessee's submissions*

[13] The lessee submitted that it was the successful party and entitled to an award of costs or, alternatively, costs should lie where they fall, or, if costs are to be awarded to the lessor, it should be on the basis of the 2B scale.

[14] As to counterclaim costs, the lessee submitted that it was successful on the maintenance fund issue. Although acknowledging the lessee was not the successful party on the insurance issue, the lessee submitted that, looking at the counterclaim overall, it was the successful party. Accordingly, the lessee seeks costs on the counterclaims on a 2B scale basis calculated at $25,307.50.

[15] The reasons why the lessee says that it was the successful party on the costs claim are:

(a) that the proceeding related to the reasonableness of the solicitor/client costs claim by the lessor, not the lessee's liability to pay such costs. Since the proceeding has resulted in the lessor's costs being fixed at a lower amount than that sought, the lessee is the successful party; and

(b) if it were otherwise, a lessee would effectively be without a remedy because a challenge to the reasonableness of costs, even if successful, would result in an award of costs against the lessee.

[16] If the Court takes the view that the lessor is the successful party, costs should lie where they fall because:

(a) settlement offers were made during the course of the litigation which were close to the amount eventually awarded for pre-proceeding costs;

(b) there should be significant reductions for the costs of the lessor on the counterclaim matters;

(c) the lessor has been only partially successful; and

(d) the costs claimed are not reasonable.

**Discussion**

*General approach*

[17] Plainly, there must be a separate approach to assessing costs in respect of the claim and the counterclaims, as they are quite separate in a legal sense. However, the legal work in respect of them was so intertwined that it is impossible to allocate the various costs invoices to one or the other. The only practicable way of separating costs is by making a broad assessment on a percentage basis of the contribution each has made to the lessor's total costs.

[18] The logical stage at which to make that apportionment is after addressing the lessee's challenge to the reasonableness of the costs as a whole because that submission applies to the lessor's costs as a whole.

[19] It is then necessary to assess which party has been successful on the claim, and on each of the two counterclaims, and then to fix the proceeding costs, taking into account, where necessary, the various arguments made by the parties.

*Reasonableness of the costs claimed*

[20] The lessor's claim for indemnity costs is made pursuant to DCR 14.6(1)(b) and 14.4(e). These rules permit the Court to award contractual indemnity costs, that is, actual costs, disbursements and witness expenses *reasonably incurred* by a party. The same requirement of reasonableness is, no doubt, also implied into cl 8(1)(c) of the

lease, the contractual provision relied upon. All other mechanisms for assessing reasonableness having been exhausted, there is no alternative to the Court undertaking that task.

[21] In doing so, I have had regard to the approach approved by the Court of Appeal in *Black v ASB Bank Ltd*.[3] Necessarily, the Court must exercise the "robust judgment as to the costs considered reasonable in all the circumstances" referred to by that court.

[22] I agree with the lessor's submission that the hourly rates charged by the various personnel working in the lessor's solicitors' firm are probably justifiable because they have been accepted by both experts in respect of the pre-proceeding costs. However, that does not mean that I accept the reasonableness of the total fee charged, which is, in large measure, the product of multiplying the hours recorded by those various personnel by their hourly rate.

[23] Ms Stoop pointed to the following factors to support her submission that the costs sought are not reasonable:

(a) That the total sought is approximately five times more than 2B scale costs (approximately $25,000). 2B scale costs are set on the basis of two-thirds of the daily rate considered reasonable.

(b) The total sought is more than three times the amount now awarded for the pre-proceeding costs, thus disproportionate.

(c) In certain respects, the invoices contain items which, on their face, seem unnecessary or excessive.

(d) Costs of $20,860 have been charged since delivery of the judgment in February 2019 which are not justified by "enforcement" steps taken since then.

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3 [2012] NZCA 384 at [77] – [81].

(e) The costs sought include attendances and correspondence in respect of a "driveway issue" in mid-2019. This related to the use of the maintenance fund and are not claimable as proceeding costs.

(f) Absent an uneconomic expert scrutiny of the proceeding costs, the Court should take note of the experts' reduction of the pre-proceeding costs by way of analogy.

[24] There appears to be some merit in some of these points but not in others. I find the comparison with 2B scale costs unhelpful. The fact is that scale costs have once more lost touch with the hourly rates charged by at least the larger commercial law firms. When considering the reasonableness of actual costs charged, the comparison must be with rates actually charged to clients for comparable work.

[25] However, I agree that proportionality must be taken into account when considering the reasonableness of costs. It is not reasonable to incur an amount of legal fees which dwarfs the sum sought or recovered. However, it must be remembered that the sum originally sought was $70,000 approximately. Although in the end only $43,549.50 has been awarded, that factor can be taken into account at a later stage of the assessment. In addition, the lessee's submission fails to acknowledge that this proceeding was originally brought, not solely to recover the lessor's legal costs, but also a substantial sum of rental arrears and interest thereon. At some point prior to the hearing, these were paid, but of course much of the costs now sought were incurred prior to the hearing. The bald comparison between the costs sought and pre-proceeding costs awarded also overlooks the fact that the costs sought include those relating to the counterclaim issues which will also be taken into account at a later stage.

[26] There are notations in the time records supporting the invoices which are hard to assess in terms of exactly what was done and whether it was necessary. In the absence of the ability to analyse them in more depth, I consider they form part of the general concern I have with the sheer amount of time expended in the course of this litigation, given the significance and monetary value of the issues.

[27] I acknowledge that it is easy for a judge, having an occasional glimpse during the process and a full view of the end product at trial, to overlook the amount of time and effort involved in litigation: the attention to detail required in discovery, the painstaking work required to brief evidence, especially expert evidence, the intricacy of legal research and preparation of submissions, and the tedious assembly of the bundle of documents. But, nevertheless, economics must play a part in the extent of time and effort and thus the costs of commercial litigation, whoever ends up paying the bills. Costs will not be reasonably incurred if they are out of all proportion to the sum which may be recoverable.

[28] Taking the unavoidable robust approach, I reduce the pre-GST costs from $110,898.84 to $90,000. This is to allow for the various specific expenditures of time (e.g. the "driveway issue") which may not be properly part of the proceeding costs, or might be unnecessary or duplicative, and the general issue of proportionality.

*Division of fees between claim and counterclaims*

[29] The only practicable way of dividing the claim costs from the counterclaim costs is by way of a percentage approach reached on a broad assessment. In making that assessment, I have perused the narrations in the invoices and the details of the time records, as well as considering the nature of the pleadings and the evidence presented at the hearing. Although these issues were dealt with fairly quickly at the hearing, they played a proportionately greater part in the leadup.

[30] My assessment is that the counterclaims accounted for about 20 per cent of the total proceeding costs, made up of 5 per cent for the insurance issue, and 15 per cent for the maintenance fund issue.

*Claim costs – successful party*

[31] There is no question that the lessor was the successful party, although that success was partial only. The claim was for about $70,000, which by the time of trial had reduced to $66,000. The lessor has been awarded $43,594.50.

[32] The lessee's claim that it was successful because it was challenging the reasonableness of the lessor's costs, not its liability for them, has no merit. The lessee did challenge its liability for some aspects of the costs (with some success) and challenged the reasonableness of all of them. It did not accept liability to pay any particular sum. If it did, it should have paid that to the lessor, or at least into court before the hearing. If it had done so, and the amount paid at least equalled the pre-proceeding costs awarded, it would have been entitled to assert that it was the successful party. But it did not.

[33] That is also the answer to the lessee's claim, that if the process for challenging the reasonableness of a lessor's costs is likely to result in a costs award against the lessee, even if it is successful, the lessee is left without a remedy. The challenge should be to only that portion of the costs which the lessee considers not reasonable. If the lessee is successful in such a challenge, it will be entitled to costs against the lessor.

[34] I do consider that a reduction should be made for the fact that the lessor's success was only partial. I discussed the basis and the authority for making such a deduction in my judgment of 12 February 2020.[4] Again, there is no mathematical formula for fixing that deduction. Applying the approach taken by Hinton J in *Herron v Wallace*[5], I fix that at 20 per cent, which compares with the approximately one-third reduction between the amount sought at trial and the amount awarded to the lessor.

[35] The lessor's claim covers only work charged for up until invoice B119346 dated 29 June 2020. That included the preparation of submissions for the hearing on 31 July. I noted the memorandum relating to interest later filed that a further invoice dated 31 July 2020 had been produced for a total of $17,901.36 presumably for work done up to that date which would include appearance at the hearing on 31 July 2020.

[36] While I consider that the lessor should be entitled to costs on that appearance and for receiving and sealing this judgment, I consider the additional amount is excessive for the additional work, considering that the submissions appear to have

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4 At [88] – [93].
5 [2018] NZHC 2638.

been already produced. I am prepared to allow $6,400 (GST exclusive) for all further work in the proceeding post 29 June 2020.

*Counterclaim costs*

[37] The counterclaims do not fall under the contractual indemnity clause. Therefore they must be dealt with on ordinary costs principles. There is no doubt that the lessor was the successful party in respect of the insurance issue. Why the lessee persisted with it is difficult to see. It is conceivable that the lessor might be entitled to increased costs on this issue, although that was not argued.

[38] The maintenance fund issue is not quite so clear cut as the interpretation formulated by the Court, and quickly accepted by the parties at trial, was not exactly that of either of the parties. However, it was effectively a rejection of the lessor's core argument that she had the power to decide which items of the lessee's maintenance the fund should be used for. In large measure, the lessee was the successful party.

[39] Ms Stoop's calculation of the counterclaim costs on a 2B scale basis treated them as a single claim. Technically they are two separate counterclaims as the difference in the successful party demonstrates. However, it is impracticable to produce two separate scale calculations. In those circumstances, the most practicable approach is to make an award to the lessee based on that calculation but reduced for the lack of success on the insurance claim and the not quite total success on the maintenance fund issue.

[40] On that basis, I award the lessee costs on the counterclaim totalling $18,000. This award will operate to reduce the final award in favour of the lessor.

*Settlement offers*

[41] Before finally quantifying the proceeding costs, it is necessary to address the submissions made by the parties reliant on various settlement offers and Calderbank letters made or sent prior to and during the course of the litigation.

[42] In view of the findings made above, it is unnecessary to address the lessor's submissions because the lessor's offers could not affect the amount of the judgment or the costs which will be awarded in this judgment.

[43] The lessee made a proposal in a letter of 20 October 2015 for the maintenance fund dispute and about legal costs which arose in part from the insurance issue to be referred to mediation or arbitration. That offer was not accepted by the lessor. In retrospect, it may have been sensible to have undertaken arbitration of what became the counterclaim issues at an earlier time because they were eminently capable of fairly quick resolution by an independent person qualified to interpret a commercial lease. However, the lessor was under no obligation to agree, so I do not think that this offer should affect costs. Even if it did so, it would be mostly relevant to the counterclaim issues in respect of which I have decided that costs will be awarded to the lessee.

[44] Another request for arbitration was made after the unsuccessful settlement conference by letter dated 14 December 2017. This was linked with threat by the lessee to abandon the lease and return to Britain. Again, in retrospect, that proposal, if accepted, may have saved some legal costs, but by that stage not necessarily. In any event, the lessor was not bound to accept that form for resolution of the dispute and the lessee has been awarded costs on the counterclaim anyway.

[45] The other point about these offers is that they were complicated by the fact that the lessee was continuously in default of its core and indisputable obligations to pay rent and reimburse insurance premiums on time, which were part of the lessor's claim.

[46] Formal Calderbank letters were sent to the lessor on 6 March 2018 and 12 November 2018. The first was after the settlement conference. It was for $30,000 for both pre-proceeding and proceeding costs to that time. That offer did not even meet the amount now fixed for pre-proceeding costs.

[47] The other was sent shortly before the trial. It was an offer to accept the amount of "claimable enforcement costs" of $40,000 payable out of the maintenance fund. My understanding of that offer is that claimable enforcement costs were intended to encompass not only the pre-proceeding costs but the proceeding costs to date. It is

again obvious that the sum offered was well short of the total of pre-proceeding costs and the proceeding costs which would have been awarded to that date. Had the offer excluded proceeding costs, it may well have affected the quantum of those because it was close to the amount now fixed for pre-proceeding costs. But that not being the case, I do not see that it can have any effect on quantum now.

*Quantification of proceeding costs*

[48] On the basis of the above findings, the amount awarded to the lessor for costs in this proceeding (on a GST exclusive basis) is:

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| Reasonable costs incurred | 90,000 |
| Less deduction for counterclaim work (20 per cent) | 18,000 |
| | 72,000 |
| Less deduction for partial success (20 per cent) | 14,400 |
| | 57,600 |
| Plus allowance for reasonable costs incurred post 29 July 2020 | 6,400 |
| | 64,000 |
| Plus GST | 9,600 |
| | 73,600 |
| Less counterclaim costs (including GST) | 18,000 |
| | $55,600 |

*Interest on proceeding costs*

[49] On 28 August 2020, nearly a month after the hearing on 31 July 2020, the lessor's solicitors filed a memorandum providing information as to the rate of interest payable under cl 7 of the lease which provides for interest to be paid by the lessee on payments due under the lease which remain unpaid for 14 days after due date. That

rate is said to be 24 per cent per annum. The memorandum also attached calculations of interest for each of the invoices which made up the total of $127,533.67 claimed by the lessor at the hearing for proceeding costs. The interest totalled $57,568.12. It included interest on the large invoice for nearly $18,000 dated 31 July 2020, the day of the hearing. This was not included in the total of $127,533.67 claimed at the hearing, which itself included costs of about $27,000 since the first hearing.

[50] This memorandum was not requested by the Court. The lessor had not sought interest on the invoices making up the claim for proceeding costs at the hearing. The memorandum was apparently prompted by some discussion at the hearing of the potential for an interest claim.

[51] The lessee's solicitors have filed a memorandum in response dated 16 September 2020, strongly opposing the claim for interest on the proceeding costs implicit in the lessor's memorandum. The opposition is based on both procedural and substantive issues.

[52] It is unnecessary to address the grounds of opposition in detail. I agree that it is not open to the lessor to add this claim at her own initiative after the second (and final) hearing had been completed and decision reserved.

[53] Even if it had been advanced with proper warning at the hearing, I would not have allowed it. The proceeding costs are at the discretion of the Court albeit underpinned by the contractual indemnity. The costs not having been fixed until the date of this judgment, they are not payable by the lessee until they are. In any event, the proceeding costs have not been fixed by direct reference to any particular invoice as the above discussion shows. Finally, I would not grant interest on the costs award in my discretion because of the proportionality issue and certainly not at the extortionate rate calculated.

**Disbursements**

[54] The lessor has sought to recover as disbursements the cost of employing John Meads, the costs expert instructed by her solicitors. Three invoices have been

presented for the periods ending 30 September 2018, 20 December 2018 and 29 February 2020 for $8,251.25, $8,162.85 and $2,062.21 respectively, totalling $18,476.31.

[55] For a combination of reasons, I am not prepared to allow these amounts. First, Mr Meads never became a witness in the proceeding and never gave any evidence. Nor did the lessee's counterpart expert, Jade Aislabie.

[56] Mr Meads' only input to the proceeding was his contribution to the joint experts' report which helped the parties and the Court to reach a pragmatic resolution of the quantum of the pre-proceeding costs. That report, in my understanding, was placed before the Court by both parties. Mr Aislabie, whose expenses must be met by the lessee, contributed equally to that report. It is fair for that reason that the parties meet their own expert's fees.

[57] This claim, if allowed, would also make the total costs award in favour of the lessor grossly disproportionate to both the amount sought and more so, to the amount recovered.

**Result**

[58] There will be judgment for the lessor in the sum of $43,549.40 for pre-proceeding costs. Costs of the proceeding are awarded to the lessor in the sum of $55,600.

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Judge CN Tuohy
District Court Judge

Date of authentication: 30/10/2020
In an electronic form, authenticated electronically.