In The Supreme Court of Bermuda

CIVIL JURISDICTION

2019: No. 167

BETWEEN:

JULIUS SÄMANN LTD.

Plaintiff

-and-

(1) JUST ADD BERMUDA LTD

(2) FAITH BRIDGES

(3) NEIL MONCRIEFF

Defendants

Before: **Hon. Chief Justice Hargun**

Appearances: **Mr Kevin Taylor, Walkers (Bermuda) Limited, for the Plaintiff**
Mr Paul Harshaw, Canterbury Law Limited, for the 2nd Defendant

Date of Hearing: **25 November 2019**

Date of Judgment: **28 November 2019**

JUDGMENT

Application for summary judgment; meaning of Federal Reserve Prime Rate intended by the parties; whether part of the loan unenforceable as it was allegedly not supported by consideration; whether the allegation of illegality afforded a defence

Introduction

1. These proceedings relate to a Loan Agreement dated 17 December 2014 between Julius Sämann Ltd, ("the Plaintiff"), on the one part and Just Add Bermuda Limited, the First Defendant, Faith Bridges, the Second Defendant and Neil Moncrieff, the Third Defendant (collectively "the Defendants"). By that Loan Agreement the Plaintiff agreed to lend to the Defendants the aggregate principal sum of US dollar $1,400,000.

2. The relevant terms of the Loan Agreement provided, *inter alia*, as follows:

    (i) "1. The draw-down of funds shall be made at such time and in such increments (but not being less than US $100,000 as [the First Defendant] *shall require until the total of US $1,400,000 shall have been advanced".*

    (ii) "5. All parties listed under the definition of JAB hereinabove (i.e. the First, Second and Third Defendants) *shall jointly and severally be liable for the Loan, the accrued interest, and any fees or penalties hereunder…"*

    (iii)"6. JAB hereby agrees to deposit the title deeds to the Property with JSL [the Plaintiff] and to execute at its own cost (whenever called upon to do so) a proper Equitable Mortgage of said Property to JSL to secure any and all funds advanced under this Agreement and any and all monies for the time being due or to become due to JSL, on the security hereof, together with interest due thereon in such form and containing such powers and provisions as the Lender may reasonably require including reservation of the right of consolidation of mortgages and including provisions for repayment of the sums advanced hereunder or to be advanced hereunder"

(iv) *"7. The interest rate under this Agreement shall be set annually on the first day of each calendar year for all funds due and owing as of that date under this Agreement, including accrued but unpaid interest from the previous calendar year (if any), and for any additional draw down of funds during the calendar year. The interest rate for each calendar year shall be determined as the United States Federal Reserve Prime Rate on the first day of relevant Calendar year plus one percent (1%)."*

(v) *"8. Interest shall accrue from the day of the draw down payment is affected by JSL's bank, irrespective of when the funds are credited to JAB."*

(vi) *"9. Interest Payments on the outstanding balance of the Loan shall be due on the last day of each calendar year, with the first payment due on or before the 31st day of December, 2015".*

3. In accordance with the Loan Agreement, the Plaintiff made the following principal advances to the Defendants:

   (i) The sum of US $700,000 on 19 December 2014;
   (ii) The sum of US $1,700,000 on 27 January 2015; and
   (iii) The sum of US $150,000 on 11 May 2015.

4. For each of the payments made as set out above, the Defendants executed a written acknowledgement of receipt.

5. On 17 February 2016, the Plaintiff and Defendants agreed a written Addendum to the Loan Agreement whereby the Plaintiff agreed to lend to the Defendants further US $300,000 which was to be treated as an addition to the Loan. The Plaintiff advanced the additional US $300,000, as agreed in the Addendum, in January 2016 and the Addendum was executed on 17 February 2016.

6. The Third Affidavit of the Plaintiff deposes to the fact that the entirety of the amount of US $2,850,000 advanced remains outstanding and as at 1 July 2019 the accrued interest stands at US $255,987.17. Judgment in default has been entered against the First and Third Defendants for the principal amount outstanding together with interest calculated to the date of judgment.

The application against the Second Defendant

7. By Summons dated 15 July 2019, the Plaintiff seeks an order that paragraphs 8, 9, 10, 14, 19, 20 and 21 of the Defence of the Second Defendant be struck out pursuant to RSC 18, the rules 19(1)(a) and (b) and/or under the inherent jurisdiction of the Court. The Plaintiff seeks summary judgment to be entered in its favour for the principal amount outstanding together with accrued interest.

8. In her Defence, the Second Defendant raises two points for the purposes of this application. First, by paragraph 8, the Second Defendant refers to clause 7 of the Agreement providing that the "*interest rate for each calendar year shall be determined as the United States Federal Reserve Prime Rate on the first day of the relevant calendar year plus one percent (1%)*" and asserts that the United States Federal Reserve Bank does not determine the "Prime Rate", and therefore the mechanism chosen for determination of the interest rate is incapable of performing the function ascribed to it.

9. Second, by paragraph 14 of the Defence, the Second Defendant asserts that the document headed "Addendum to the Loan Agreement" and dated 17 February 2016 is not supported by consideration and therefore is not a contract on which the Plaintiff can sue the Second Defendant.

10. At the hearing of this application on 25 November 2019 counsel for the Second Defendant, Mr Harshaw, opened his response to this application by advancing an argument that the entire Loan Agreement was tainted with illegality and losses lie where they fall with the result that the Second Defendant was not liable to pay anything to the Plaintiff. Mr Harshaw pursued this argument despite the fact that

it was not hinted upon in the Defence which he prepared on behalf of the Second Defendant dated 5 June 2019 or in the Skeleton Argument which he prepared for the Second Defendant for this hearing dated 19 November 2019.

Meaning of United States Federal Reserve Prime Rate

11. Lord Hoffmann, in his seminal speech in *I.C.S. Ltd. v West Bromwich Building Society* [1998] 1 WLR 896 said at 913C:

> *"(4)The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax. (see Mannai Investments Co. Ltd. v. Eagle Star Life Assurance Co. Ltd. [1997] 2 WLR 945"*

12. As the Federal Reserve website states the Federal Reserve has no direct role in setting the Prime Rate but many banks choose to set their prime rates based partly on the Target Level of the Federal Funds Rate, the rate that the banks charge each other for short-term loans established by the Federal Open Market Committee. The prime rate is an interest rate determined by individual banks and is often used as a reference rate (also called the base rate) for many types of loan, including loans to small businesses and credit card loans. In the context of the United States banking system, no one can have any serious doubt as to what is meant by the United States Prime Rate. It seems clear beyond any real doubt that when the parties referred to the United States Federal Reserve Prime Rate in clause 7 of the Loan Agreement they were referring to the United States Prime Rate and that is

the rate which has been used for the purposes of calculating the accrued interest under the Loan Agreement.

The issue of the Addendum and past consideration

13. The Second Defendant argues that the document headed "Addendum to Loan Agreement" dated 17 February 2016 is not supported by consideration given that the payment made by the Plaintiff of US $300,000 took place in January 2016 and therefore before the Addendum was executed.

14. In my judgment this point advanced by Mr Harshaw is entirely without merit. No authority was cited in support of this contention. Paragraph 4.027 of Chitty on Contracts, Volume 1, 33rd edition, states:

> *"In determining whether consideration is past, the courts are not, it is submitted, bound to apply a strictly chronological test. If the giving of the consideration and making of the promise are substantially one transaction, the exact order in which these events occur is not decisive (Thornton v Jenkyns (1840) 1 M.&G. 166; Tanner v Moore (1846) 9 QB 1; Lictor Anstalt v MIR Steel UK Ltd [2015] EWHC 3316 (Ch) at [223] ("whole matter can be construed as a single transaction")."*

15. It is beyond any sensible argument that the payment of US $300,000 in January 2016 and the execution of the Addendum on 17 February 2016 was one transaction and accordingly it cannot be said that there was no valuable consideration for the Addendum.

16. Furthermore, the Addendum dated 17 February 2016 expressly refers to the Loan Agreement between the Plaintiff and the Defendants and the payment of US $300,000 is being described as an "*Additional payment"* under the Loan Agreement. The Loan Agreement is an agreement under seal and does not require that it be supported by consideration.

The alleged illegality and its consequences

17. As noted earlier, Mr Harshaw's main point as to why summary judgment should be refused was that the Loan Agreement was an illegal scheme and as such this court should not give any assistance in its enforcement.

18. The starting point of this argument was reliance upon clause 6 of the Loan Agreement which provided that the Defendants agreed to deposit the title deeds to the property with the Plaintiff and execute (whenever called upon to do so) the proper Equitable Mortgage of the said property to the Plaintiff to secure any and all funds advanced.

19. Mr Harshaw then referred to the Bermuda Immigration and Protection Act 1956. Under the 1956 Act exempted companies such as the Plaintiff are defined as "restricted persons". Section 78(1) provides that no restricted person shall appropriate land in Bermuda with the intention of occupying it, or of using it or developing the land for profit at any time whether for his own benefit or for the benefit of another person. Section 80 provides that no restricted person shall, without the prior approval of the Minister of Finance, accept or take, directly or indirectly, any mortgage or charge on land in Bermuda, whether legal or equitable. Mr Harshaw then referred us to *Irish Land Law*, Prof J.C.W. Wylie, 4th edition, in support of the proposition that the deposit of title deeds will be regarded as *prima facie* evidence of an equitable mortgage, unless the deposit is otherwise accounted for. Mr Harshaw contended that as title deeds had been delivered to the Plaintiff that amounted to an attempt to acquire an equitable mortgage and as a result the entire scheme was illegal including the underlying loan transaction.

20. Mr Harshaw referred the Court to the celebrated passage in the judgment of Lord Mansfield CJ in *Holman v Johnson* (1775) 1 COWP 342:

> *"If, from the plaintiff's own stating or otherwise, the cause of action appears to arise ex turpi causa, or the transgression of a positive law of this country, there the court says he has no right to be assisted. It is upon that ground the court goes; not for the sake of the defendant, but because they will not lend their aid to such a plaintiff. So if the plaintiff and defendant were to change sides, and the defendant was to bring his action against the plaintiff, the latter would then have the advantage of it; for where both are equally in fault, potior est conditio defendentis."*

21. Relying upon *Holman v Johnson,* Mr Harshaw argued that this Court should not assist the Plaintiff in the enforcement of the Loan Agreement which was infected with illegality. He argued that it necessarily followed that no judgment for any amount could be given in favour of the Plaintiff and against the Second Defendant.

22. As stated earlier this illegality point was not hinted upon in the Defence of the Second Defendant dated 5 June 2019. No mention of the illegality point was made in the written submissions prepared by Mr Harshaw and dated 19 November 2019, four days before the hearing. The illegality point was first raised by Mr Harshaw when he commenced his oral submissions. As I pointed out to Mr Harshaw this was a completely unacceptable way of conducting litigation. In any event if a fundamental point such as illegality is to be taken by a party it is the duty of counsel to ensure that the Court is provided with all relevant authority so that it can properly determine the validity of the contention. In this regard it is to be noted that counsel failed to provide two relevant authorities of the Supreme Court of Bermuda on the very point and a 2016 decision of the United Kingdom Supreme Court which reviewed the consequences of illegality on the parties' rights under their contracts. The Bermuda decisions are *Lydia Caletti v Ralph DeSilva* [2017] Bda LR 102 and *E&C Well Drilling Services Ltd v Vera Marie*

Hayward [2011] SC (Bda) 1 Civ (13 January 2011) and the UK Supreme Court decision is *Patel v Mirza* [2016] UKSC 42.

23. *Caletti v Ralph DeSilva* dealt with a materially identical issue. In that case a restricted person had lent monies and had sought to obtain security by way of mortgage of certain residential properties owned by the borrower. The borrower argued that this arrangement was in breach of section 80(1) of the 1956 Act. Counsel for the borrower argued, just as Mr Harshaw in the present case, that the obtaining of the mortgage was sufficient to render the entire promissory note illegal and therefore, as a matter of law, unenforceable. Counsel for the borrower relied upon, just as Mr Harshaw, in this case on the passage in the judgment of Lord Mansfield CJ in *Holman v Johnson*. Hellman J reviewed the legal position in light of the decision of the United Kingdom Supreme Court in *Patel v Mirza* and concluded that any alleged illegality did not affect the underlying obligation of the borrower to pay under the promissory note. The learned judge's reasoning appears as follows:

> *"38. Mr Scott relied upon the oft quoted dictum of Lord Mansfield CJ in Holman v Johnson 1 Cowp 341 at 343 that: "No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act". The principle that a court will not enforce an illegal 40 contract is expressed by the Latin maxim: "ex turpi causa non oritur actio"1. The explication of that principle has proven, in the words of Sir Robin Jacob in ParkingEye Ltd v Somerfield Stores Ltd [2013] QB 840 at para 28: "notoriously knotty territory". However, the House of Lords and UK Supreme Court consistently held that its application was a rule of law and not a matter of discretion. As Lord Sumption JSC, giving the judgment of the plurality, stated in Les Laboratoires Servier v Apotex Inc [2015] AC 430 SC(E) at para 23: "The ex turpi causa principle precludes the judge from performing his ordinary adjudicative function in a case where that would lend the authority of the state to the enforcement of an illegal transaction or to the determination of the legal consequences of an illegal act."*

1 Translated by Jowitt's Dictionary of English Law, 4th ed, 2015, as: "no disgraceful matter can ground an action", and by Osborn's Concise Law Dictionary, 12th ed 2013, as: "an action does not arise from a base cause".

39. That changed with Patel v Mirza [2017] AC 467 UKSC. As summarised in the headnote to the report, the claimant paid a large sum of money to the defendant pursuant to an agreement that he would use it to bet on the movement of shares on the basis of inside information. The agreement contravened the prohibition on insider dealing in section 52 of the Criminal Justice Act 1993. The agreement could not be carried out because the expected insider information was not forthcoming. The claimant sued the defendant for recovery of his money. He failed at first instance but succeeded both in the Court of Appeal and before a nine judge panel of the UK Supreme Court. Although the Supreme Court decided the case on the basis of unjust enrichment rather than contract, the justices took the opportunity to examine the common law doctrine of illegality as a defence to a civil claim.

40. The majority, departing from the position taken previously by the House of Lords and the UK Supreme Court, held that when considering a defence of illegality the Court should consider whether on the particular facts of the case public policy required that the claim be disallowed. Lord Toulson JSC, giving judgment for a plurality of five justices, and with whom a sixth agreed, summarised the position at para 120: "The essential rationale of the illegality doctrine is that it would be contrary to the public interest to enforce a claim if to do so would be harmful to the integrity of the legal system (or, possibly, certain aspects of public morality, the boundaries of which have never been made entirely clear and which do not arise for consideration in this case). In assessing whether the public interest would be harmed in that way, it is necessary (a) to consider the underlying purpose of the prohibition which has been transgressed and whether that purpose will be enhanced by denial of the claim, (b) to

consider any other relevant public policy on which the denial of the claim may have an impact and (c) to consider whether denial of the claim would be a proportionate response to the illegality, bearing in mind that punishment is a matter for the criminal courts. Within that framework, various factors may be relevant, but it would be a mistake to suggest that the court is free to decide a case in an undisciplined way. The public interest is best served by a principled and transparent assessment of the considerations identified, rather by than the application of a formal approach capable of producing results which may appear arbitrary, unjust or disproportionate."

41. In the present case, the underlying purpose of the prohibition which has been transgressed is the policy summarised in the heading of Part VI of the 1956 Act as "Protecting Land in Bermuda for Bermudians". Another relevant public policy on which the denial of the claim may have an impact is that where a lender contracts with a borrower to lend money then, absent illegality, the courts will enforce the terms of the contract. In the present case, the illegality does not lie in the terms of the Promissory Note. It was not illegal for Mr Caletti to lend Mr DeSilva $3 million. Neither was it illegal for him to charge a rate of interest higher than the judgment debt rate: a point I will deal with further below. Nor was it illegal for the parties to the Promissory Note to execute a valid legal mortgage, ie having first obtained the prior approval of the Minister. The illegality complained of is the manner in which Mr Caletti sought to enforce payment of the judgment debt, ie that he and Mr DeSilva executed mortgages over Mr DeSilva's properties without first obtaining ministerial approval.

42. In my judgment, denial of Mr Caletti's claim would not be a proportionate response to this illegality. The illegality relates not to the terms of the Promissory Note, none of which are illegal on their face, but the manner in which it was sought to enforce them. Even if the term requiring Mr DeSilva to execute a valid legal mortgage over his

properties was illegal, which it was not, it was severable from the obligation to repay the loan monies. As Ground CJ stated in E&C Well Drilling Services Ltd v Hayward [2011] Bda LR 1 at para 17: "The personal obligation to pay is severable from the security, and survives it". Thus, the personal obligation to pay, which is unobjectionable, would remain if para 4 of the Promissory Note, which deals with enforcement, was struck out altogether. The upshot is that illegality provides no basis for the Court to set aside the Consent Judgment."

24. The majority in the Supreme Court (Lord Toulson, Lady Hale, Lord Kerr, Lord Wilson and Lord Hodge) in *Patel v Mirza* expressly stated that *Holman v Johnson* can no longer be prayed in aid of results which are entirely arbitrary as between the contracting parties:

> *"91. Fifth, although Lord Mansfield made it clear in Holman v Johnson that the illegality defence operates as a rule of public policy and is not designed to achieve justice between the parties, that does not mean that any result, however arbitrary, is acceptable. The law should strive for the most desirable policy outcome, and it may be that it is best achieved by taking into account a range of factors."*

25. In relation to the illegality point, it is to be noted that the relevant clause in the Loan Agreement expressly obliges the Defendants to execute "a proper Equitable Mortgage", the implication being that no equitable interest has been acquired by the Plaintiff. No doubt if such an interest was to be acquired, the appropriate consent from the Minister of Finance would be sought and obtained.

26. In any event based upon the reasoning in *Caletti v Ralph DeSilva*; *E&C Well Drilling Services Ltd v Vera Marie Hayward* and *Patel v Mizra* (set out in paragraphs 23-24 above) I am satisfied that, even if there was a breach of section 80 of the 1956 Act, there is no arguable case that the underlying primary obligation of the Second Defendant to pay in accordance with the Loan Agreement falls away. In my judgment, even assuming such illegality, the Second

Defendant continues to be contractually obliged to repay the loans in accordance with the Loan Agreement and public policy does not prevent this court from ordering that she does so.

27. In coming to this conclusion, I have borne in mind the authorities cited by Mr Harshaw in relation to the practice relating to order 14 and in particular the passages in the 1999 Supreme Court Practice at paragraphs 14/4/2; 14/4/3; 14/4/9 and 14/4/11. I have also borne in mind the authorities cited by Mr Taylor in relation to striking out parts of the pleadings and the grant of summary judgment. I have in mind the Court of Appeal decision in *Broadsino Finance Company Limited v Brilliance China Automotive Holdings Ltd* [2005] Bda LR 12 and *Lecolia Caines v Shannon v Caines* [2017] SC (Bda) 22 Civ (16 March 2017).

Conclusion

28. In the circumstances, judgment is entered against the Second Defendant in the principal amount of US $2,850,000 and interest calculated up to 1 July 2019 in the amount of US $255,987.17. Counsel has advised that accrued interest up to 28 November 2019 is $333,349.42. Accordingly judgment is entered in the principal amount of US $2,850,000 together with interest accrued thereon in the amount of $333,349.42.

29. I shall hear the parties in relation to the issue of costs, if required.

Dated this 28 November 2019

NARINDER K HARGUN
CHIEF JUSTICE