Jones v Society of Lloyds; Standen v Society of Lloyds
CHANCERY DIVISION
The Times 2 February 2000, (Transcript)
HEARING-DATES: 16 DECEMBER 1999
16 DECEMBER 1999

COUNSEL:
D Oliver QC and R Morgan for the Applicant Jones; C Mackenzie Smith for the Applicant Standen; E Bannister QC and L Hilliard for the Respondent

PANEL: RATTEE J
JUDGMENTBY-1: RATTEE J
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RATTEE J: These two sets of proceedings arise out of the complex scheme by which the Society of Lloyd's sought to settle the mass of litigation between underwriting members ('Names') and agents which arose from the large scale losses suffered by Names for the years up to 1992. As it is described in the judgment of the Court of Appeal in Society of Lloyd's v Leighs [1997] CLC 1,398, The Times 11 August 1997, at 1,399 of the former report it was a scheme which involved:

a voluntary global settlement of claims of various descriptions made by and against names in respect of business written in or before 1992 coupled with a reinsurance and run-off contract, in the nature of a global reinsurance to close, with a group of companies ('Equitas') formed specifically for this purpose."

As part of the scheme provision was made for a fund contributed to by various parties to be applied in part satisfaction, and therefore reduction, of Names' liabilities in respect of insurance losses underwritten by them, provided their net liability after such reduction was paid by a specified date, 30 September 1996. If such payment was not made by that date, then the scheme provided (or at least purported to provide) that the Name concerned would not enjoy the benefit of reduction of his full liability. It is one of the contentions of the two Names concerned in these proceedings, that is to say a Mr Jones and a Mr Standen, that this latter provision is in the nature of a penalty, and therefore unenforceable by Lloyd's.

The scheme was embodied in a long and complex Settlement Offer Document which was sent to all relevant Names, and which included in its Appendix 1 a form of written agreement ('the Settlement Agreement') to which Names who accepted the scheme became parties. The Settlement Agreement was made between Lloyd's and, among other parties not relevant for present purposes, those Names who accepted the proposed scheme, Equitas, E & O insurers and underwriting agents. The agreement recited, amongst other things, that:

(a) the purpose of the agreement was to achieve the objective of reconstructing the Lloyd's market:

with the aim of resolving the problems of the past and building a strong market for the future;"

(b) all Names' '1992 and Prior Business' was to be conditionally reinsured into Equitas;

(c) Lloyd's had made an offer to Names to settle certain claims in respect of their '1992 and Prior Business';

(d) a Settlement Fund of approximately £3.2 billion was to be distributed, in part through 'Combined Litigation Settlement Funds' and 'Debt Credits', in accordance with the terms set out in the Settlement Offer Document and the Settlement Agreement itself; and

(e) A 'Finality Statement' had been sent to each Name setting out (inter alia):

each Name's allocation from the Combined Litigation Settlement Funds . . . and Debt Credits."

Schedule 1 to the Settlement Agreement contains numerous definitions used for the purpose of the Settlement Agreement. Included in these are the following:

‘1992 and Prior Business’ means all liabilities under contracts of insurance or reinsurance underwritten at Lloyd’s and originally allocated to the 1992 year of account or any earlier year of account, with certain exceptions not material for present purposes;

‘Finality Statement’ means ‘the statement of a Name’s Lloyd’s affairs in respect of his 1992 and Prior Business sent to him with the Settlement Offer Document or otherwise’, together with certain supporting data;

‘Combined Litigation Settlement Funds’ means ‘the sum of the Litigation Settlement Fund and the Auditor Settlement Fund’;”

‘Litigation Settlement Fund’ means a fund of approximately £980 million offered to names in accordance with the terms of the Settlement Offer Document;

‘Auditor Settlement Fund’ means another fund of approximately £156 million offered to names in accordance with the terms of the Settlement Offer Document; and

‘Debt Credits’ means ‘in respect of each Name, any amount offered to that Name as so described and set out in his Finality Statement . . . , to be applied in the reduction of the amount to be paid by that Name pursuant to his . . . Finality Statement (which may include the waiver of certain amounts owing to Lloyd’s arising out of the application of assets of the Central Fund on his behalf)’.”

I should quote some of the other provisions of the Settlement Agreement which are relevant to the submissions made in this case:

Clause 3.1:

Lloyd’s agrees to apply the benefits of the Combined Litigation Settlement Funds and Debt Credits, or procure that such benefits are applied, in accordance with the terms of the Settlement Offer Document and hereof and that accordingly each Accepting Name will be entitled, in accordance with such terms:

(a) to have applied for his benefit such amounts, if any, as are set out in his Finality Statement from the Combined Litigation Settlement Funds . . . and/or the Debt Credits, provided he has paid, or otherwise satisfied his obligation to pay, all amounts due from him in respect of his Finality Statement; and

(b) . . .

The remainder of Clause 3 includes waivers of claims that Lloyd’s might otherwise have against the Accepting Name, provided the name pays or otherwise satisfies ‘all amounts due from him in respect of his Finality Statement’.”

Clause 4.1:

Without prejudice to his obligations under the Reinsurance Contract, each Accepting Name agrees with Lloyd’s to pay, or otherwise satisfy his obligation to pay, all amounts due in respect of his Finality Statement in accordance with the terms set out in the Settlement Offer Document and hereof, free and clear of any set off, counterclaim or other deduction on any account whatsoever including, without limitation, in respect of any claim against Lloyd’s, Equitas or any other person and further agrees to the waiver of any stay of execution and to the immediate enforcement of any judgment in respect of his obligations to pay all or any such amounts due in respect of his Finality Statement.”

Clause 4.3:

. . . each Accepting Name hereby accepts in full and final settlement of all of [there follows a reference to all sorts of claims the name might otherwise have against parties to the Settlement Agreement in respect of his 1992 and Prior Business] the benefit of the amount, if any, as set out in his Finality Statement to be applied to his benefit from the

Combined Litigation Settlement Funds and/or Debt Credits . . . and the mutual covenants and agreements and other good and valuable consideration given by the other Parties to this Settlement Agreement under or as a consequence of this Settlement Agreement."

Clause 12.12:

Any liability of any of the Parties to any other Party hereunder may in whole or in part be released, compounded or compromised by that other Party, or time or indulgence may be given by that other Party in its absolute discretion, without in any way prejudicing or affecting any other rights of the Parties against that other Party or any other Party, provided that any release, compounding, compromise or other indulgence must be in writing and be expressly stated to be a release, compounding, compromise or indulgence for the purposes of this clause. Any delay by any Party in exercising, or failure to exercise, any right or remedy under this Settlement Agreement shall not constitute a waiver of the right or remedy. No single or partial exercise of any rights or remedy under this Settlement Agreement shall prevent any further exercise of the right or remedy, or the exercise of any other right or remedy."

Since the Settlement Agreement refers to and, in effect, incorporates the terms of the Settlement Offer Document, it is necessary also to quote certain of the provisions of that. Appendix 2 includes the following provisions:

Paragraph 9:

Irrespective of any references to allocations of debt credits or any part of the combined litigation settlement funds, no Name or other person will have an interest of any type in any part of the settlement fund or any right to receive any monies from it. Where in the Settlement Agreement . . . Lloyd's has agreed to apply the benefit of allocations of debt credits, or any part of the combined litigation settlement funds . . . , or to procure that such benefits are applied, Lloyd's will (subject to the other terms and conditions set out in this document [or] . . . the Settlement Agreement) procure that the Equitas premium of the accepting Name . . . and any other liabilities covered by his finality statement will be reduced by the amount of any such allocations shown on his finality statement. The allocations of benefits from the settlement fund may be used only for the reduction of such liabilities and for no other purpose . . ."

Paragraph 31 defined the 'Finality Payment Deadline' as:

12 noon (London time) on 30 September 1996 or such later time and date as Lloyd's may allow."

Paragraph 32:

Without prejudice to the provisions of paragraph 39, an accepting Name will be entitled to receive the benefits set out in Clauses 3.1(a) and 3.3 of the Settlement Agreement if he has paid, in accordance with paragraphs 42 to 48, by the Finality Payment Deadline, not less than his Finality Amount."

A name's Finality Amount was defined by reference to an extremely complicated formula which is not relevant for present purposes. The essential feature of the Finality Amount was that it is the figure for the liability of the Name reached after deducting his allocation of benefits under Clause 3.1 of the Settlement Agreement.

Paragraph 38:

If an accepting Name fails to pay, in accordance with paragraphs 42 to 48, his Finality Amount by the Finality Payment Deadline, he will:

(a) be in default; and

(b) . . .

(c) not be entitled to have applied for his benefit the amounts, if any, as set out in his finality statement from the combined litigation settlement funds and/or debt credits save to the extent that he has any entitlement pursuant to the terms of any Action Group Settlement Agreement."

Paragraph 42:

A Name will only be treated, for the purpose of the Settlement Agreement and these terms and conditions, as having paid:

(a) if the Name has delivered cash or cash equivalent, in accordance with the terms of paragraph 43; or

(b) for the purpose of payment of his Finality Amount only, to the extent of:

(i) . . .

(ii) the value of the deferred payment amount (before interest) given in any letter from a financial institution acceptable to Equitas offering the Name a guarantee for a Structured Payment Plan received at [a specified department of Lloyd's] by Lloyd's by the Finality Payment Deadline;

(iii) . . .

(iv) . . .

I shall refer a little later to the meaning of a 'Structured Payment Plan'."

Paragraph 43 specified various forms of payment of cash equivalent, for example cheques, which would be acceptable as payment for the purpose of paragraph 42(a).

Those, I think, are the relevant provisions of the Settlement Agreement and the Settlement Offer Document. I must next set out the relevant facts concerning Mr Jones, on the one hand, and Mr Standen, on the other.

Mr Jones

He was a Lloyd's Name from 1987 to 1991, during which years the syndicates of which he was a member made consistent losses. He received a copy of the Settlement Offer Document in July 1996 and a Finality Statement in August 1996. That Statement showed his total underwriting liabilities as £288,711. That figure was, as appears from the Statement, made up of the following elements:

(i) Losses declared up to 31 December 1994, but not called by 15 March 1996 (£44,099);

(ii) Losses which had actually been called but not paid by 15 March 1996 (£59,508);

(iii) Interest and other charges (£7,720);

(iv) Amounts that had been paid towards Mr Jones' losses on his behalf from the Lloyd's Central Fund (£85,531);

(v) Members' agent's expenses (£1,216); and

(vi) An additional premium due in respect of the reinsurance of Mr Jones' losses into Equitas (£90,637).

The Finality Statement showed debt credits in the sum of £188,468 to be deducted from the gross underwriting liabilities, pursuant to the Settlement Agreement, leaving a net figure (after other minor, irrelevant adjustments) said to be:

Amount due from you after the above adjustments before taking into account funds at Lloyd's"

of £99,999.

Mr Jones signed a form of acceptance of the Settlement Offer Document on 22 August 1996, thereby becoming an Accepting Name. On the advice of his accountants, Messrs. Morgan Brown & Spofforth, on whom at that time he

relied to handle his affairs at Lloyd's, Mr Jones decided to take advantage of the availability under the Settlement Agreement of the option to satisfy part of his liability by a Structured Payment Plan. In his form of acceptance he said he would settle his £99,999 by paying £15,000 in cash, with the balance of £84,999 being covered by a Structured Payment Plan. Mr Jones says he then left it to his accountants to see that the financing arrangements were put in place by the deadline of 30 September 1996.

The concept of a Structured Payment Plan was explained in the Settlement Offer Document in these terms:

An accepting Name may wish to pay part of his Equitas premium (calculated as described below) in up to five annual instalments starting in 1997. To pay in this way, a Name must have gained approval from a bank to issue a guarantee before 30 September 1996. The guarantee must be in favour of Equitas and to the value of the deferred payment plus interest at 8 per cent and an additional 'cushion' equivalent to six months' simple default interest also at 8 per cent on the deferred amounts. The bank providing the guarantee must be acceptable to Equitas and have a branch in London."

The Settlement Offer Document went on to explain that the amount that could be deferred and made subject to a Structured Payment Plan was the net liability shown on the Finality Statement less certain items including the amount shown on the Finality Statement as 'members' agent's expenses'. The £15,000 which Mr Jones elected to pay in cash was sufficient to cover these items.

On 25 September 1996 Lloyd's wrote to Mr Jones a letter which I should quote:

Thank you for returning your payment form to Lloyd's on which you indicated you will be using the Structured Payment Plan as a method of payment. Your application is currently under consideration and you will be advised of the progress of your individual application shortly.

We shall also be sending you the final documentation to be completed by you and your bank in the near future. You should return this documentation as soon as possible, but it is not necessary for it to be returned prior to 30 September 1996 in order to maintain your settlement benefits. It will be sufficient for us to have received a letter from an approved bank stating that they are willing to provide a guarantee in the name of Equitas, as set out in the Settlement Offer.

If you have any questions please do not hesitate to contact me."

The terms of this letter were consistent with the provisions of paragraph 42 (b)(ii) of Appendix 2 to the Settlement Offer Document, which required that if a Name was proposing a Structured Payment Plan, what had to be received by Lloyd's by the Finality Payment Deadline on 30 September 1996 was, not a completed guarantee, but a letter offering such a guarantee from an acceptable financial institution. It is Mr Jones' evidence that he did not receive the final documentation referred to in the letter I have just quoted, and there is in fact no evidence that he did.

However, whether Mr Jones' received any draft guarantee or not is beside the point, because what he had to do by 30 September 1996 to take the advantage of the Debt Credits shown on his Finality Statement was (a) to pay to Lloyd's the £15,000 which he had opted to pay in cash and (b) provide to Lloyd's a letter offering a guarantee from an acceptable financial institution. It is common ground that he did neither.

On 18 October 1996 Lloyd's financial recovery department sent a standard form letter to Mr Jones which included the following:

According to our records, you have accepted the Lloyd's settlement offer but to date you appear not to have paid the full amount due under the settlement agreement. Payment was due on 30 September 1996 and this deadline has not been extended. I must advise that you are in default of your obligations under the settlement agreement.

. . .

Although you have failed to pay the amount due from you under the terms of the settlement, the settlement agreement remains fully effective. You are bound by all the waivers and releases that you gave in the document in

respect of your litigation and other rights. However, by virtue of non payment, you are no longer entitled to the following benefits:

credits from the combined litigation settlement fund;

debt credits; and

any refund of your contributions to members' Special Central Fund contribution.

You are now liable, therefore, to pay the amount shown on your finality statement without the benefit of such credits (the increased amount) together with interest on the outstanding amount from the 30 September 1996 at 2 per cent above the National Westminster Bank base rate. You are exposed to legal proceedings to recover the increased amount that you owe in full and it will not be a defence to any such claim that you intended to pay but have been prevented from doing so by some reason or that you were expecting others to make arrangements on your behalf."

On the same day, 18 October 1996, the Manager of Lloyd's Members Agency Services Limited wrote a letter to Mr Jones also stating that it appeared that Mr Jones had lost the benefit of (inter alia) the debt credits because he had not paid by 30 September. However, this letter went on:

. . . I do not believe that you intended this result by virtue of your acceptance and non payment. I can only assume that you have failed to understand the time critical nature of the payment date and the potential losses and detriment you will suffer by virtue of your non payment.

Lloyd's financial recovery department will be writing to you today requesting payment of the increased amount by the 31st October. You must appreciate that you are now liable for this increased amount. I would point out however that Lloyd's retains a discretion to allow late acceptances and late payment in individual circumstances. The Council of Lloyd's will be considering how to proceed against members who have accepted but failed to pay on time in the light of their obligations to other members as well as the interest of Equitas in relation to the recovery of outstanding amounts for the benefit of policyholders.

Obviously I am not in a position to commit Lloyd's or Equitas to acceptance of late payment of the full amount due under the settlement (ie your net finality bill). I believe, however, that it will be possible to make representations on your behalf to seek the exercise of Council's discretion in your favour, if payment in full of the net finality bill due from you under the terms of the Settlement Offer is made to Lloyd's by 31st October 1996.

If for any reason you are unable to make payment of your net finality, please contact me with details in order that I may discuss the position with the financial recovery department on your behalf to ensure that whatever benefits can be retained are secured in your interest.

I urge you to act upon this letter and contact my office as soon as possible."

Mr Jones then contacted National Westminster Bank, and apparently there was a telephone conversation between someone at the Bank and someone at Lloyd's, for on 23 October 1996 Lloyd's sent a fax to the Bank referring to such a telephone conversation and asking the Bank to let Lloyd's have its letter of intent, and on 28 October the Bank wrote to Lloyd's a letter saying:

I write to confirm that the Bank is willing to enter into the Lloyds Bank Guarantee for £100,000 as discussed. Please arrange to forward me the Guarantee in order that I can forward this on to our Securities Department for their attention."

On 4 November 1996 Lloyd's wrote a rather surprising letter to Mr Jones' accountants which included the following:

I confirm that your client has been in contact with our Membership Department to arrange payment by instalments. I further confirm that our letter of 18 October [ie the demand for payment of the gross amount shown in the Finality Statement] does not apply to your client assuming that the bank guarantee is provided as requested."

One odd feature of this letter is that it appears to ignore the fact that, quite apart from any question of providing a guarantee for the amount which he had elected to make subject to a Structured Payment Plan with interest, Mr Jones had completely failed to make the cash payment of the £15,000 he was, in accordance with his form of acceptance, to pay in cash, either by the original deadline of 30 September 1996, or even by the possibly extended deadline of 31 October offered by the letter of 18 October from Lloyd's Members Agency Services Ltd. The letter from Lloyd's of 4 November totally ignores that default.

Consistently with that letter, on 24 January 1997 Lloyd's issued to Mr Jones' accountants a Taxation Advice statement which appeared to be drawn on the basis that Mr Jones was liable only for the net finality amount.

However, still Mr Jones provided neither his £15,000 cash payment nor a completed bank guarantee for the Structured Payment Plan. According to Lloyd's, on 21 March 1997 they wrote to Mr Jones offering him a further opportunity to pay the £15,000 cash sum by 1 April 1997, and telling him that if he did not, his Structured Payment Plan for the balance of his finality amount would be cancelled, and he would be liable for the gross sum shown on his Finality Statement. A copy of a letter in these terms is in evidence, but it is Mr Jones' evidence that he did not receive it. He did not pay the £15,000, and on 27 June 1997 the Financial Recovery Department of Lloyd's wrote demanding payment of the gross sum shown on the Finality Statement plus interest, the demand being for £302,963 odd. On several occasions after this last letter Mr Jones tendered a cheque for the net amount shown on the Finality Statement with interest, but such tenders were refused by Lloyd's.

On 23 November 1998 Lloyd's served on Mr Jones a statutory demand for £342,240.88. By the application before me Mr Jones seeks to have that statutory demand set aside. After the statutory demand had been served Lloyd's accepted from Mr Jones a cheque for £123,044.52 - the net finality amount plus interest - 'as part payment'.

Mr Standen

Mr Standen was an underwriting member of Lloyd's from 1979 to 1992. He also suffered substantial losses. He was sent a copy of the Settlement Offer Document and a Finality Statement in July 1996. That showed his total underwriting liabilities as being £180,636, made up as follows:

(i) Losses declared to 31 December 1994 but not called by 15 March 1996 (£62,417);

(ii) Losses called but unpaid as at 15 March 1996 (£66,754);

(iii) Interest and other charges (£7,506);

(iv) Amounts paid towards losses by Lloyd's on behalf of Mr Standen out of the Lloyd's Central Fund (£18,682);

(v) Members' agent's expenses (£2,028);

(vi) Personal expenses (£36); and

(vii) Equitas additional premium (£23,213).

The Finality Statement then showed certain credits against that gross amount, including in particular a figure in respect of Debt Credits of £66,512. The net amount shown as:

Amount due from you after the above adjustments before taking into account funds at Lloyd's"

was £99,914.

Mr Standen accepted the Settlement Offer Document on 22 August 1996. He did not elect to make any part of the amount due from him subject to a Structured Payment Plan. He intended to pay the full amount in cash by the deadline of 30 September 1996, but found himself unable to do so. Lloyd's wrote to him on 18 October 1996 a letter in form similar to that sent on the same date to Mr Jones, demanding payment of the net amount shown on the Finality Statement plus the amount allowed in respect of Debt Credits. The Finality Statement also made an

allowance of £17,080 in respect of Mr Standen's entitlement in respect of a particular litigation settlement fund which was unaffected by his failure to pay by the Finality Deadline.

Mr Standen failed to pay, and eventually, on 2 September 1998, Lloyd's served a statutory demand on him in the sum of £187,228.51, being (according to Lloyd's) the amount due on the Finality Statement after adding back the figure shown for Debt Credits, with interest. On 2 September 1998 Mr Standen applied to the court to set the statutory demand aside. The application was dismissed on 3 December 1998. Lloyd's presented a bankruptcy petition on 15 December 1998. The petition was adjourned on several occasions on Mr Standen's application to give him an opportunity to provide security for the petition debt, which he has failed to do.

On 14 September 1999 Mr Standen for the first time gave notice of intention to oppose the bankruptcy petition on the ground that the difference between the net amount shown on the Finality Statement and the amount claimed by Lloyd's represents an unenforceable penalty. The bankruptcy petition is now before this court to be determined by me. I suggested at an early stage of the hearing that, since Mr Standen had already made an unsuccessful attempt to set aside the statutory demand on which the petition is based, he ought not now to be allowed to go behind that demand by arguing that the debt thereby demanded was never due (see Brillouet v Hachette Magazines Ltd [1996] BPIR 518). However I was persuaded that it was appropriate, since the question whether the provisions of paragraph 38 of Appendix 2 to the Settlement Offer Document constituted an unenforceable penalty was being argued on Mr Jones' behalf, to hear argument also by counsel for Mr Standen.

The Penalty Argument

Both Mr Jones and Mr Standen contend that the effect of the Settlement Agreement is to impose on a Name an obligation to pay the net amount shown on the Finality Statement by 30 September 1996, and that the effect of paragraph 38 of Appendix 2 to the Settlement Offer Document as incorporated in the Settlement Agreement (if enforced) is to penalise a Name for failing to meet that obligation by imposing an obligation to pay a much greater sum - the gross amount shown on the Finality Statement - which bears no relationship to any loss suffered by Lloyd's as a result of the Name's failure to pay the lesser sum by 30 September 1996. Paragraph 38 therefore purports to impose a penalty of the nature which the law will not enforce.

Counsel for Mr Jones and Mr Standen relied on the definition of an unenforceable penalty to be found in the judgment of Nicholls LJ (as he then was) in Jobson v Johnson [1989] 1 All ER 621, [1989] 1 WLR 1026 at 1038E of the latter report:

In considering this appeal it is right to have in mind that the legal principles applicable today regarding penalty clauses in contracts and those applicable regarding relief from forfeiture stem from a common origin. A penalty clause in a contract, as that expression is normally used today, is a provision which, on breach of the contract, requires the party in default to make a payment to the innocent party of a sum of money which, however it may be labelled, is not a genuine pre-estimate of the damage likely to be sustained by the innocent party, but is a payment stipulated in terrorem of the party in default. For centuries equity has given relief against such provisions by not permitting the innocent party to recover under the penal provision more than his actual loss."

Messrs Jones and Standen submit, as is clearly right, that the difference between the net sums stated in their Finality Statements and the amounts which they are required to pay because of their failure to pay those net sums on time do not bear any relationship to loss suffered by Lloyd's as a result of that failure. The requirement to pay the larger sums is therefore a penalty which the court will enforce only to the extent of any loss suffered by Lloyd's.

Lloyd's, on the other hand, argue that the true nature of the Settlement Agreement as a whole is that each Accepting Name was offered an option to pay his true liabilities reduced by Debt Credits by 30 September 1996, or to pay his full underwriting liabilities without such reduction at a later date. Viewed in this light paragraph 38 is no more a penalty than is any contractual provision of the option of taking a discount for prompt payment.

According to Lloyd's' submission the Settlement Agreement does not impose any obligation on a Name to make any payment by 30 September 1996, so that there is no question of the obligation to pay the gross amount of underwriting liabilities at a later date being a penalty for failure to satisfy an obligation to pay the net amount by 30 September 1996. The only materiality of that date is that the effect of paragraphs 32 and 38 of Appendix 2 to the

Settlement Offer Document is to make the amount payable by the Name depend on whether payment is made before or after 30 September 1996.

Counsel for Messrs Jones and Standen pointed out with some force that this last submission is scarcely consistent with the terms of paragraph 38 itself, which provides that if the Name fails to pay by the 30 September 1996 deadline he will 'be in default'. Counsel submitted that the fact that this was Lloyd's' own understanding of the effect of the Settlement Agreement is confirmed by the terms of the letters sent out by its Financial Enforcement Department on 18 October 1996 to those Names who had not paid by 30 September, which said:

Payment was due on 30 September 1996 . . . I must advise that you are in default of your obligations under the settlement agreement."

It is unnecessary to resolve this argument, because I accept an alternative submission by counsel for Lloyd's to the effect that it does not really matter for present purposes whether the effect of the Settlement Agreement as a whole was, or was not, to impose a contractual obligation to pay the lesser sum by 30 September 1996. In my judgment what is essential to the enquiry whether a provision is of the nature of a penalty is the nature and origin of the secondary obligation sought to be imposed in the event of the breach of the primary obligation. Support for this conclusion is to be found in one of the authorities relied on by counsel for Lloyd's, namely Thompson v Hudson (1869) 4 HL 1. In that case R was indebted to A in respect of three different sums of money, all of which debts were the subject of suits in Chancery. There had already been a final decree in those suits in respect one of the debts, but not of the other two. R and A agreed that R should admit the amount of the debts in respect of which there had as yet been no final decree, that he should give security for the debts, and pay specified amounts by certain specified dates. On those conditions A would accept smaller sums in satisfaction of the original debts. The agreement provided that A was to be entitled to enforce full payment of the original debts if R failed to comply with any of the terms of the new agreement. The Master of the Rolls held that this provision was a penalty. His decision had been affirmed on appeal apparently on different grounds. A successfully appealed to the House of Lords. At p 27 of the report Lord Westbury said this:

I am sure your Lordships will agree with me that the Appellants have been very unfortunate in this litigation. In answer to the questions which they were required to answer in the Chamber of the Master of the Rolls, they thought that it was very rational and very right for a creditor to say to his debtor, 'Provided you pay me half of the debt or two-thirds of the debt on an appointed day I will release you from the rest, and will accept the money so paid in discharge of the whole debt; but if you do not make payment of it on that day, then the whole debt shall remain due to me, and I shall be at liberty to recover it'. If you were to put that proposition to any plain man walking the streets of London, there could be no doubt at all that he would say that it is reasonable and accordant with common sense. But if he was told that it would be requisite to go to three tribunals before you could get that plain principle and conclusion of common sense accepted as law, he would undoubtedly hold up his hands with astonishment at the state of the law.

The Master of the Rolls appears to have thought that the residue of the debt in the case I have put would be converted into a penalty, and that the penalty could not be enforced. It is impossible to hold that money due by contract can be converted into a penalty. A penalty is a punishment, an infliction, for not doing, or for doing something; but if a man submits to receive, at a future time and on the default of his debtor, that which he is now entitled to receive, it is impossible to understand how that can be regarded as a penalty. I have not therefore the least hesitation in stating that (if the Master of the Rolls is rightly reported), it could not have been present to him at the moment when he delivered his judgment, that the rest of the debt still remained due by contract, and that what was due by contract could not be a penalty."

At page 33 of the report Lord Colonsay said:

I think we are brought to look at the original position of the parties; and the question comes to be, whether when a stipulation is made by a creditor that he will accept a sum smaller than the amount of the debt, and certain securities for that smaller sum, provided the payment is made within a definite time, but that if the payment is not made within that definite time the right which he possesses, and which is treated throughout the deed of October as a present existing right, shall be open to be enforced by him, that is to be regarded as a penalty. I cannot understand that it is to be regarded as a penalty? It is a reservation of an existing right. It is not the emergence of a right that never had any

existence at all except on the violation of the agreement which was made. It is merely the reservation of what is the just and honest right of the party, which he was willing to waive to a certain extent, provided his debtor would do certain things, but if the debtor fails in doing those things, then that right which belongs to the creditor shall continue to belong to him, and he may enforce it. That being the view I take of the case, I am under the necessity of coming to the conclusion that the judgments appealed against ought to be reversed."

As I understand their Lordships' reasoning in that case it was to the effect that the sum to be paid in the event of failure to comply with the new agreement for security etc could not be regarded as a penalty, because it was a sum contractually due to the Appellants before the new agreement was entered into, an obligation to pay which was expressly preserved by the new agreement to take effect in the event of the breach of the latter. As Lord Colonsay pointed out, it was the reservation of an existing right, not the creation of a right that never had any existence at all except on breach of the new agreement.

In my judgment similar reasoning applied to the Settlement Agreement leads to the conclusion that the provisions of paragraph 38 of Appendix 2 to the Settlement Offer Document do not give rise to a penalty. They preserve the Name's original underwriting liabilities without deduction of, in particular, Debt Credits in the event of the Name failing to comply with the new settlement provisions for payment of a lesser sum by a specified date. True it is that before the coming into force of the Settlement Agreement all the elements of the Name's gross underwriting liabilities set out at the beginning of the Finality Statement were not owed to Lloyd's. Some (for instance recoupment of the Central Fund) were. Some were liabilities to others, including managing agents, which became enforceable by Lloyd's as part of the settlement scheme. The liability for a premium in respect of reinsurance by Equitas arose, as I understand it, under a separate agreement with Equitas which took effect before the Settlement Agreement became unconditional. But they were all existing liabilities of the Name before the Settlement Agreement took effect, as opposed to a liability that came into being only as a penalty for subsequent failure to pay a reduced sum by the specified date. It would indeed be a surprising result if those pre-existing liabilities were extinguished by the equitable doctrine of relief against penalties. In my judgment the provisions of paragraph 38 do not constitute a penalty. Their true effect is that the benefit of the reduction of pre-existing liabilities offered on certain conditions by the Settlement Agreement is lost if those conditions are not fulfilled. There is nothing objectionable in equity about such a provision.

The Forfeiture Argument

An alternative argument relied on on behalf of Mr Jones and Mr Standen was that the provisions of paragraph 38 constitute a provision for forfeiture, against which the court has an equitable jurisdiction to grant relief. Paragraph 38 deprives the Name of an interest in the funds set up as part of the scheme to provide the Debt Credits in the event of a breach of the obligation to pay the reduced sum by 30 September 1996. It is accordingly a provision for forfeiture against which equity will relieve in appropriate circumstances.

Lloyd's' short answer to this argument is that the doctrine of relief against forfeiture is applicable only where the alleged forfeiture is of some proprietary interest, and the Settlement Agreement makes it clear in paragraph 9 of Appendix 2 to the Settlement Offer Document that a Name has no proprietary interest in the Settlement Fund, which, as defined in Schedule 1 to the Settlement Agreement, includes Debt Credits. Paragraph 9 of Appendix 2 expressly provides that:

irrespective of any references to allocations of debt credits . . . no Name or other person will have an interest of any type in any part of the settlement fund . . ."

In the context of this submission counsel for Lloyd's relied on BICC plc v Burndy Corporation [1985] Ch 232, [1985] 1 All ER 417, in which, at page 252A of the former report Dillon LJ said, in a judgment with which the other members of the court agreed:

There is no clear authority, but for my part I find it difficult to see why the jurisdiction of equity to grant relief against forfeiture should only be available where what is liable to forfeiture is an interest in land and not an interest in personal property. Relief is only available where what is in question is forfeiture of proprietary or possessory rights, but I see no reason in principle for drawing a distinction as to the type of property in which the rights subsist. The fact that the right to forfeiture arises under a commercial agreement is highly relevant to the question whether

relief against forfeiture should be granted, but I do not see that it can preclude the existence of the jurisdiction to grant relief, if forfeiture of proprietary or possessory rights, as opposed to merely contractual rights, is in question."

Mr Oliver QC, counsel for Mr Jones, sought to persuade me that on their true construction the words I have just quoted from paragraph 9 of Appendix 2 mean that a Name acquires no interest in any divided share of the Settlement Fund. They are quite consistent with the Settlement Fund belonging to the Names in undivided shares, ie. as joint tenants as opposed to tenants in common. Despite its ingenuity I cannot accept that submission. It seems to me clear that the intent - and effect - of the Settlement Agreement, and in particular the words I have quoted from paragraph 9 of Appendix 2, are that a Name has no proprietary interest in the Settlement Fund. The provisions relating to the application of Debt Credits to Names' primary liabilities have effect in contract only. It follows, in my judgment, that, even if it might otherwise be applicable, the doctrine of relief against forfeiture can have no application to a Name's loss of the benefit of a deduction from his primary underwriting liability in respect of Debt Credits.

Mr Jones' Compliance Argument

Counsel for Mr Jones put forward a further alternative submission that it was at least arguable that Mr Jones in fact complied with all his obligations under the Settlement Agreement by offering through his bank a guarantee in the sum of £100,000, leaving it to Lloyd's to produce the form of guarantee it required, which it never did. The offer was made by National Westminster Bank's letter to Lloyd's of 28 October 1996, to which I have referred earlier in this judgment.

Clearly the offer of such a guarantee cannot have satisfied Mr Jones' obligations under the terms of the Settlement Agreement itself. For to satisfy those obligations he had to pay (in accordance with his letter of acceptance of the Settlement Offer Document) £15,000 in cash and produce a satisfactory offer of a bank guarantee in the sum of £84,999 plus interest for five years in accordance with the terms of the Settlement Offer Document relating to Structured Payment Plans. However Mr Oliver submitted that it is at least seriously arguable that the only sensible interpretation of the correspondence between Lloyd's and Mr Jones which I have quoted earlier in this judgment is that Lloyd's either (a) agreed to vary the terms of the Settlement Agreement in the case of Mr Jones to the effect that a guarantee for £100,000 would represent complete satisfaction of his obligations or (b) entered into a collateral contract with Mr Jones to that effect or (c) exercised their power under the Settlement Agreement to waive its conditions to similar effect. In this respect Mr Jones relies on the letter of 4 November 1996 from Lloyd's to Mr Jones' accountant (which I have quoted earlier), in which Lloyd's said that the notice of default sent by Lloyd's to Mr Jones on 18 October 1996 would not apply to Mr Jones:

assuming that the bank guarantee is provided as requested."

I do not consider there is any real substance in this submission. I accept that Lloyd's letter of 4 November is odd. As I have already said, apart from anything else it ignores Mr Jones' failure to pay his £15,000 by 30 September. Reading that letter in the context of the surrounding correspondence it is, in my judgment, clear that it was written in error. In my judgment it cannot prove any variation of the Settlement Agreement by agreement between Lloyd's and Mr Jones, because the Settlement Agreement was a multipartite agreement that could not be varied by two parties to it. As for the submission that the letter of 4 November evidences a collateral contract, again I find it impossible to see how such a contract can have been effective to vary the terms of the Settlement Agreement under which all parties to it had an interest in seeing its terms adhered to, save to the extent that Lloyd's was given power by Clause 12.12 to grant indulgence to another party on the terms set out in that sub-clause.

As for the alternative submission that the letter of 4 November 1996 is evidence of an exercise by Lloyd's of its power under Clause 12.12 of the Settlement Agreement to waive the requirement of strict compliance with the terms of that Agreement, this submission fails, if for no other reason, because Clause 12.12 requires any indulgence granted under that power to be in writing expressly stating that it represents an exercise of that specific power.

Finally counsel for Mr Jones sought to argue that the letter of 4 November gave rise to some sort of estoppel against Lloyd's now enforcing its strict rights under the Settlement Agreement as against Mr Jones. This submission is, in my judgment, bound to fail, because there is no evidence that Mr Jones in any way acted, or failed to act, in reliance on the letter. Indeed his evidence is that he did not even know of the letter at the time it was written to his accountants. He has only recently learnt of it. There is no evidence that his accountants acted in any way on his

behalf in reliance on the letter. Moreover no guarantee was ever produced to Lloyd's as required by the letter. Mr Jones complains that Lloyd's did not provide the draft that had been asked for by his bank in its letter to Lloyd's of 28 October 1996, but it seems strange indeed, if the accountants were somehow relying on the letter of 4 November as a representation that Lloyd's were not going to insist on strict compliance by Mr Jones with his obligations under the Settlement Agreement, that there is no suggestion that after receipt of that letter, which in terms required Mr Jones to produce a guarantee, the accountants ever asked Lloyd's for a draft.

Conclusion in Mr Jones' Case

The power of the court to grant an application such as that made by Mr Jones to set aside a statutory demand is to be found in rule 6.5 of the Insolvency Rules 1986 (SI 1986 No 1925). Rule 6.5(4) provides, so far as material:

The court may grant the application [to set aside a statutory demand] if:

(a) . . .

(b) the debt is disputed on grounds which appear to the court to be substantial; or

(c) . . . ; or

(d) the court is satisfied, on other grounds, that the demand ought to be set aside."

In my judgment, there is no substance in any of the submissions made on behalf of Mr Jones to dispute the debt claimed by Lloyd's in its statutory demand, and, despite his very thorough and ingenious submissions, Mr Oliver failed to show me any other reason to be satisfied that the demand ought to be set aside.

Accordingly I shall dismiss Mr Jones' application.

Conclusion in Mr Standen's Case

For the reasons I have already endeavoured to explain Mr Standen's argument that Lloyd's claim against him is largely based on an unenforceable penalty or a relievable forfeiture fails.

In fact Mr Standen has not paid any part of the debt claimed by Lloyd's, not even the net amount shown on his Finality Statement. He now submits that I should order the taking of an account between himself and Lloyd's, because he maintains (in the form of a statement made by his solicitor) that the Finality Statement fails to account for a sum of some £70,000 odd in respect of his entitlement under certain stop loss policies. Even if this argument were right, the fact remains that Mr Standen has paid no part of the undisputed part of Lloyd's' claim. Therefore this point can be no reason for not making a bankruptcy order, as is recognised by its omission from Mr Standen's notice of opposition to the petition served under rule 6.21 of the Insolvency Rules 1986.

However, from evidence filed on an application under section 284 of the Insolvency Act 1986 made by Mr Standen since I reserved judgment on the bankruptcy petition it appears that, by reason of the sale of certain property owned by him, he may now be in a position to pay all his debts. As I have already indicated to counsel, I wish to hear further submissions on behalf of Lloyd's and Mr Standen as to whether, in the light of the latest evidence of Mr Standen's financial position, I should make a bankruptcy order, having regard to the discretion conferred on the court by section 271(3) of the Insolvency Act 1986. As I have also indicated to counsel, I also wish to hear further argument in the light of the conclusions reached in this judgment as to whether I should, as Mr Standen submits, make some order for an account as between him and Lloyd's to deal with Mr Standen's argument on his stop loss insurance entitlement.

DISPOSITION:
Judgment accordingly.

SOLICITORS:
None stated at original source