

**EASTERN CARIBBEAN SUPREME COURT
IN THE HIGH COURT OF JUSTICE**

SAINT LUCIA

COMMERCIAL DIVISION

CLAIM NO. SLUHCM2020/ 0022 formerly SLUHCM2018/ 0088

**IN THE MATTER OF A PETITION FOR THE WINDING UP OF
HARLEQUIN BOUTIQUE HOTEL LIMITED**

**AND IN THE MATTER OF SECTION 385 (a) and 387 OF THE
COMPANIES ACT CAP 13.01 OF THE REVISED EDITION OF
THE LAWS OF SAINT LUCIA**

BETWEEN:

JP SERVICES CORPORATION LLC

Applicant

and

**HARLEQUIN BOUTIQUE HOTEL LIMITED
[In Liquidation]**

Respondent

Before:

The Hon. Mde. Justice Cadie St Rose-Albertini

High Court Judge

Appearances:

Mr. Bota McNamara with Mr Anwar Brice for the Applicant
Mr. Garth Patterson KC, with Ms Taylor Laurayne and Mr Mark Maragh for the Respondent
Mr Luke Foster of Counsel for the Financial Services Compensation Scheme Limited of the UK,
as interested creditor
Mrs Candace Polius of Counsel for the National Insurance Corporation as interested creditor
Mrs Antonia Charlemagne of Counsel for the Inland Revenue Department as Interested Creditor
Mr Andie George and Ms Sherene Francis of Counsel for the Water and Sewerage Company Inc
as interested creditor

2022: July 14;
October 11

DECISION IN CHAMBERS

- [1] **ST ROSE-ALBERTINI, J. [Ag]:** The applicant, JP Services Corporation LLC (“JPSC”), is a creditor of the respondent, Harlequin Boutique Hotel Limited (“HBH”) in liquidation. JPSC is aggrieved by the decision of the joint liquidators of HBH, to disallow its debt claim in entirety, in the liquidation, and has applied to the Court for the following orders:
- (i) that the joint liquidators’ Notice of Disallowance of Claim dated 28th January 2022 be reversed;
 - (ii) that its Proof of Claim dated 16th August 2021 be allowed in full; and
 - (iii) costs.

Background

- [2] HBH owns Blu Hotel Saint Lucia (“Blu” or “the Hotel”) and the property registered as Block 1256B Parcels 25 and 26 in the quarter of Gros-Islet (“the Property”), on which Blu is situate. JPSC is a company that provides advice and operations to companies facing economic and management difficulty. On 25th September 2017, HBH entered into a Hotel Operation and Management Services Agreement with JPSC to manage and operate Blu (“the Management Agreement” or “the Agreement”).
- [3] Subsequently, on 5th October 2018, a petition for the compulsory winding-up of HBH was filed. Thereafter, on 23rd October 2018, JPSC filed a claim against HBH for XCD\$14,364,000.00 plus interest, as liquidated damages for breach of the Management Agreement. On 14th November 2018, JPSC obtained judgment in default of acknowledgment of service against HBH for the sum claimed plus costs (the “Default Judgment”).

- [4] On 20th November 2018, joint provisional liquidators were appointed for HBH, and on 14th January 2019, it was ordered that HBH be compulsorily wound up and the joint provisional liquidators were appointed as the joint liquidators. On 21st May 2019, the joint liquidators applied for and received approval for sale of the Property, as HBH's sole asset, for the agreed purchase price of US\$3,000,000.00. The Managing Director of JPSC, Mr Jeffrey Coyne, and Counsel for JPSC were present at the hearing and did not object to the sale. Thereafter on 8th August 2019, JPSC registered the Default Judgment at the Office of Deeds and Mortgages, and on 9th August 2019 registered it at the Land Registry, as an encumbrance over the Property, thereby creating a judicial hypothec.
- [5] On 20th August 2019, the joint liquidators filed an application to set aside the Default Judgment and to cancel the judicial hypothec. On 30th September 2019 the set aside application was dismissed. Although HBH had shown a real prospect of successfully defending the claim, it had failed to meet the other requirements of CPR 13.3(1) and (2). On the same day, the application to cancel registration of the judicial hypothec was allowed as having been registered without leave of the court after the winding-up order had been made, in violation of article 1915 of the **Civil Code**¹ and sections 391 and 394 of the **Companies Act**.² The liquidation proceeded with JPSC having an unregistered judgment against HBH.
- [6] JPSC's Proof of Claim was submitted for the full sum arising from the Default Judgment. It was stated to be an unsecured sum for which JPSC claimed no priority and for which no payments had been received from HBH and no credits had been allowed by JPSC. The liquidators' Notice of Disallowance of Claim sets out the reasons for refusal of the claim. They noted that the only evidence supporting JPSC's Proof of Claim was the Default Judgment. They asserted that, in carrying out their duties as liquidators, they were entitled to investigate the nature and grounds of every claim filed and to go behind judgments obtained against HBH, and covenants for payment given by HBH, and to require satisfactory evidence that the debt on which proof is founded is a real debt that is justly and truly due. They concluded that had there been a properly conducted judicial process in

¹ Cap 4.01 of the Laws of Saint Lucia

² Cap 13.01 of the Laws of Saint Lucia

Claim No. SLUHCV2018/0522, instead of the claim being summarily determined in default of HBH's acknowledgment, it is likely that the court would have found that JPSC was not entitled to the full amount awarded in the Default Judgment.

- [7] The liquidators reasoned that the Management Agreement which took effect on 25th September 2017 was terminated by JPSC on 7th December 2017 because of HBH's alleged default. The judgment sum was claimed pursuant to a clause in the Agreement which provided for payment of liquidated damages in the sum of XCD\$14,364,000.00, calculated by multiplying US\$5,000.00 by the number of guest rooms, by the number of remaining years of the term of the Agreement. Notwithstanding, under the terms of the Agreement, JPSC was entitled to payment of 3% of Blu's gross revenue plus an incentive fee of 7.5% of its gross operating profit per year, in consideration of performance. The liquidators noted that JPSC had not provided evidence of HBH or Blu's financial performance during the period 25th September to 7th December 2017 to determine the amount which would have been due to JPSC under the Agreement for that period, had the contract been properly performed.
- [8] The liquidators concluded that as HBH had not been operating at a profit during the period in question, and JPS had not provided evidence of actual damage suffered. Further that JPSC would likely only have sustained nominal loss or damages, if any. The liquidators further concluded that as the liquidated damages stipulated in the Management Agreement is extravagantly disproportionate to the highest level of loss or damage that would have foreseeably arisen from HBH's breach of the Agreement, a court would have determined the liquidated damages clause to be a penalty, and not a genuine pre-estimate of damage and, therefore, unenforceable.
- [9] They considered that they were therefore entitled to disregard the liquidated damages clause and require satisfactory evidence that JPSC's claim represents real indebtedness by HBH. However, since JPSC had failed to furnish evidence of loss suffered, as requested, they concluded that they were unable to verify the amount justly due, and therefore, disallowed the claim.

The Issue

- [10] The sole issue on this application is whether the circumstances in which the default judgment was obtained are circumstances which warrant the Court and the liquidator to go behind the judgment, to consider the validity of the debt. If so, the Court would then have to go on to consider such evidence, as is presented, afresh and determine the just amount, if any, due to JPSC from HBH.

The Law

- [11] The application is made pursuant to section 407(5) of the Companies Act.³ It states:

“407. Exercise and control of liquidator’s powers

.....

(5) If any person is aggrieved by any act or decision of the liquidator, that person may apply to the court, and the court may confirm, reverse, or modify the act or decision complained of, and make such order as it thinks fit.”

- [12] On the authority of **Re Kentwood Constructions Ltd.**⁴, when an application is made to the court to reverse the decision of a liquidator to reject a proof of debt, the court is bound to decide the rights of the claimant in light of the evidence which is before the court, and which is commonly much fuller than the evidence available to the liquidator at the time when he decided to reject the proof. The function of the court is not limited merely to expressing a view on whether the liquidator was right or wrong in rejecting the proof, when he rejected it. The court may vary the decision in any way that it thinks necessary in the light of the evidence before it. The court must approach the question de novo and determine to what extent the creditor ought to be allowed to rank as a proving creditor.

- [13] It is well established that in doing so, the court is entitled to look behind a judgment debt to see whether it is in fact due, and in this regard, the power of the liquidator is no different from that of the court. The rationale for the principle is that the duty of the liquidator is to

³ Cap 13.01 of the Laws of Saint Lucia.

⁴ [1960] 2 All ER 655 at page 656.

ensure that the assets of an insolvent company are distributed amongst those who are justly, legally, and properly creditors. It is also equally well-established that the court or a liquidator will not look behind every judgment debt to consider afresh its validity, but will only do so in appropriate circumstances such as those tending to show fraud, collusion, or a miscarriage of justice. 'Miscarriage of justice', although of wide application, has been accepted as including circumstances where for some good reason there ought not to have been a judgment; circumstances which warrant a judgment being treated as not creating or evidencing any debt enforceable in bankruptcy proceedings; and circumstances from which it can conclude that had there been a properly conducted judicial process it would have been found, or very likely would have been found, that nothing was in fact due to a claimant. Thus, a liquidator and the court are entitled to go behind a judgment and to require satisfactory evidence that the debt on which the proof is founded is a real debt.⁵

- [14] The relevant principles were skillfully summarized in **Menastar Finance Ltd (in liq), Menastar Ltd. v Simon**⁶, which I have extracted below. There the applicant was a creditor in the winding up of its wholly owned subsidiary (MFL) which had been managed by another company (BMS). BMS had obtained an order for summary judgment in an action against MFL for unpaid management fees and interest, and the liquidator had admitted BMS' proof of debt based on that summary judgment order. The applicant applied for an order reversing the decision of the liquidator to admit BMS' proof of debt on the basis that the judicial process from which the summary judgment arose had not been properly conducted and therefore the court should look behind the judgment and reverse the liquidator's decision. In support of its application, the applicant contended that MFL always had a good defence to the action by BMS; MFL had a counterclaim in excess of the amount claimed which had been withdrawn; and MFL was absent and unrepresented at the summary judgment hearing.

- [15] Etherton J held:

"The law

⁵ Menastar Finance Ltd (in liq), Menastar Ltd. v Simon [2003] 1 BCLC 338

⁶ [2003] 1 BCLC 338

[43] There is a long line of authority going back to the nineteenth century establishing the principle that, on making a winding-up order or a bankruptcy order, and, in the case of both personal and corporate insolvency, **in considering whether to admit a creditor's proof based on a judgment debt, the court can in appropriate circumstances go behind the judgment to see whether the debt is truly due.**

[44] **The power of a liquidator is, in this respect, no different from that of the court itself, since the liquidator, in deciding whether to accept or reject a creditor's proof in whole or in part, is acting in a quasi-judicial capacity: see *Tanning Research Laboratories Inc v O'Brien* [1990] LRC (Comm) 664 at 670, (1990) 8 ACLC 248 at 253, citing *Re Britton & Millard Ltd* (1957) 107 LJ 601. His statutory duty is to ensure that the company's property is collected in and applied in satisfaction of its liabilities *pari passu* among its proper creditors.**

[45] In deciding whether to go behind the judgment debt, and, if so, in appraising the validity of the creditor's claim, **neither the court nor the liquidator nor the trustee in bankruptcy is limited to the evidence that was before the court when it gave its judgment: see *Re Trepka Mines Ltd* [1960] 3 All ER 304, [1960] 1 WLR 1273.**

[46] **The rationale behind the principle is that the duty of the liquidator is to ensure that the assets of the insolvent company 'are distributed amongst those who are justly, legally and properly creditors ...': see *Re Van Laun, ex p Chatterton* [1907] 2 KB 23 at 29 per Cozens-Hardy MR, and also *Ex p Kibble, Re Onslow* (1875) LR 10 Ch App 373 at 376–377 per Sir W M James LJ. The same is equally true of the trustee of a bankrupt.**

[47] In *Re Van Laun, ex p Chatterton*, the Court of Appeal approved the way the matter had been put by Bigham J at first instance, who said ([1907] 1 KB 155 at 162–163):

'The trustee's right and duty when examining a proof for the purpose of admitting or rejecting it is to require some satisfactory evidence that the debt on which the proof is founded is a real debt. No judgment recovered against the bankrupt, no covenant given by or account stated with him, can deprive the trustee of this right. He is entitled to go behind such forms to get at the truth, and the estoppel to which the bankrupt may have subjected himself will not prevail against him. In the present case the trustee desires to satisfy himself that the claims for costs represent a real indebtedness. He can only do this by seeing and examining the bills. When he sees them, it may be that he

thinks them fair and reasonable and, if so, he will probably admit the truth. But until Mr. Chatterton furnishes him with the means of forming an opinion I think the trustee cannot do otherwise than reject the proof.'

[48] It is equally well established that the court (and the liquidator or trustee in bankruptcy) will not, as a matter of course, look behind every judgment debt and consider afresh the validity of the debt. *In Re Flatau, ex p Scotch Whisky Distillers Ltd (1888) 22 QBD 83 at 85*, Lord Esher MR said:

'It is not necessary now to repeat that, when an issue has been determined in any other court, if evidence is brought before the Court of Bankruptcy of circumstances tending to shew that there has been fraud, or collusion, or miscarriage of justice, the Court of Bankruptcy has power to go behind the judgment and to inquire into the validity of the debt. But that the Court of Bankruptcy is bound in every case as a matter of course to go behind a judgment is a preposterous proposition.'

[49] There has been some debate before me as to the circumstances, outside fraud and collusion, in which the court will (and a liquidator or trustee in bankruptcy should) go behind a judgment in order to examine the validity of the creditor's proof. *In Re Flatau*, as has been seen from the passage I have quoted, Lord Esher MR referred to circumstances in which there has been a 'miscarriage of justice'. In the earlier case of *Ex p Lennox, Re Lennox (1885) 16 QBD 315 at 323* Lord Esher MR said that the court is bound to look into the alleged debt 'upon a sufficient case being shewn'. *In Re Van Laun, ex p Chatterton [1907] 2 KB 23 at 31*, Buckley LJ, drawing the two statements of Lord Esher MR together, said:

'If there be a judgment it is not necessary to shew fraud or collusion. It is sufficient, in the language of Lord Esher, to shew miscarriage of justice—that is to say, that for some good reason there ought not to have been a judgment.'

[50] Many of the authorities were reviewed by Warner J in *McCourt v Baron Meats Ltd [1997] BPIR 114*. Warner J, with whose judgment Peter Gibson J agreed, said that the bankruptcy court would—

'in appropriate circumstances go behind the judgment, that is to say, inquire into the circumstances in which the judgment was obtained and, if satisfied that those circumstances warrant such a course, treat it as not creating or evidencing any debt enforceable in bankruptcy proceedings.' (See *[1997] BPIR 114 at 120*.)

[51] Finally, in *Dawodu v American Express Bank* [2001] BPIR 983 at 990, I said, by way of observation on the summary of the law by Warner J in the *McCourt* case:

*'... what is required before the court is prepared to investigate a judgment debt, in the absence of an outstanding appeal or an application to set it aside, is some fraud, collusion or miscarriage of justice. The latter phrase is of course capable of wide application according to the particular circumstances of the case. What in my judgment is required is that the court be shown something from which it can conclude that had there been a properly conducted judicial process it would have been found, or very likely would have been found, that nothing was in fact due to the claimant.'*⁷

[Emphasis added]

[16] However, in applying the law to the facts of that case, Etherton J determined that the liquidator was fully justified in refusing to go behind the judgment, as the applicant was responsible for the withdrawal of assets from MFL, its wholly owned subsidiary, by way of dividend, so as to leave MFL unable to defend BMS' action. Further, the applicant had taken the deliberate decision not to fund MFL to fight BMS' action, or to appeal against or set aside the summary judgment, or indeed to challenge the winding-up petition brought by BMS on the ground that MFL was not, in fact, indebted to BMS. The decision to challenge the debt on which the summary judgment was based was taken only after, and because of, the liquidator's decision to pursue the applicant in the winding up. In the circumstances, there was no reason for the court to come to the applicant's assistance, bearing in mind that applicant itself had engineered the situation in which there was no active defence to the BMS' action and no representation of MFL on the summary judgment hearing.⁸

[17] Another useful case is **Barclays Bank plc v Atay**, where the court, quoted Warner J in *McCourt and Siequien v Baron meats Ltd and the Official Receiver*. Warner J considered the authorities concerning the jurisdiction to go behind judgments and summarized the principles and the factual circumstances that have been held to warrant same as follows:-

"(1) A court exercising the bankruptcy jurisdiction (a "bankruptcy court"), although it will treat a judgment for a sum of money as prima facie evidence that the

⁷ At pages 346 to 348; See also paragraphs 52-56 at pages 348-349 of the judgment.

⁸ At paragraphs 52-56, pages 348-349.

judgment debtor is indebted to the judgment creditor for that sum may, in appropriate circumstances, go behind the judgment, that is to say, inquire into the circumstances in which the judgment was obtained and, if satisfied that those circumstances warrant such a course, treat it as not creating or evidencing any debt enforceable in bankruptcy proceedings.

(2) The reason for the existence of that power of a bankruptcy court is that such a court is concerned not only with the interests of the judgment creditor and of the judgment debtor, but also with the interests of the other creditors of the judgment debtor. *The point was succinctly made by James LJ in Ex parte Kibble; In re Onslow (1875) LR 10 Ch App 373 at 376-377, in the following words:*

“It is the settled rule of the court of bankruptcy, on which we have always acted, that the court of bankruptcy can inquire into the consideration for a judgment debt. There are obviously strong reasons for this, because the object of the bankruptcy laws is to procure the distribution of a debtor's goods among his just creditors. If a judgment were conclusive, a man might allow any number of judgments to be obtained by default against him by his friends or relations without any debt being due on them at all; it is therefore necessary that the consideration of the judgment should be liable to investigation.”

(3) It follows that the grounds upon which a bankruptcy court may go behind a judgment are more extensive than the grounds upon which an ordinary court of law or equity may set it aside.

(4) In particular, a bankruptcy court will go behind a judgment if satisfied that the judgment creditor manifestly had no claim against the judgment debtor on which the judgment could have been founded. Thus, in Ex parte Kibble the court went behind a judgment obtained by default which was founded on a bill of exchange drawn by the debtor during his infancy. In Ex parte Banner; In re Blythe (1881) 17 Ch D 480 it went behind a judgment giving effect to a compromise of an action brought by one party to a fraud against the other party to it for the fruits of it. Ex parte Lennox; In re Lennox (1885) 16 QBD 315 was a somewhat similar case. In that case the court ordered an inquiry into the facts because the debtor, who had submitted to the judgment tendered evidence to the effect that the debt on which the judgment, was founded never really existed, but was based on the fault of the creditor. Lastly, in In re Fraser (above) the court went behind a judgment obtained by the holders of a bill of exchange against a former partner in the firm in whose name the bill had been accepted. He was not liable on the bill, but his defence to an action on the bill had been so ineptly

conducted that the judgment had been obtained against him on Ord 14 and that an application made on his behalf for the judgment to be set aside had failed...’’⁹ [Emphasis added]

[18] At paragraph 9 of the **Barclays Bank case**, in considering the justification of the power and quoting the text Law of Insolvency by Ian Fletcher, the court commented:

*“... But the far more usual occasion for invoking this doctrine is when it is the debtor who will otherwise suffer injustice, and this is particularly capable of occurring when the judgment was obtained by a compromise of action or by default. **A default judgment, by its very nature involves a one-sided presentation of the facts which may lack objectivity and may even be inaccurate or unfair**, whilst it may equally be possible to show that the terms upon which an action was compromised were unfair or unreasonable from the debtor’s point of view. **In either situation if the court accepts that the result is unfair the petition may be dismissed**”. [Emphasis added]*

Analysis

[19] Counsel for the joint liquidators have argued that the Court is entitled to look behind the Default Judgment because the amount of the judgment debt was based on the liquidated damages clause in the Management Agreement. The argument is that the liquidated damages clause would have been found to be a penalty and not a genuine pre-estimate of damages, and therefore void and unenforceable, had there been a hearing of JPSC’s claim on its merits. The liquidators contends that in such a case, it is likely that nothing, or an amount significantly less than the Default Judgment sum would have been found to be due from HBH to JPSC. This, Counsel says, amounts to a miscarriage of justice that warrants the Court treating the judgment debt as not creating or evidencing any debt which is enforceable in the liquidation.

[20] On the other hand, Counsel for JPSC asserted that no fraud, collusion, or miscarriage of justice occurred and there is no compelling circumstance to warrant looking behind the judgment. He submits further that the actions of the liquidators amount to an abuse of

⁹ At paragraph 10.

process, as the question of whether the judgment sum is a penalty or liquidated damages was ventilated previously and the joint liquidators were not entitled to determine that question, which is a matter of law. Counsel submits that in any event, the joint liquidators have not shown how the amount is extravagant or unconscionable. They have not considered that much of the contract contained front-end loaded damages. The contract was for 15 years, it was revenue generating and the liquidators have not ascertained what loss of income or bargain JPSC suffered, so as to put JPSC in the same position it would have been had the contract been fully performed. If that sum equals the amount of the default judgment, there can be no extravagance.

[21] The liquidated damages clause in the Management Agreement provides as follows:

“(C) Termination by JPS. In case of termination of this Agreement by JPS, caused by the Owner’s breach, JPS shall have the right to (i) collect all amounts owed by Owner in connection to Management Fees, Incentive Fees, reimbursements of Expenses and/or any other amounts payable to JPS pursuant to this Agreement, (ii) liquidated damages in the following terms:

(i) Liquidated damages: equivalent 50% (fifty percent) of the sum of the Management Fee and the Incentive Fee of the last 12 months multiplied by the remaining Fiscal years of the Term of the Agreement.

(ii) If termination by JPS occurs before the 12 (twelfth) month mentioned in item (i) above has lapsed, then the liquidated damages will be the amount that results from multiplying \$5,000.00 by the number of rooms referred to in paragraph (B) of Section Two of this Agreement, by the number of remaining years in the Agreement’s Term.”

[22] The law in relation to whether a stipulated sum in a contract will be considered a penalty or liquidated damages has been authoritatively set out in a number of cases. In **Dunlop Pneumatic Tyre Company Limited v New Garage and Motor Company Limited**¹⁰, Lord Dunedin set out the following principles:

“1. Though the parties to a contract who use the words "penalty" or "liquidated damages" may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment

¹⁰ [1915] A.C. 79

stipulated is in truth a penalty or liquidated damages. This doctrine may be said to be found passim in nearly every case.

2. The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage (*Clydebank Engineering and Shipbuilding Co. v. Don Jose Ramos Yzquierdo y Castaneda* (1)).

3. The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach (*Public Works Commissioner v. Hills* (1) and *Webster v. Bosanquet* (2)).

4. To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are:

(a) It will be held to be penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach. (Illustration given by Lord Halsbury in *Clydebank Case*. (3))

(b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid (*Kemble v. Farren* (4)). This though one of the most ancient instances is truly a corollary to the last test. Whether it had its historical origin in the doctrine of the common law that when A. promised to pay B. a sum of money on a certain day and did not do so, B. could only recover the sum with, in certain cases, interest, but could never recover further damages for non-timeous payment, or whether it was a survival of the time when equity reformed unconscionable bargains merely because they were unconscionable, - a subject which much exercised Jessel M.R. in *Wallis v. Smith* (5) - is probably more interesting than material.

(c) There is a presumption (but no more) that it is penalty when "a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage" (Lord Watson in *Lord Elphinstone v. Monkland Iron and Coal Co.* (6)).

On the other hand:

(d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties (Clydebank Case, Lord Halsbury (1); Webster v. Bosanquet, Lord Mersey (2)).”¹¹

[23] Lord Dunedin further clarified that what is meant by the expression ‘incapable of being ascertained’ is that it is a case where no rule or measure of damages is available for the guidance of a jury as to the amount of the damages, and a judge would have to tell them they must fix the amount as best they can.

[24] His Lordship analyzed the case thus:

*“Turning now to the facts of the case, it is evident that the damage apprehended by the appellants owing to the breaking of the agreement was an indirect and not a direct damage. So long as they got their price from the respondents for each article sold, it could not matter to them directly what the respondents did with it. Indirectly it did. Accordingly, the agreement is headed “Price Maintenance Agreement,” and the way in which the appellants would be damaged if prices were cut is clearly explained in evidence by Mr. Baisley, and no successful attempt is made to controvert that evidence. But though damage as a whole from such a practice would be certain, yet damage from any one sale would be impossible to forecast. It is just, therefore, one of those cases where it seems quite reasonable for parties to contract that they should estimate that damage at a certain figure, and provided that figure is not extravagant there would seem no reason to suspect that it is not truly a bargain to assess damages, but rather a penalty to be held in terrorem.”*¹²

[25] In **Clydebank Engineering and Shipbuilding Company Limited and others v Don Jose Ramos Yzquierdo y Castaneda and others**¹³, Halsbury L.C. stated:

“We come then to the question, What is the agreement here? and whether this sum of money is one which can be recovered as an agreed sum as damages, or whether, as has been contended, it is simply a penalty to be held over the other

¹¹ At pages 86-88

¹² At page 88

¹³ 1905 A. C. 6

party in terrorem - whether it is, what I think gave the jurisdiction to the Courts in both countries to interfere at all in an agreement between the parties, unconscionable and extravagant, and one which no Court ought to allow to be enforced.

My Lords, it is impossible to lay down any abstract rule as to what it may or it may not be extravagant or unconscionable to insist upon without reference to the particular facts and circumstances which are established in the individual case. I suppose it would be possible in the most ordinary case, where people know what is the thing to be done and what is agreed to be paid, to say whether the amount was unconscionable or not. For instance, if you agreed to build a house in a year, and agreed that if you did not build the house for 50l., you were to pay a million of money as a penalty, the extravagance of that would be at once apparent. **Between such an extreme case as I have supposed and other cases, a great deal must depend upon the nature of the transaction - the thing to be done, the loss likely to accrue to the person who is endeavouring to enforce the performance of the contract, and so forth.** It is not necessary to enter into a minute disquisition upon that subject, because the thing speaks for itself. But, on the other hand, it is quite certain, and an established principle in both countries, that the parties may agree beforehand to say, "Such and such a sum shall be damages if I break my agreement." The very reason why the parties do in fact agree to such a stipulation is that sometimes, although undoubtedly there is damage and undoubtedly damages ought to be recovered, the nature of the damage is such that proof of it is extremely complex, difficult, and expensive..."¹⁴[Emphasis added]

[26] In the case of **Cavendish Square Holding BV v Talal El Makdessi**¹⁵ commenting on the **Dunlop case** and the nature of the investigation of whether a sum is a penalty, Lord Neuberger and Lord Sumption had this to say:

"[23] Lord Atkinson pointed (pp 90-91) to the critical importance to Dunlop of the protection of their brand, reputation and goodwill, and their authorised distribution network. Against this background, he observed (pp 91-92):

"It has been urged that as the sum of £5 becomes payable on the sale of even one tube at a shilling less than the listed price, and as it was impossible that the appellant company should lose that sum on such a transaction, the sum fixed must be a penalty. In the sense of direct and immediate loss the appellants lose nothing by such a sale. It is the agent

¹⁴ At pages 10-11.

¹⁵ [2015] UKSC 67

or dealer who loses by selling at a price less than that at which he buys, **but the appellants have to look at their trade in globo, and to prevent the setting up, in reference to all their goods anywhere and everywhere, a system of injurious undercutting. The object of the appellants in making this agreement, if the substance and reality of the thing and the real nature of the transaction be looked at, would appear to be a single one, namely, to prevent the disorganization of their trading system and the consequent injury to their trade in many directions. The means of effecting this is by keeping up their price to the public to the level of their price list, this last being secured by contracting that a sum of £5 shall be paid for every one of the three classes of articles named sold or offered for sale at prices below those named on the list.** The very fact that this sum is to be paid if a tyre cover or tube be merely offered for sale, though not sold, shows that **it was the consequential injury to their trade due to undercutting that they had in view. They had an obvious interest to prevent this undercutting, and on the evidence it would appear to me impossible to say that that interest was incommensurate with the sum agreed to be paid."** [Emphasis Added]

Lord Atkinson went on to draw an analogy, which has particular resonance in the *Cavendish* appeal, with a clause dealing with damages for breach of a restrictive covenant on the canvassing of business by a former employee. In this context, he said (pp 92-93):

"It is, I think, quite misleading to concentrate one's attention upon the particular act or acts by which, in such cases as this, the rivalry in trade is set up, and the repute acquired by the former employee that he works cheaper and charges less than his old master, and to lose sight of the risk to the latter that old customers, once tempted to leave him, may never return to deal with him, or that business that might otherwise have come to him may be captured by his rival. **The consequential injuries to the trader's business arising from each breach by the employee of his covenant cannot be measured by the direct loss in a monetary point of view on the particular transaction constituting the breach."** [Emphasis added]

Lord Atkinson was making substantially the same point as Lord Robertson had made in the *Clydebank* case. **"The question was: what was the nature and extent of the innocent party's interest in the performance of the relevant obligation. That interest was not necessarily limited to the mere recovery of compensation for the breach.**

Lord Atkinson considered that the underlying purpose of the resale price maintenance clause gave Dunlop a wider interest in enforcing the damages clause than pecuniary compensation. £5 per item was not incommensurate with that interest even if it was incommensurate with the loss occasioned by the wrongful sale of a single item.”¹⁶

[27] Attempting to refine the test, Lord Neuberger and Lord Sumption stated:

“[28] ... A damages clause may properly be justified by some other consideration than the desire to recover compensation for a breach. This must depend on whether the innocent party has a legitimate interest in performance extending beyond the prospect of pecuniary compensation flowing directly from the breach in question...

[31] ...The real question when a contractual provision is challenged as a penalty is whether it is penal, not whether it is a pre-estimate of loss. These are not natural opposites or mutually exclusive categories. A damages clause may be neither or both. The fact that the clause is not a pre-estimate of loss does not therefore, at any rate without more, mean that it is penal. To describe it as a deterrent (or, to use the Latin equivalent, in terrorem) does not add anything. A deterrent provision in a contract is simply one species of provision designed to influence the conduct of the party potentially affected. It is no different in this respect from a contractual inducement. Neither is it inherently penal or contrary to the policy of the law. The question whether it is enforceable should depend on whether the means by which the contracting party's conduct is to be influenced are “unconscionable” or (which will usually amount to the same thing) “extravagant” by reference to some norm.

[32] The true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation. The innocent party can have no proper interest in simply punishing the defaulter. His interest is in performance or in some appropriate alternative to performance. In the case of a straightforward damages clause, that interest will rarely extend beyond compensation for the breach, and we therefore expect that Lord Dunedin's four tests would usually be perfectly adequate to determine its validity. But compensation is not necessarily the only legitimate interest that the innocent party may have in the performance of the defaulter's primary obligations...

¹⁶ Supra note 15

[28] Applying these principles to the facts of this case, it is necessary to examine the nature of the transaction, being the obligation to be performed, the amount to be paid, and the likely loss that would accrue to the innocent party. Under the Management Agreement, it was agreed that JPSC was to provide hotel operation and management services to HBH. The term of the Agreement was 15 years. The consideration due to JPSC for performance of its obligations was a management fee and an incentive fee. The management fee was stated to be 3% of the gross revenue of the Hotel in consideration for the operation services, and the incentive fee was stated to be the amount equivalent to 7.5% of the gross operating profits of the Hotel for the years 2017, 2018 and 2019 and 10% for each fiscal year thereafter. In respect of the incentive fee, if during a given year, JPSC operated the Hotel for less than the full fiscal year, that fee would be payable in the proportion applicable. Gross revenues were to be calculated monthly and therefore both the management fee and the incentive fee were payable to JPSC in monthly installments. The Agreement also made provision for JPSC to be reimbursed for expenses incurred by it, in the performance of its obligations. Provision was made for the reimbursement of marketing expenses, reservations and online sales services expenses, and group services expenses. HBH was also required to fund operating expenses.

[29] The Agreement also lists certain default events by HBH, which would give JPSC the right to exercise any right or remedy available to it, under the Agreement, or according to law. In summary, such events were stated to be failure to make timely payments of the management fee, the incentive fee, reimbursement of expenses, funding of the operating expenses and any other amounts that HBH is required to pay to JPSC under the Agreement; filing of bankruptcy, commercial insolvency or similar action by HBH; failure to obtain permits; failure to deliver insurance policies; failure to contribute the amounts required for the Hotel operation; interference by HBH with the activities entrusted to JPSC; and early termination of the Management Agreement within the initial term of 15 years without any breach by JPSC.

[30] According to the Notice of Default and Termination of Services served by JPSC on HBH on 7th December 2017, it is alleged that the breaches of the Management Agreement were

in summary, causing cash deficits by failing to comply with demands for funding in respect of the Hotel's operations and failure to deposit all operational proceeds in JPSC's operating account. Further, JPSC alleged that HBH failed to pay its management fees and incentive fees and expenses. JPSC also alleged that contrary to warranties provided by HBH, the hotel was not free of all liens and was not in compliance with all tax obligations, and HBH also failed to maintain appropriate insurance. As notice of these defaults had been given on 7th November 2017, and were not remedied, JPSC terminated the Management Agreement.

[31] Concerning JPSC's interest in performance and the loss suffered as a result of the alleged breaches, Mr. Coyne's evidence is that Mr Dave Ames, Chairman and CEO of HBH contacted him and indicated that the Hotel was doing poorly and that he wanted to retain JPSC to manage the Hotel. JPSC has since its inception in 2004 provided advice and operations to companies in economic and management difficulty. Mr Coyne, himself, has, since 1986, worked to advise and turn around hotels in economic trouble. He had concerns about doing business with Mr Ames but agreed that if the understanding was well documented, long term and had no impropriety, JPSC would be willing to manage the Hotel. The tasks and investment by JPSC to turn around the Hotel were very much front loaded, such that money spent early in the engagement would not be repaid for years. Mr. Coyne says it was therefore very important that the Management Agreement was long term and contained substantial penalties for breach. He communicated this to Mr Ames and a draft Management Agreement was provided, which he believes to be an industry standard form. The Agreement was negotiated and amended many times over the following months. There were delays, as it appeared that Mr Ames was reluctant to hand over management during months with good cash flow, and he later learned that Mr Ames was negotiating to sell the Hotel to the current proposed purchaser.

[32] Mr. Coyne stated that the Management Agreement which was signed on 25th September 2017, contained many representations and penalty provisions, which JPSC requested because it had hired a team of professionals to perform the contracted work. Due to delays by Mr Ames, these professionals were in place and paid for several months before the Agreement was signed. Moreover, the team was hired from other long-term jobs with an

understanding that their positions were related to a long-term Management Agreement. Further, before the Hotel was handed over, an accounting system and draft budget were developed, a marketing plan created, physical inspections were performed, and repairs were planned. Thus, substantial expenditures were made in preparation for the Hotel takeover, however, from the very day of takeover, HBH breached the Management Agreement.

[33] Mr. Coyne says JPSC attempted to patch the many issues and make the arrangement work including advancing funds for salaries, advancing funds to maintain water and electricity services, and advancing funds to make urgent repairs. Mr Ames made repeated promises to remit funds, however, this was never done. JPSC provided multiple opportunities for HBH to cure the many defaults. A notice of default was sent to Mr Ames on 7th November 2017, but no attempt was made to cure the default. JPSC continued to manage the Hotel until 7th December 2017, at which time a detailed notice of termination was delivered to HBH.

[34] Mr. Coyne's evidence is that at no time during JPSC's involvement with HBH was it ever paid for services rendered under the Agreement, or reimbursed for any monies advanced on behalf of HBH. He says JPSC and himself turned away another project with a substantial monthly payment by a solvent party, to devote time to the Management Agreement and this project could not be accepted later. JPSC has never received income from HBH from the inception of the Agreement and Mr. Coyne says he has personally invested substantial monies into JPSC to mitigate the impact of the breach. The team hired for the purpose of the Management Agreement could not readily regain their previous employment and JPSC was required to maintain their employment for over a year. JPSC worked to treat this team ethically and to limit damage, which required expenditure of substantial funds. Following the breach of the Agreement JPSC was approached by a group preparing to purchase the Hotel and which proposed to work with JPSC as part of the acquisition. As a result, JPSC held off initiating litigation while these discussions were ongoing, however, when the group ceased discussions, JPSC initiated the litigation.

The Liquidated Damages Clause and the Default Judgment

- [35] The sum quantified in the liquidated damages clauses amounts to the full contract price, being an estimate of the amount that would have been earned by JPSC, if the contract had been duly performed for the entirety of the term, and assuming the Hotel performed at a particular level. It does not seek to represent the loss flowing from any particular breach and in fact applies to all conceivable breaches as set out in the events of default, including the circumstance where there has been no default by either party, but HBH simply did not wish to continue the contract.
- [36] In the circumstances, the clause seeks to compel HBH to complete the contract and, failing this, to be penalize for not doing so by paying the full contract price regardless of the circumstances. JPSC has not stated that it has any legitimate interest in enforcing the contract in this manner, or what such interest would be. It is not for the court or the liquidators to supply this. It does not seem to be like the **Dunlop case** where Dunlop was less interested in the amount of the loss on the underpricing of each individual tyre sold, but sought to protect the greater interest in preventing the disorganization of its trading system on which its entire business rested and the consequential loss. The present case also does not appear similar to the example of the breach of a restrictive covenant on the canvassing of business by a former employee, where the employer is less concerned with the particular competing act but more so with the consequential injuries to his business which cannot be measured by the direct monetary loss occasioned by the particular rival transaction.
- [37] This case seems to be strictly in the nature of a penalty and Mr. Coyne describes and justifies it as such on several occasions in his evidence. Although the description given by the parties is not conclusive, it does hold some evidential weight of their intention. Additionally, the liquidated damages clause is a secondary obligation of the kind mentioned in the **Cavendish case** where the primary obligation would have been HBH's payment obligations of fees and expenses, maintenance of insurance and so forth. The sum stipulated as liquidated damages is an additional payment, arising only upon breach of the primary obligation and is out of proportion to any legitimate interest JPSC could

have in performance of any of the primary obligations stipulated. Thus, I find that the sum stipulated as liquidated damages is a penalty and not a genuine pre-estimate of damages, or reasonable and commensurate compensation, for any legitimate interest in due performance of the obligations alleged to have been breached, and would therefore be void and unenforceable.

Is JPSC entitle to just and true compensation

[38] I agree with counsel for HBH that had the Agreement been performed, JPSC would have been entitled to payment of 3% of the Gross Revenue plus 7.5% of the Gross Operating Profit for the months from 25th September 2017 to 7th December 2017, as stated at the Seventh Clause of the Agreement and that such compensation was dependent on performance of the Hotel. I also agree that it was known and understood between the parties that the Hotel was operating poorly at the commencement of the Agreement, and that monies spent early in the engagement would not be repaid for years. Although it cannot be said with certainty, it is unlikely that the Hotel would have made a profit within the first 3 months of the contract. Hence the expected payment of management and incentive fees to JPSC, would have been a relatively small sum. However, I do not agree that all JPSC would have been entitled to is the compensation of these nominal fees, as asserted by Counsel for HBH. The Agreement also provides for payment by HBH of various expenses and amounts for funding the Hotel's operations. These would also have been included in any assessment of damages which flowed from breach of the Management Agreement.

[39] Notwithstanding that the liquidated damages clause is a penalty, I am of the view that JPSC would have been entitled to damages based on the normal measure of damages in contract, which is to put the innocent party in the position it would have been had the contract being properly performed. As such, JPSC would have been entitled to payment of its fees and expenses as expressly stipulated, and could also claim special damages for reasonable and foreseeable expenses justifiably incurred in executing its obligations under the Agreement, which would have been assessed by the court.

[40] JPSC's investment under the Agreement, was stated to be front-loaded, and HBH has not challenged the position that there would have been some legitimate expenses incurred by JPSC in performance of its obligations under the Agreement. Thus, these would ordinarily fall to be assessed by the liquidators in determining the just and true debt due from HBH to JPSC.

Conclusion

[41] In the circumstances, I conclude that the fact that the Default Judgment was based on a liquidated damages clause which was arguably a penalty, this would warrant both the liquidators and the Court looking behind the judgment. Having done so, I also conclude that the liquidated damages clause was in the nature of a penalty which would have been unenforceable, had it been tested on the merits. Nonetheless, JPSC would have been entitled to some measure of damages under the Agreement, based on the alleged breaches by HBH.

[42] On an application such as this, as a de novo hearing, the Court is entitled to consider the evidence and decide the just and true entitlement of JPSC. However, JPSC has failed to provide any evidence from which a determination or assessment of what might be justly due, can be made. All that is before the Court is the default judgment and the basis of its quantification. Thus, this Court is not in a position to conduct the exercise of assessing what would be just and truly due to JPSC. Moreover, it is very apparent that the liquidators had made repeated requests for JPSC to provide evidence and documentation in support of its proof, but JPSC stubbornly refused on the basis that it was entitled without more, to the judgment sum, and only provided the default judgment. In these circumstances the liquidators were correct in disallowing the claim.

[43] Section 407(5) of the Companies Act empowers the Court on this application to confirm, reverse, or modify the act or decision complained of, and make such order as it thinks fit. The legal authorities also say that where appropriate the court may vary the decision in any way that it thinks necessary, in the light of the evidence before it.

[44] As I have determined that JPSC would have been entitled to some measure of damages under the Agreement, the liquidators will be required to undertake a further assessment in lieu of the Court, to receive further evidence of proof of JPSC actual debt. To facilitate this process the joint liquidators will be required to re-open their assessment of the Proof of Debt, to receive further evidence from JPSC on the actual loss suffered on account of breach of the Agreement, which would qualify as its just and true debt in the liquidation. For this purpose the Notice of Dis-Allowance will be suspended for the duration of the assessment. However, if JPSC fails to provide such evidence within the time stipulated at paragraph 45 (1) below, then the Notice of Dis-Allowance shall stand as affirmed from the date of issue.

[45] Conversely, once the evidence is provided, and the joint liquidators have conducted the assessment and arrived at an amount which is justly and truly due, the outcome of that assessment and the sum assessed as due to JPSC will stand, and the Notice of Dis-Allowance will fall away.

[46] In light of the foregoing, I make the following orders:

1. Unless the applicant, JP Service Corporation LLC provides the joint liquidators of Harlequin Boutique Hotel Limited with evidence and documentation in support of its actual debt within 60 days hereof for determination of the amount truly and justly due to JPSC, the Notice of Disallowance of Claim dated 28th January 2022, shall be affirmed.
2. Costs on this application is awarded to the joint liquidators of Harlequin Boutique Hotel (in liquidation) to be assessed, if not agreed within 21 days.

Cadie St Rose-Albertini
High Court Judge

By the Court

[SEAL]

Registrar