IN THE SUPREME COURT OF BERMUDA

COMMERCIAL COURT

2006: No. 158

BETWEEN:

MILAGROS A. GONZALES ZEVALLOS
AND
SARA M. GONZALES ZEVALLOS
Plaintiffs

-and-

SUN LIFE FINANCIAL SERVICES LTD.
Defendant

RULING

Date of hearing: September 26, 2006, March 13, 2007
Date of Ruling: March 23, 2007

Mr. Jai Pachai, Wakefield Quin, for the Plaintiffs
Mr. Michael Fahy, Appleby Hunter Bailhache, for the Defendant

Introductory

1. By Specially Indorsed Writ dated May 23, 2006, and issued two days later, the Plaintiffs claimed repayment of the balance of their investment account, net of the withdrawal fee, having placed a fixed-term deposit with the Defendant in the amount of $100,000, in or about 2003.

2. It is agreed that, as is alleged in the Statement of Claim, the Plaintiffs completed a withdrawal of deposit form on August 25, 2005, and directed the Defendant to transfer the funds to a specific account in the name of the 2nd Plaintiff at a bank in Peru. In breach of these instructions, the monies were transmitted in the joint names of the Plaintiffs, and were blocked in the United States because the 1st Plaintiff's name is on a "court blocking list".

3. By Summons dated July 3, 2006, the Plaintiffs applied for summary judgment under Order 14 of this Court's Rules. When the hearing commenced, it was clear that there was some uncertainty as to the nature of the Plaintiff's claim. Mr. Pachai indicated that the claim was in contract, not in tort. It was conceded that a breach of contract had occurred, but Mr. Fahy did not concede that the Plaintiffs were entitled to succeed nevertheless.

4. The Court, having regard to the unchallenged evidence adduced by the Defendant to the effect that the 1st Plaintiff was on a "Drug Kingpin" list in the United States

queried whether an illegality defence might arise, and the Defendant's Counsel sought an adjournment to consider this issue. This application was granted on September 26, 2006.

5. At the resumed hearing, Mr. Pachai relied on authorities supporting the case that the Plaintiff's claim was for the recovery of a debt, not damages for breach of contract. Mr. Fahy, unsurprisingly in light of the position adopted by the Plaintiffs' Counsel at the last hearing, argued primarily that triable defences to a claim for damages for breach of contract existed. In addition, it was contended (without reference to a draft pleading) that an arguable defence of illegality could be advanced.

6. By the end of the resumed hearing, it was reasonably clear that the Plaintiffs' application for summary judgment essentially turned on whether or not the claim was properly to be characterised as a claim for the recovery of debt, in which case the defences of no foreseeable loss, and failure to mitigate, would have no application.

7. There was plenty of room for suspicion about the legitimacy of the source of the deposit having regard to the benefit of hindsight (the 1st Plaintiff was only placed on the Drug Kingpin List after the deposit was placed). But no evidence was placed before the Court which indicated that the Defendant could plead a viable defence based on illegality.

The Legal Nature of the Plaintiff's claim

8. The Plaintiffs case is that (a) they placed $100,000 on fixed deposit with the Defendant for six years in or about 2003, (b) that they completed a withdrawal request form and forwarded wire instructions to the Defendant, which instructions were not complied with in breach of the agreement between the parties, and (c) that they have not received the return of "*their money*". The prayer at the end of the Specially Indorsed Writ does not claim damages for breach of contract, but "*(i) the balance of their investment account less the withdrawal fees charged by the Defendant…*"

9. Mr. Pachai's off-the–cuff suggestion at the September hearing, in refuting the suggestion that the claim was a tortious claim, that the claim was a contractual one cannot alter the true legal character of the claim as pleaded. A breach of contract is relied upon, and the claim is contractual in the sense that it arises out of a contractual relationship, but the relief sought is the return of a specific sum, not damages for breach of contract. And the law treats these as legally distinct claims. The Defendant's Counsel relied on the following passage from '*Halsbury's Laws*' 4th Edition Reissue, Volume 9(1) at paragraph 942:

> "*Whilst both may arise out of a contract, a clear distinction must be drawn between: (1) a debt; and (2) damages. An action in debt lies upon a primary obligation to pay a definite sum of money fixed and made payable by the contract on the happening of some event; whereas a claim for damages for breach of contract is a secondary obligation arising from breach of any other primary obligation of performance. A claim for debt may be maintained upon the happening of that event regardless of loss, whereas a claim for more than nominal damages requires proof of loss and is subject to a number of restrictions…*"

10. The relationship between a banker and a customer with respect to monies placed by the customer into an account in the customer's name with the bank is the quintessential "debtor and creditor" relationship. The draft Defence admits that (a) that $100,000 was placed on deposit with the Defendant, (b) in August 2005 the Plaintiffs said they wished to close the account and forwarded wire transfer instructions, and (c) that in attempting to return the Plaintiffs' money, their wire transfer instructions were not complied with. No triable issue has been raised in relation to the existence of a primary contractual obligation on the Defendant's

part to return the proceeds of the Plaintiffs' investment account to them in accordance with their instructions. Accordingly, although this conclusion is only apparent after careful analysis, it is unarguably clear that the Plaintiffs' claim is in debt, and is not a claim for damages for breach of contract.

Are there any triable issues raised by the draft Defence?

11. The consequences of the conclusion that the Plaintiffs' claim is in debt are plain, having regard to Mr. Pachai's authorities[1], and also the following dictum of Millett LJ (as he then was) in Jarvis-v-Harris [1996] Ch 195[2]:

> "*The law of contract draws a clear distinction between a claim for payment of a debt and a claim for damages for breach of contract. The distinction and its consequences are set out in* Chitty on Contracts, *27th ed. (1994), vol. 1, p. 1046, para. 21-031. As there stated, a debt is a definite sum of money fixed by the agreement of the parties as payable by one party to the other in return for the performance of a specified obligation by the other party or on the occurrence of some specified event or condition; whereas damages may be claimed from a party who has broken his primary contractual obligation in some way other than by failure to pay such a debt.*
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> *The plaintiff who claims payment of a debt need not prove anything beyond the occurrence of the event or condition on the occurrence of which the debt became due. He need prove no loss; the rules as to remoteness of damage and mitigation of loss are irrelevant; and unless the event on which the payment is due is a breach of some other contractual obligation owed by the one party to the other the law on penalties does not apply to the agreed sum. It is not necessary that the amount of the debt should be ascertained at the date of the contract; it is sufficient if it is ascertainable when payment is due…*"

12. The overpowering logic of this legal reasoning becomes obvious when one steps back from the somewhat unusual facts of this case. Credit is a cornerstone of the free enterprise system, and is extended on the basis that the legal mechanisms for recovering debts will be swift and true. A bank or other entity that has lent money to a customer would hardly expect to be denied repayment because the customer's wallet containing the cash intended to be used to repay the loan was unexpectedly stolen while the customer was on the way to the Bank.

13. It was not disputed in the present case that the "*general rule is that a party to a contract must perform exactly what he undertook to do*"[3], and so the Defendant could not advance a defence of having performed the contract. If the instructions had been complied with, there is no identifiable reason as to why the 2nd Plaintiff should not have received the funds. The only defences set out in the draft Defence were twofold: (a) no loss had been suffered, so no cause of action arose, and (b) in any event, the consequence of any breach of contract was not foreseeable, so the Defendant was not liable for any loss. These defences are, for the above reasons, not viable in answer to a claim in debt. It remains to consider the oral submission that (a) a duty to mitigate still exists, and (b) that an arguable illegality defence exists.

14. Mr. Fay submitted that *Chitty on Contracts*, paragraph 21-040, on which Mr. Pachai relied, left open the possibility that mitigation of damage applied to a claim in debt in stating that "*the claimant's duty to mitigate his loss does not generally apply.*" Mr. Pachai submitted that in paragraph 26-107, Chitty states

[1] *Chitty on Contracts'*, 29th Edition Volume 1, paragraph 21-040.
[2] At 202H-203A.
[3] *Chitty on Contracts,* paragraph 21-001.

more unequivocally that "*the House of Lords has decided that the rules on mitigation do not apply to a claim for a debt due under a contract*". Both Counsel agreed that the case in question, *White and Carter (Councils) Ltd.-v- McGregor* [1962] A.C. 413, was difficult to interpret in this regard. A far clearer and more modern treatment of the law on this topic, which confirms the accuracy of the law as stated by *Chitty*, merits extensive reproduction. The passage appears in the Judgment of Hirst LJ in *Royscot Commercial Leasing Ltd-v- Ismail*, Court of Appeal Civil Division, Judgment dated April 29, 1993 (unreported), and states as follows:

> "*Mr McGuire, on behalf of the plaintiffs, first approached the case on the issue of principle, without recourse to the actual terms of the indemnity or of the lease agreement. He submitted that a claim under a contract of indemnity, such as this, is not a claim in damages at all, but is a claim in debt for a specified sum due on the happening of an event which has occurred. Accordingly, it should not be open to a person providing an indemnity to challenge his obligation to pay under the contract of indemnity by reference to principles relating to the assessment of damages for breach of contract which have no application to debts. Consequently, he submitted that the learned judge was wrong in principle in his approach as set out in the paragraph of his judgment quoted above.*
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> *In my judgment this submission is correct as a matter of law though, for reasons which appear later, I do not think it carries the plaintiff home on the facts of the present case.*
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> *In Scottish Midland Guarantee Trust v Woolley [1964] 144 LJ 272, which was a hire purchase agreement case where the plaintiff's finance company sued the defendant under a guarantee of the hirer's liability, Mr Justice John Stephenson, as he then was, held that the plaintiffs were entitled to the total sum claimed, namely, the unpaid instalments which were due from the hirer and that, since their claim was one in debt and not in damages for breach of contract, the plaintiffs were under no legal obligation to mitigate their loss. This case is cited in the current edition of Professor Goode's text book "Hire Purchase Law and Practice, 2nd Edition, 1970, as authority for the proposition that in such cases: "The principle that a party claiming damages must have taken reasonable steps to mitigate his loss has no application", (page 656).*
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> *I also think Mr McGuire is right in submitting that this approach is fully in line with the leading decision of the House of Lords in White and Carter (Councils) Ltd v McGregor [1962] AC 413, [1961] 3 All ER 1178, where it was held by a majority, Lords Reid, Tucker and Hodson, that where the appellants, who were advertising contractors, had agreed to display advertisements for the respondent's garage for three years, they were entitled to continue the contract notwithstanding a purported cancellation at the outset by the respondents, and that when the latter failed to pay the due instalments the appellants were entitled to rescind the agreement and claim the sum equivalent to the full three years' rental under the agreement pursuant to a clause providing that, in such circumstances, the full amount became immediately due. The minority, Lord Morton of Henryton and Lord Keith of Avonholm dissented on the ground inter alia that the plaintiffs had a duty to mitigate, (PP 433 and 439)*
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> *It is therefore, in my judgment, implicit in the majority decision that the rules of mitigation do not apply to a claim for a debt due under a contract as contrasted with a claim for damages for breach of contract: (see also paragraph 6-049 of Benjamin's Sale of Goods, 4th Edition, 1992, under the heading: "No duty to mitigate where a debt is claimed" for full consideration of this case).*
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> *Mr McGuire very properly drew our attention to the Court of Appeal decision in Goulston Discount Company Ltd v Sims [1967] 111*

Solicitors Journal 670 which might superficially seem to be authority for the opposite proposition. In that case a finance company sued an indemnifier of a hire purchase agreement under a recourse agreement after the hire purchase agreement had been frustrated as a result of the destruction of the vehicle in an accident. The County Court judge reduced the amount of damages claimed by the plaintiffs, based on outstanding instalments, on the ground that they had accepted less than the full amount payable under the vehicle's insurance policy (which had been assigned to them) and also that an allowance for accelerated payment should have been made.

We have obtained the full transcript of the Court of Appeal judgment dated 25th May, 1967.

Lord Denning stated as follows:

"The case turns upon the true interpretation of the printed indemnity form. It is in terms an indemnity: 'We indemnify you against any loss', says the dealer. The word 'indemnify' is the governing word. Under an indemnity a person cannot expect to make a profit. He cannot get any more than his loss. True it is that the word 'loss' is defined as 'the difference between the total amount the hirer would have to pay, less payments received by you'. But if there is any variation between the defined loss and the actual loss, then the finance company can only recover the actual loss. The recourse agreement here is contract to indemnify and the finance company cannot get more than their loss.

"That is how the judge interpreted this document. The finance company ought to give credit for the amount which they ought reasonably to have received on the insurance policy, also for the fact that the payment was accelerated".

Lord Justice Winn stated as follows:

"This is an indemnity contract: 'We agree to indemnify you'. An indemnity, as the dictionary shows, is: 'A security against damage or loss: compensation for loss incurred", and the verb 'indemnify' means 'to protect or secure a person from or against harm or loss or compensate a person for loss'. What the parties to this contract, or one of them, quite plainly meant to produce was the same result as would have been produced, clearly in the use of the English language, by saying: 'We agree to grant you an indemnity as hereinafter defined for the purposes of this contract, ie, amounting to the difference between the total amount the hirer would have had to pay', and so on. But the draftsman of this document failed to define the word 'indemnify'; he gave instead, by error, a definition of the word 'loss', which is defined by the contract as meaning 'the difference between the total amount which the hirer would have paid'. In fact, I think it is perfectly clear that since some eighteen months -- I do not purport to be precise -- of future instalments of interest had not become due at the time when this contract was frustrated by the total destruction of its subject matter in an accident, again on a very rough arithmetical approach, it appears to me £36 of still not-due interest was included in the claim by the finance company".

Lord Justice Danckwerts agreed.

While, at first sight, the closing passage of Lord Denning's judgment might possibly be interpreted as referring to mitigation I am satisfied, considering the case as a whole, and especially in the light of Lord Justice Winn's judgment (which began by agreeing with Lord Denning), that the ratio of the Court of Appeal was as stated in Lord Denning's opening words viz: that the case turned on the true interpretation of the agreement, and that the plaintiffs were entitled to recover the amount, but no more, that was due in accordance with the proper construction of that agreement: and that, since the plaintiffs had been clearly entitled to recover the full amount under the insurance policy, they should be treated as having done so in order to ascertain their true loss and should,

furthermore, make allowance for interest not yet due having regard to the accelerated payment.

It follows that, in my judgment, mitigation as strictly defined does not come into the picture in a claim for debt such as the present, and to that extent, the approach of the learned Judge was wrong."

15. So there is no duty to mitigate which can be invoked against the Plaintiffs, based on the assertion that they should, before asserting a claim against the Defendant, first seek to recover the monies from the US Federal authorities. Nevertheless, the Court in my view retains the discretion, be it on general equitable grounds[4] or under the rule against double recovery, to decline to permit a creditor to insist on full performance from the debtor. Mr. Pachai accepted that it should not be right for his clients to make double recovery, and tendered a signed undertaking by his clients not to seek to recover the US funds, or to turn over to the Defendant any monies received from the US authorities. The Plaintiff's letter undertaking to account to her insurers for recoveries made from the Defendant in respect of medical expenses already paid by her insurers, was recently held to be sufficient to defeat an argument that a portion of a plaintiff's claim was barred by the rule against double recovery, in *Horton –v- Evans* [2007]EWHC (QB) 315[5].

Illegality

16. The only other potential defence positively advanced, but not in the form of a draft pleading, was the illegality argument raised by the Court in September. It was supported by reference to publicly available information which suggests that the Peruvian airline which the 1st Plaintiff deposes to work for, and its senior manager (who shares the same surname as the Plaintiffs), were on the Drug Kingpin List from 2004, and have been the target of criminal investigations and/or proceedings over the last few years. None of this in any way adds to the bare undisputed fact that the 1st Plaintiff is on the List too, and the inference that there is reason to suspect her guilt by association with her employer company (and possibly relatives) which is also on the List.

17. Mr. Fahy contended the Defendant should be given a further opportunity to investigate and formulate a case that the Plaintiff could not recover because performance of the contract was illegal as a matter of US law. The Plaintiffs' summary judgment application was adjourned on September 26, 2006 for this very issue to be explored. In my view, the Defendant has had a reasonable opportunity to attempt to formulate a coherent case on illegality, if one can be pleaded, and no adequate case for further time to do so has been made out.

18. The Court raised the issue because there were grounds for suspicion that (a) the original funds deposited represented the proceeds of crime, and/or (b) the wire transfer instruction requesting the transfer of the money into the sole name of the 2nd Plaintiff, who happened not to be on the Drug Kingpin List, was a deliberate attempt to evade the consequences of the US freezing regime. It seems probable that this Court "*would not enforce any contract the recognition of which might constitute a hostile act against a foreign friendly country*": *Chitty*, paragraph 16-31. This principle is not engaged, there being no tangible suggestion that the funds in question were linked with hostile actions against the US or any other foreign power. There is no suggestion that the contract between the parties was in and of itself contrary to the law of Bermuda or any other friendly nation. Moreover, in looking at whether or not illegal performance of a contract is a bar to enforcement, *Chitty* has commented:

> " *Nor has the fact that strict compliance with the contract would cause a party to perform illegal acts contravening exchange control*

[4] *Clea Shipping Corp-v- Bulk Oil International Ltd., The Alaskan Trader* [1984] 1 All ER 129, cited in *Chitty*, Volume 1, paragraph 26-107 n.572.
[5] Keith J, Judgment dated March 7, 2007, paragraphs 13-17.

> *regulations in the country of his residence, or place of business prevented the English court from upholding the contract and awarding damages in the event of its breach. The explanation of these cases was that performance of the contracts did not "necessarily" involve the doing of an act which was unlawful by the law of the place where it had to be carried out. Difficulties have been encountered in ascertaining whether performance of a contract involves such an illegal act. In making this assessment it was said to be "immaterial whether one party has to equip himself for performance by an illegal act in another country. What matters is whether performance itself necessarily involves such an act."* [6]

19. The high point of the case that the Defendant can presently make is that if the funds are to be remitted to the 2nd Plaintiff through the United States, there may be some yet-to-be defined breach of US law. Seemingly, if the funds were transferred to one or both Plaintiffs via correspondent banks located anywhere other than in the US, no legal questions would arise. The Defendant has placed in evidence '*An overview of the Foreign Narcotics Kingpin designation Act*'[7] It appears that this legislation (a) permits the Executive to designate individuals and entities, whose assets in the US will be frozen, and (b) prohibits "*US persons*" from dealing with the assets of designated persons or entities. It is unclear how, if at all, this legislation would have been infringed if the Defendant had performed the contract in the manner specified by the Plaintiffs.

20. I must bear in mind the need for any allegations of illegality under foreign law to be fully particularized and supported by expert evidence as to foreign law. The costs of fully exploring these issues at trial, in the absence of a straightforward case based on compelling and readily available evidence, would very obviously be disproportionate to the sum in issue.

21. In all the circumstances I decline to further adjourn this matter to allow the Defendant yet a further opportunity to explore a speculative and likely costly defence.

Conclusion

22. The Plaintiffs are accordingly entitled to summary judgment as prayed, together with the costs of the action, save that I make no order as to the costs between September 26, 2006 and March 13, 2007, because these costs were necessitated by the Court's concerns to ensure that no public policy grounds for refusing the Plaintiffs' summary judgment application existed[8].

23. However, in my discretion, I would award interest only from the date of judgment until payment, and not from August 25, 2005 until payment as the Plaintiffs seek. As Chief Justice Ground has observed, the award of interest on a judgment debt under section 10 of the Interest and Credit Charges (Regulation) Act is entirely at the Court's discretion: *Jupiter Asset Management (Bermuda) Ltd.-v- The Asset Management Group Ltd.*

24. In ordinary circumstances, interest would have been awarded from the date of the failure to pay in accordance with the contract until payment. In the present case, it appears that the Defendant has effectively been punished by the loss of the funds transferred to the US for its admitted failure to comply with the Plaintiffs' instructions. This apparent loss has been sustained because, rightly or wrongly, the 1st Plaintiff is a designated person under the US Drug Kingpin legislation. It seems to me to be obvious that the joint accountholders requested the Defendant

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[6] Paragraph 16-031.
[7] 21 U.S.C. #1901-1908, 8 U.S.C. #1182.
[8] Although it seems both sides focused on non-illegality matters at the adjourned hearing, summary judgment would likely have been entered for the Plaintiffs at the September hearing but for the fact that the 1st Plaintiff was admittedly on the Drug Kingpin List.

to transfer the funds into the sole name of the 2nd Plaintiff with a view to avoiding the consequences of this very legislation.

25. The suggestion that the Plaintiffs were unaware of the designation and that the1st Plaintiff (who was earning US$15,000 per month as a Sales Manager) simply had no bank account is a wholly implausible explanation for the request. Income tax returns for the 1st Plaintiff have been filed on oath, exhibited to an Affidavit in which it is expressly or impliedly represented that although the 2nd Plaintiff contributed to the funds, the primary contributor to the funds placed with the Defendant was the 1st Plaintiff. In my view, it was open to the Plaintiffs to avoid the delay which has occurred by apprising the Defendant of the true position by making full and frank disclosure of the concerns which they must have had. The Plaintiffs ought to have sought to negotiate a legally acceptable way of procuring the return of the funds, and if they had apprised the Defendant of the legally and commercially significant reasons why they should not transfer the funds in joint names, it is inconceivable that this would have occurred.

26. Even if these conclusions are not justified, on the Plaintiffs' own case this is not a case where the Defendant has had the use of their money from the date of the breach until judgment. To compel the Defendant to pay interest from the date of their breach of contract in these circumstances would, in my judgment, be manifestly unjust.

27. I will hear Counsel, if necessary, on the terms of the final Order.

Dated this 23rd day of March, 2007

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KAWALEY J.