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1. *EURO-DIAM LTD. v. BATHURST [1987] 2 WLR 1368, [1987] 2 WLR 1368*

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EURO-DIAM LTD. v. BATHURST [1987] 2 WLR 1368

[1984 E. No. 1273]

[QUEEN'S BENCH DIVISION]

Staughton J.

1986 July 14, 15, 16, 17, 21, 22Oct. 1

Insurance — Indemnity insurance — Enforceability of claim — Company exporting precious stones to wholesalers abroad — Value of consignment falsely invoiced — Breach of foreign country's revenue laws — Theft from importers' premises — Whether claim tainted with illegality — Whether enforceable — Whether contrary to public policy to enforce

Insurance — Contract — Implied term — Indemnity policy for loss by theft in respect of export of precious stones — Breach of foreign country's revenue laws by false invoicing — Whether term to be implied that venture to be carried out lawfully — Whether extending to compliance with foreign law

The plaintiffs, a United Kingdom company supplying precious stones including diamonds to wholesalers at home and abroad, entered into a contract of indemnity insurance with, inter alia, the defendant for one year from September 1981 in respect of the export of consignments of precious stones. In May 1982 certain of the plaintiffs' diamonds exported to West Germany were stolen from a German company's warehouse. The diamonds were part of two consignments negotiated by B., an Israeli citizen engaged in business in contravention of West German immigration laws, and addressed to the German company. The plaintiffs brought an action for U.S.$142173 against the defendant, as a representative insurer, claiming to be indemnified for the loss under the contract of insurance. The defendant denied liability, claiming that the plaintiffs had misrepresented the value of the second consignment of diamonds on the invoice sent to the German company so as to enable that company to evade West German import tax law, and that the plaintiffs were in breach of an implied term to carry out the adventure in a lawful manner and their claim was tainted with illegality.

On the plaintiffs' action: —

Held , giving judgment for the plaintiffs, (1) that, since the contract of insurance was a non-marine policy on the goods and not on any adventure connected with the goods, there could be no implied term that the performance of the contract would be carried out in a lawful manner (post, p. *1378A–B*, *C*, *1379F*).

Moore v. Evans [1918] A.C. 185, H.L.(E.) applied.

(2) That a claim could be said to be tainted with illegality, and unenforceable, in English law if the plaintiff needed to plead or prove illegal conduct in order to establish his claim, or if the claim was so closely connected with the proceeds of crime as to offend the conscience of the court; but that, on the facts, the plaintiffs did not need to plead, prove or show any of the illegal acts, their title to the goods was not in any way affected by illegality and public policy did not require the plaintiffs to be deprived of their claim; that, accordingly, the claim was not tainted with illegality; that, further, for an English claim to be unenforceable as being tainted by foreign illegality the transaction from which the taint was said to arise had to be unenforceable in England and sufficiently connected with the claim to amount to a taint; and that, as there was insufficient connection between ***[*1369]***

the activities which were illegal under German law and the insurance claim, the plaintiffs' claim was not unenforceable (post, pp. *1384B–F*, *1387F–G*, *1388D–E*, *1389C–D*).

Beresford v. Royal Insurance Co. Ltd. [1938] A.C. 586, H.L.(E.); *Bowmakers Ltd. v. Barnet Instruments Ltd.* [1945] K.B. 65, C.A.; *In re Emery's Investments Trusts* [1959] Ch. 410; *Mackender v. Feldia AG* [1967] 2 Q.B. 590, C.A. and *United City Merchants (Investments) Ltd. v. Royal Bank of Canada* [1983] 1 A.C. 168, H.L.(E.) considered.

Geismar v. Sun Alliance and London Insurance Ltd. [1978] Q.B. 383distinguished.

Per curiam. If it had been an implied term of the contract of insurance that performance was to be in a lawful manner, there would have been considerable doubt as to whether it extended to compliance with foreign law as well as English (post, p. *1379E*).

The following cases are referred to in the judgment:

Attorney-General of New Zealand v. Ortiz [1984] A.C. 1; [1983] 2 W.L.R. 809; [1983] 2 All E.R. 93, H.L.(E.)

Bamburi, The [1982] 1 Lloyd's Rep. 312

Belvoir Finance Co. Ltd. v. Stapleton [1971] 1 Q.B. 210; [1970] 3 W.L.R. 530; [1970] 3 All E.R. 664, C.A.

Beresford v. Royal Insurance Co. Ltd. [1938] A.C. 586; [1938] 2 All E.R. 602, H.L.(E.)

Bird v. Appleton (1800) 8 Durn. & E. 562

Bowmakers Ltd. v. Barnet Instruments Ltd. [1945] K.B. 65; [1944] 2 All E.R. 579, C.A.

Brown v. New Jersey Insurance Co. (1932) 14 P.(2d) 272

Cleaver v. Mutual Reserve Fund Life Association [1892] 1 Q.B. 147, C.A.

Direct Cosmetics Ltd. v. Customs and Excise Commissioners (Case 5/84) [1985] 2 CML.R. 145, E.C.J.

Emery's Investments Trusts, In re [1959] Ch. 410; [1959] 2 W.L.R. 461; [1959] 1 All E.R. 577

Geismar v. Sun Alliance and London Insurance Ltd. [1978] Q.B. 383; [1978] 3 W.L.R. 38; [1977] 3 All E.R. 570

Gordon v. Chief Commissioner of Metropolitan Police [1910] 2 K.B. 1080, C.A.

Hornal v. Neuberger Products Ltd. [1957] 1 Q.B. 247; [1956] 3 W.L.R. 1034; [1956] 3 All E.R. 970, C.A.

Mackender v. Feldia AG [1967] 2 Q.B. 590; [1967] 2 W.L.R. 119; [1966] 3 All E.R. 847, C.A.

Marles v. Philip Trant & Sons Ltd. [1954] 1 Q.B. 29; [1953] 2 W.L.R. 564; [1953] 1 All E.R. 651, C.A.

Moore v. Evans [1917] 1 K.B. 458, C.A.; [1918] A.C. 185, H.L.(E.)

Palaniappa Chettiar v. Arunasalam Chettiar [1962] A.C. 294; [1962] 2 W.L.R. 548; [1962] 1 All E.R. 494, P.C.

Parkin v. Dick (1809) 11 East 502

Planche v. Fletcher (1779) 1 Doug. 251

Pye Ltd. v. B.G. Transport Service Ltd. [1966] 2 Lloyd's Rep. 300

Ralli Brothers v. Compania Naviera Sota y Aznar [1920] 2 K.B. 287, C.A.

Regazzoni v. K.C. Sethia (1944) Ltd. [1958] A.C. 301; [1957] 3 W.L.R. 752; [1957] 3 All E.R. 286, H.L.(E.)

St. John Shipping Corporation v. Joseph Rank Ltd. [1957] 1 Q.B. 267; [1956] 3 W.L.R. 870; [1956] 3 All E.R. 683

Singh v. Ali [1960] A.C. 167; [1960] 2 W.L.R. 180; [1960] 1 All E.R. 269, P.C.

Thackwell v. Barclays Bank Plc. [1986] 1 All E.R. 676

Tinker v. Tinker [1970] P. 136; [1970] 2 W.L.R. 331; [1970] 1 All E.R. 540, C.A.

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United City Merchants (Investments) Ltd. v. Royal Bank of Canada [1983] 1 A.C. 168; [1982] 2 W.L.R. 1039; [1982] 2 All E.R. 720, H.L.(E.)

Williams and Humbert Ltd. v. W. & H. Trade Marks (Jersey) Ltd. [1986] A.C. 368; [1986] 2 W.L.R. 24; [1986] 1 All E.R. 129, H.L.(E.)

The following additional cases were cited in argument:

Bodley Head Ltd., (The) v. Flegon [1972] 1 W.L.R. 680

British and Foreign Marine Insurance Co. Ltd. v. Gaunt [1921] 2 A.C. 41, H.L.(E.)

De Borbon v. Westminster Bank Ltd. (1933) 49 T.L.R. 414, C.A.

Dudgeon v. Pembroke (1874) L.R. 9 Q.B. 581, D.C.

Rossano v. Manufacturers' Life Assurance Co. [1963] 2 Q.B. 352; [1962] 3 W.L.R. 157; [1962] 2 All E.R. 214

ACTION

By a specially endorsed writ, dated 11 July 1984, the plaintiffs, Euro-Diam Ltd., claimed against the defendant, Andrew Eric Bathurst, a representative underwriter, to be indemnified, under a contract of insurance by which the defendant, inter alios, agreed to insure the plaintiffs worldwide for a period of 12 months at 20 September 1981 against all risks of physical loss and/or damage in respect of diamonds and other precious stones, against the loss on 14 May 1982 of certain of the plaintiffs' diamonds consigned on a "sale or return" basis to Verena GmbH of Pforzheim, West Germany and/or one Bonim, the insured value of which amounted to U.S.$142173.88. By amended points of defence the defendant denied that the plaintiffs were entitled to the relief claimed and alleged, inter alia, that (1) when the diamonds were consigned to Verena GmbH or Bonim the plaintiffs issued an invoice, dated 2 February 1982, which represented the price and value of the consignment as U.S.$131411 when the true list price of the goods was U.S.$223416, with a view to deceiving the West German customs authorities into charging less import turnover tax than was properly due, and thereby committing a criminal offence under the law of West Germany; (2) Mr. Bonim was an Israeli citizen carrying on business as a self-employed diamond dealer in West Germany where he had resided for approximately three years without the requisite residence permit for a person in business occupation resident for more than three months, and had therefore committed illegal acts in West Germany; (3) the plaintiffs' claims were tainted by their own illegality in consigning the diamonds to Mr. Bonim and/or Verena GmbH with a view to evading import turnover tax and/or by the illegality of their own "on consignment" agent, Mr. Bonim; (4) the plaintiffs were in breach of an implied term of the policy in that they failed (in relation to the invoice) to ensure in so far as they could control the matter, that the adventure was carried out in a lawful manner; and (5) it would be contrary to public policy to permit the plaintiffs to recover under the policy.

The facts are stated in the judgment.

Jeffrey Gruder for the plaintiffs.

Julian Malins for the defendant.

Cur. adv. vult.

1 October. STAUGHTON J. read the following judgment. The plaintiffs ***[*1371]*** in this action are an English company dealing in diamonds which have been cut and polished. They obtain the diamonds from manufacturers, and supply them in the main to wholesalers both in England and abroad. The defendant is sued as a representative underwriter on a contract of insurance in favour of the plaintiffs subscribed on behalf of two syndicates at Lloyd's. I shall call him, perhaps with more sense than syntax, the insurers.

The issues divide under three heads. (A) On the facts, did a loss occur which was covered by the policy, in the amount claimed by the plaintiffs? (B) Did a breach or breaches of the law of the Federal Republic of Germany occur in connection with the diamonds which are said to have been lost? (C) If so, does that afford the insurers a defence to the claim, wholly or in part? There is no general interest in issues (A) and (B), although they are of importance in this particular case. By contrast issue (C) is one of general interest and importance. Before I come to those issues, I must set out some of the terms of the contract of insurance.

The contract

This is contained in a slip which is undated, but may be assumed to have been subscribed at or about the time when the insurance commenced in September 1981. Its terms are as follows:

> "Type: cargo insurance. Assured: L.B.C. Purchasing (Pty) Ltd. &/ or associated and/or subsidiary companies as per schedule. Form: J(A) form. Period: 12 months at 20.9.1981. Conveyances: conveyances &/or registered post &/or registered air mail &/or express air mail &/or courier &/or insured parcel post &/or airfreight (vln. cl. as expiring). Trading: worldwide. Interest: diamonds &/or other precious stones &/or associated interest. The assured's stocks including property for which they are responsible, including returned goods. A. For 'sight' collections by armoured car to, from or between assured's premises &/or banks. B. In transit from time of leaving sender's address until delivered to ultimate consignee (including transhipment where incurred). C. Whilst outside assured's premises anywhere within geographical areas as per schedule. D. Whilst at assured's premises or in bank &/or safe deposits or between. Basis of valuation: Sendings: as per register. In event of loss prior to registration, invoice + 10 per cent. tax if applicable. Other: standard value + 10 per cent. + tax if applicable … Conditions: all risks of physical loss &/or damage excluding loss &/or damage arising from war risks on land but for sendings subject ICC A/R including war, S.R.C.C. as per inst. clauses, including confiscation and expropriation as *per* LOP 325 amended."

The reference to LOP 325 is, it was agreed, in fact intended to and marked in the bottom corner LPO 325. That contains these additional clauses:

> "1. (a) This policy is to cover loss of and/or damage to the property hereby insured directly caused by confiscation, seizure, appropriation, expropriation, requisition for title or use or wilful destruction by/or under the order of the Government (whether civil, military or de *[*1372]* facto and/or public or local authority of the country in which the vessel(s)/craft/property hereby insured are covered by the terms of this policy in respect of transit risks. (b) Nevertheless this policy does not cover any such loss or damage by or under the order of the Government and/or public or local authority of the sender … 3. (a) Warranted that the assured comply in all aspects with the laws (local or otherwise) of any country within whose jurisdiction the property may be. (b) Warranted all permits necessary for legal operation are obtained. Should failure to comply with the above warranties prejudice this insurance to the extent of a loss, no liability shall attach hereunder."

(A) Did a loss occur which was covered by the policy, in the amount claimed by the plaintiffs?

Apart from the expert evidence of German law, there was only one witness of fact — Mr. Laub, the managing director of the plaintiffs. There were three *Civil Evidence Act 1968* statements from Mr. Bonim, an Israeli citizen who was concerned in the import of some diamonds belonging to the plaintiffs into West Germany and their sale there; and another Civil Evidence Act statement from Mr. Badower, an employee of a German company called Verena GmbH ("Verena") who were also concerned in that transaction. I also have an affidavit of a Mr. Greenslade, who was formerly an inspector with the Metropolitan Police and investigated this claim on behalf of the insurers in the course of his employment as a loss adjuster. He was unable to give oral evidence at the trial due to illness, and it was agreed that his affidavit should be read in evidence. But a difficulty arises because a good deal of the affidavit is concerned with statements made to him by other persons. In so far as those statements were made by Mr. Laub (or any other employee of the plaintiffs) they are admissible as admissions. But Mr. Greenslade's evidence of statements made to him by others, such as Mr. Bonim or employees of Verena, is not admissible on that ground; and I did not understand the parties to have agreed that, by admitting Mr. Greenslade's affidavit, they were also content to admit so much of it as was hearsay only. Finally, there were three contemporary documents in respect of which Civil Evidence Act notices had been served.

From that material I find the facts as follows. At some time in 1981 Mr. Bonim was introduced to the plaintiffs by a cousin of Mr. Laub who was connected with a company selling diamonds in Israel. Mr. Laub was told that Mr. Bonim might find the diamonds which the plaintiffs had to sell more suitable. In November 1981 Mr. Bonim came to London. He told Mr. Laub that he required diamonds to be sent to Germany and sold there, for his profit and the profit of his associates. It was agreed that Mr. Laub would state the plaintiffs' minimum selling price for each diamond; if a diamond was sold in Germany that amount would be paid to the plaintiffs; any diamonds unsold would be returned to them.

Mr. Bonim then selected a number of diamonds, weighing 59.87 carats in all. A few he took with him to Germany, but most of the diamonds were sent by registered air mail, addressed to Verena. A list was prepared by the plaintiffs of the number, size, weight and price of the diamonds, also addressed to Verena. And there was an invoice from the plaintiffs to Verena for "polished diamonds, $78279.25" which was the total of the prices stated in the list.

*[*1373]*

Part of that collection was sold in Germany and the minimum selling price paid to the plaintiffs, part was returned to the plaintiffs, and some few stones remained in Germany unsold. Then in January or February 1982 Mr. Bonim came again to London, and a second transaction was concluded with the plaintiffs. It was in most respects similar but in one important respect different. A list was again prepared of the diamonds, weighing 188.85 carats; the prices stated totalled $223416; and the list was addressed to "Bonim." The diamonds were despatched by registered air mail to Verena. But an invoice was prepared stating the price to be $131411.

Why was the invoice price substantially less than the price which the plaintiffs were to receive if the goods were sold in Germany? Mr. Laub's evidence, which I accept, was that it was issued in that way at the request of Mr. Bonim. Mr. Laub according to his own evidence did not go into details as to the reasons for the request; he merely acceded to it, rather foolishly as he now supposes. I accept that evidence also. From Mr. Laub's point of view any invoice could only be provisional, as he did not know how many of the diamonds would be sold in Germany. But it must have been obvious to Mr.

Laub that the purpose of the invoice was to deceive somebody. Indeed, Mr. Laub accepted that in his evidence. In my judgment the obvious candidate was the German customs authorities. Although Mr. Laub was otherwise a most impressive and frank witness, I cannot accept his evidence that there might plausibly have been others whom Verena or Bonim wished to deceive, such as their auditors. He must have realised that in all probability the object was to deceive the German customs.

There was one other respect in which it might perhaps have been argued that the invoice was false: it was addressed to Verena, who were registered for the German equivalent of value added tax, rather than to Mr. Bonim, who was not. But there is no complaint about that in the insurers' points of defence; and as will appear, I do not think that any charge of deliberate falsehood against the plaintiffs on that ground could have been substantiated.

I have no direct evidence as to whether Verena did or did not in fact use the invoice for the purpose of paying the German turnover equalisation tax. Mr. Laub of course did not know. The point does not feature at all in the written evidence of Mr. Bonim and Mr. Badower. On the balance of probabilities, and bearing in mind that Verena in doing so would be guilty of criminal behaviour (see *Hornal v. Neuberger Products Ltd.* [1957] 1 Q.B. 247) I find that they did: they presented the invoice to the German customs authorities as evidence of the value of the diamonds being imported, on which the tax would be calculated. In a criminal case silence is not evidence of guilt; but if tax had in fact been paid on the true value of the diamonds, I would have expected that to be stated somewhere in the evidence.

At the beginning of April 1982 there was a conversation between Mr. Bonim and Mr. Laub. In the course of it Mr. Bonim said that sales were not going well. Mr. Laub replied that the diamonds not sold should be returned, and that the plaintiffs would select more suitable goods. It was agreed that Mr. Bonim would contact Mr. Laub again early in May. On 10 May 1982 Mr. Bonim wrote this letter to the plaintiff on the headed paper of Verena: "Dear Mr. Theo, Hereby we send you seven cheques total amount U.S. $70000, on account of shipment February 1982. Regards, I. Bonim." The seven cheques were ***[*1374]*** drawn by Verena in favour of the plaintiffs; all appear to be post-dated. When later presented they were dishonoured; and Verena went into liquidation.

Meanwhile it is said that a theft occurred. The evidence as to that is in the statement of Mr. Badower. He recounts how a box containing diamonds, itself kept in a black leather case in the office of Verena, disappeared during working hours on 14 May 1982. A number of customers and other people had been in the office during the day. The police were called, people were searched, and other inquiries were made. But the box and the diamonds in it were not found. As to the contents of the box, there is written evidence that Mr. Bonim and Verena were able to reconstruct from their sales invoices and other records which diamonds had previously been sold and which had been stolen. They estimated the total loss at about $500000, and claimed to be able to identify a number of diamonds from the plaintiffs which must have been in the box and therefore stolen. These were for the most part from the February parcel; but a few were diamonds from the November parcel which had neither been sold nor returned to the plaintiffs.

The insurers have legitimate grounds for criticising the evidence as to a loss. For the fact that a theft occurred at all there is only the written evidence of Mr. Badower. As to what was stolen, the plaintiffs could not produce documents showing how the diamonds came into their possession in the first place; and no documents were produced evidencing the resale of any diamonds in Germany. Except for one letter there was no evidence, oral or written, from the principals concerned at Verena. They and Mr. Bonim left for Israel when Verena went into liquidation, shortly after the theft. Nevertheless, I consider that I ought to accept the evidence that a theft occurred, and that among the diamonds stolen were those emanating from the plaintiffs which are set out in a list prepared by Mr. Bonim and Verena. Mr. Greenslade, the loss adjuster, was instructed on 20 May 1982 and went with Mr. Laub to Germany on the following day. If there were solid grounds for suspecting that no theft had occurred, or that the diamonds in the list were not among those stolen, I would have expected his inquiries to reveal that. Furthermore, the somewhat casual manner in which valuable diamonds were cared for, and their history documented, may not be unusual in the trade, although Mr. Greenslade would have expected dealings to be recorded in a notebook. Mr. Malins for the insurers submitted that, on the evidence, there was no more that a possibility that events occurred as the plaintiffs maintained. In my judgment, on the balance of probabilities they did so occur. The value of the diamonds listed as stolen and emanating from the plaintiffs is not in dispute. Under the contract of insurance it was to be the "standard value + 10 per cent.

+ tax if applicable." That comes to $142173.88.

Before leaving the facts it is necessary that I reach a conclusion on two questions. First, what was the nature of the contract between the plaintiffs and Mr. Bonim or Verena? Was it a contract of agency, such that Mr. Bonim or Verena would import the diamonds into Germany and sell them there (if they could) on behalf of the plaintiffs? Or were they acting as principals, and were the diamonds sent to them on sale or return? It would be an unusual agency relationship, in that Mr. Bonim or Verena were to receive the entire profit if they succeeded in selling the diamonds for more than the minimum price stated by the plaintiffs. But such a transaction could in law be one of agency. Nevertheless I am *[*1375]* convinced on the evidence that in this case it was not. The plaintiffs entrusted the diamonds to Mr. Bonim on terms that he, or Verena, should have an option to buy them from the plaintiffs at the minimum selling price; and that if the option were not exercised they would be returned. The transaction was one of sale or return, between the plaintiffs and Mr. Bonim or Verena.

A more difficult question is as to the nature of the relationship between Mr. Bonim and Verena. In one of his Civil Evidence Act statements Mr. Bonim says: "During 1981 I entered into a contract of A copy of the contract was attached. It was written in the Hebrew or "service agreement." There was provision for Mr. Bonim to receive a commission from Verena on the sale of goods of which he had organised the supply. Clause 12 provided:

> "Verena undertake to ask from the German authorities a permanent work permit for Mr. Bonim and after receiving the work permit they will make a new work agreement and Mr. Bonim will be employed as an employee on a salary by Verena."

In another Civil Evidence Act statement, however, Mr. Bonim stated that he was not employed by Verena, and worked as a self-employed agent. That statement is not signed, but was made to Mr. Greenslade on 21 May 1982, as appears from paragraph 14 of Mr. Greenslade's affidavit. In addition a letter from the plaintiffs to the insurance brokers dated 1 September 1982, in respect of which I was told that there was also a Civil Evidence Act notice, had this paragraph:

> "Bonim told us that he had no official trading status in West Germany, but that he had an arrangement with Verena … who acted as his nominees and who provided him with the various trading facilities he required."

I reject the evidence which suggests that Mr. Bonim was an employee of Verena. But I am not confident as to what the true relationship was between them. The most likely analysis is that it was one of agency, or a joint venture. What matters, as will appear, is that Mr. Bonim was not solely carrying on his employer's business; in part at least, he was carrying on his own business. But Verena also were concerned on their own behalf with the diamonds received from the plaintiffs, whether they were joint venturers or the sole principals. That is why I concluded earlier that a charge of falsehood on the part of the plaintiffs, in making out their invoice to Verena rather than Mr. Bonim, could not (if such a charge had been made) be substantiated. On this issue my conclusion is that there was a loss to the extent of $142173.88 covered by the contract of insurance.

(B) Did a breach or breaches of German law occur in connection with the diamonds lost?

[His Lordship considered provisions of the General Tax Code of West Germany, whether the plaintiffs and Verena were in breach of those provisions and whether offences were committed by Mr. Bonim, and continued:]

So I conclude that the following offences were committed in connection with the diamonds: (1) by Verena, the offence of tax evasion under section 370 of the General Tax Code of West Germany *[*1376]* (but confiscation of the diamonds would not have been ordered); (2) by the plaintiffs, the offence of tax endangerment under section 379 of the General Tax Code, subject to the question of jurisdiction; (3) by Mr. Bonim the offence of living and working in Germany without a residence permit; and (4) by Mr. Bonim the offence of failing to report the commencement of his business to the local authority. I have said that these offences were committed in connection with the diamonds, but it should be observed, in case it turns out to be relevant, that a few of the diamonds stolen were from the November consignment, and not that sent in February. It cannot be said that those few diamonds were in any sense at all connected with offences (1) and (2) above, but only with offences (3) and (4). The precise degree of connection that is significant falls to be considered in the next section.

As to the knowledge of the plaintiffs that these offences would be or were being committed, I have already found that Mr. Laub must have realised that in all probability the object of the false invoice was to deceive the German customs. He must also have appreciated that such conduct would be unlawful in Germany. More

difficult is the question whether he knew about the offences being committed by Mr. Bonim. Mr. Laub knew that Mr. Bonim "had no official trading status in West Germany." It does not necessarily follow that he knew Mr. Bonim was committing offences (3) and (4) above, or any offences of that nature. I do not find it proved that Mr. Laub or anyone at the plaintiffs knew that.

(C) Do the breaches of German law afford the insurers a defence to the claim, wholly or in part?

It is not proved, nor was it suggested, that any of those breaches caused or contributed to the loss of the diamonds in any way. What is said in the amended points of defence is that: (1) it was an implied term of the contract of insurance that, in so far as the defendant (which must have been intended to mean the plaintiffs) could control the matter, the adventure would be carried out in a lawful manner; (2) the plaintiffs' claims are tainted by illegality; and (3) it would be contrary to public policy to permit the plaintiffs to recover. No separate argument was put forward in relation to ground (3), except perhaps a point relating to European Community law which I shall mention later. Otherwise public policy has been put forward only as an alternative label for ground (1) or ground (2) or both of them.

Implied term

This, as was confirmed in further and better particulars, is said to be implied by law and on no other ground. It would have been difficult to justify such an implication on the facts, for two reasons. First, the term is said, again in the further and better particulars, to be a warranty, in the peculiar sense of that word which is found in *section 33(3)* of the Marine Insurance Act 1906, which provides:

> "A warranty, as above defined, is a condition which must be exactly complied with, whether it be material to the risk or not. If it be not so complied with, then, subject to any express provision in the policy, the insurer is discharged from liability as from the date of the breach of warranty, but without prejudice to any liability incurred by him before that date."

[*1377]

The breach need not be in any way a cause of the loss. I do not see how such a term could be necessary for business efficacy, or so obvious that it would pass the officious bystander test. Secondly, the confiscation and expropriation wording, which formed part of the contract, contained express warranties that the plaintiffs would comply with the laws of any country where the property might be, and that all permits necessary for legal operation would be obtained. But the sanction provided was that if failure to comply with the warranties should prejudice the insurance to the extent of a loss, there should be no liability on the insurers. That, as it seems to me, requires proof that the breach of warranty was at least a cause of the loss. It does not have the same effect as *section 33(3)* of the Marine Insurance Act 1906. The confiscation and expropriation wording was evidently drafted by a separate hand and at a different time from the rest of the contract. It may well be that the warranties it contains are only applicable to the additional cover, if such it be, which the wording provides. Nevertheless it would, in my judgment, be a major obstacle to the implication, on the facts, of the term which the insurers contend for.

So I turn to implication as a matter of law. This is said to arise from *section 41* of the Marine Insurance Act 1906:

> "There is an implied warranty that the adventure insured is a lawful one, and that, so far as the assured can control the matter, the adventure shall be carried out in a lawful manner."

The contract here was not one of marine insurance, as defined in sections 1 to 3 of the Act of 1906. That is supported by the fact that the slip specifies the J(A) form of policy, rather than the S.G. form. So the Act of 1906 is not in terms applicable. But it was an Act to codify the common law, some aspects of which were equally applicable to non-marine insurance. One such is dealt with in section 18 (disclosure by assured) which is commonly referred to in non-marine cases. The question is therefore whether section 41 in particular reflects the common law applicable to all classes of insurance, or is peculiar to marine insurance.

Immediately there is the problem that non-marine insurance does not in general constitute an insurance on an adventure but on property, whereas marine insurance is on an adventure at any rate in the case of goods if not also of a ship: see the reasoning of the judge-arbitrator (Staughton J.) in *The Bamburi* [1982] 1 Lloyd's Rep. 312, 318. In *Moore v. Evans* *[1918] A.C. 185*a firm of jewellers had insured their stock of jewellery by a non-marine policy, and claimed that certain pearls were lost because they were detained, albeit safe and sound, in Germany and Belgium during wartime. The claim failed. Lord Atkinson said, at p. 191:

> "It is not pretended in this case that the policy is a marine policy on goods; it was not argued, it could not be argued

> rationally, that, this being a non-marine policy, the appellants could recover for the loss or defeat of the adventure on which the goods were embarked."

Lord Parker of Waddington agreed with Lord Atkinson, and also with Bankes L.J. in the Court of Appeal [1917] 1 K.B. 458, 466 where he had said: ***[*1378]***

> "In my opinion the policy is a policy upon the goods enumerated therein, and not a policy upon any adventure connected with those goods."

If there is no adventure in a non-marine policy, the implied term suggested by the insurers makes no sense; and that is the end of the matter. The same result can be reached more readily by the application of common sense. Suppose that a motor car is insured for a calendar year, and is driven in January in excess of the speed limit. Would that be an answer to a claim for a loss by theft or fire or a road accident in June? If a publican insured his stock of glasses and they were stolen in June, would it matter that they had been used for drinking after permitted hours in January? Those examples illustrate the point that the insurance here was on goods, and not on any adventure. I therefore reject the argument of an implied term.

If I had not done so, I have considerable doubt as to whether the term to be implied should embrace foreign illegality as well as illegality by English law. Section 41 of the Marine Insurance Act 1906 is not mentioned in *Dicey & Morris, The Conflict of Laws* , 10th ed. (1980), although that may be because, if it does embrace foreign law, it is not a conflict rule but a rule of construction. I was referred to *Parkin v. Dick* (1809) 11 East 502 for the common law basis of the rule. In that case there was an insurance on goods to be thereafter specified, from London to the Brazils. A small part of the goods comprised naval stores, the export of which was prohibited by English law. Mr. Taddy, for the plaintiff, apparently conceded that he could not recover in respect of the naval stores, but claimed in respect of the other goods which were lawfully carried. Lord Ellenborough C.J. said, at p. 503:

> "It has been decided a hundred times that if a party insure goods altogether in one policy, and some of them are of a nature to make the voyage illegal, the whole contract is illegal and void."

There is nothing in that case to suggest that illegality by foreign law would have the same result; or, for that matter, that it would be a breach of any implied warranty. I asked counsel if there was any case where foreign law had been invoked in connection with this doctrine, and was told that there was only one: *Planche v. Fletcher* (1779) 1 Doug. 251. There goods were insured on a ship from London to Nantz, with liberty to call at Ostend. Bills of lading described the goods as shipped at Ostend; but in fact the vessel did not go there, and the goods had been shipped at London. The reason for this deception was apparently to avoid the high import duty payable in France on English goods. Lord Mansfield C.J. said, at p. 253, that there "was no fraud in this country. One nation does not take notice of the revenue laws of another." That provides no support for any implied term that the adventure will not be illegal by foreign law. However, Lord Mansfield's observation on foreign revenue laws has been much criticised.

There is some authority for the view that in other classes of contract there can be an implied term as to compliance with foreign law: *Ralli Brothers v. Compania Naviera Sota y Aznar [1920] 2 K.B. 287*. There a charterparty governed by English law required the freight to be paid in Spain. By Spanish law it was illegal to pay freight in excess of 875 pesetas per ton. Owing to alterations in the rate of exchange the freight reserved by the charterparty exceeded that figure when the time for ***[*1379]*** payment arrived. It was held that the shipowners could not recover the excess. Scrutton L.J. said, at p. 304:

> "where a contract requires an act to be done in a foreign country, it is, in the absence of very special circumstances, an implied term of the continuing validity of such a provision that the act to be done in the foreign country shall not be illegal by the law of that country. This country should not in my opinion assist or sanction the breach of the laws of other independent states."

If that result ensues from an implied term, then presumably the parties can contract out of it. For an implied term which the parties cannot contract out of is, so far as I am aware, a creature unknown to the common law. Sometimes, as in consumer protection legislation, statute law inserts a term in a contract which the parties cannot displace; but that seems to me more aptly described as an incident of the contract imposed by law, rather than an implied term.

Those reflections suggest that the solution adopted by Scrutton L.J. in 1920 of an implied term was not altogether a happy one. In my opinion, illegality of a contract by foreign law is now affected by a rule of law rather than an implied term. The rule is stated in *Dicey &*

Morris, The Conflict of Laws , 10th ed., at p. 794:

> "A contract (whether lawful by its proper law or not) is, in general, invalid in so far as the performance of it is unlawful by the law of the country where the contract is to be performed …"

The rule is one of public policy, as appears from *Regazzoni v. K.C. Sethia (1944) Ltd.* [1958] A.C. 301. But it is of no assistance to the insurers in this case. Performance of the contract of insurance would take place wholly in England. I can thus find no support for an implied term such as the insurers rely on in relation to foreign law. As I have said, even if I had held that there was such an implied term so far as concerns compliance with English law, I would have considerable doubt whether it extended to foreign law as well. But I rest my judgment on the conclusion that there is no implied term at all of the kind proposed, in a contract of non-marine insurance on goods.

Tainted with illegality

In *Mackender v. Feldia AG* [1967] 2 Q.B. 590, 600–601, there is this passage in the judgment of Diplock L.J.:

> "It is said that the adventure insured was 'tainted' with illegality, not under Belgian law but under English law. This is a picturesque metaphor which invites analysis."

For my part, I would with respect substitute the word "demands" for "invites." Another metaphor is to be found in the speech of Lord Diplock in *United City Merchants (Investments) Ltd. v. Royal Bank of Canada* [1983] 1 A.C. 168, 189 — "tarred with the same brush." "Tainted" in its literal sense means contaminated with something poisonous, or with incipient putrefaction. As a metaphor in the context of a contract and illegality I think it means that, while the contract is not itself illegal, it has a connection with some other illegal transaction which renders it obnoxious.

The contract of insurance was not itself illegal in the present case; neither the making of the contract nor the performance of it, by the ***[*1380]*** payment of premium on the one hand and claims on the other, was illegal by English law. The question is therefore whether it has that degree of connection with illegal acts in Germany which would render it tainted and therefore unenforceable here. One can divide this question into two parts. First, if the acts concerned had been illegal by English law, would the contract of insurance have been enforceable? Secondly, if so do the rules of conflict of laws justify reference to German law, and so produce the same result in this case?

As to English law, three first instance decisions were cited which provide helpful guidance. In *Pye Ltd. v. B.G. Transport Service Ltd.* [1966] 2 Lloyd's Rep. 300 the plaintiffs claimed on a contract of carriage for the loss of their goods in Stepney, where they were stolen. It had been agreed between the plaintiffs and their buyers that the goods, which were to be shipped to Persia, would be invoiced at less than the true price in order to deceive the Persian customs authorities. That involved the plaintiffs in breaches of English law, viz. the Customs and Excise Act 1952. It was argued for the carriers that the plaintiffs could recover no more than the value stated in the invoice. That argument was rejected. Browne J. said, at p. 309:

> "The plaintiffs do not have to rely on their contract with [their buyers], to establish or support their cause of action against the defendants, and it is quite irrelevant for that purpose. The measure of damages is prima facie the market value of the goods at the time of their loss. Even if the plaintiffs had agreed to make a free gift of these goods to [their buyers], they could still recover the value of the goods as against the defendants."

That case is, as it seems to me, an example of what I will later call the *Bowmaker* principle: see *Bowmakers Ltd. v. Barnet Instruments Ltd.* [1945] K.B. 65.

Next, *Geismar v. Sun Alliance and London Insurance Ltd.* [1978] Q.B. 383. The facts, as set out in the headnote, were that

> "The plaintiff had brought into the United Kingdom various items of jewellery which he failed to declare and on which he did not pay customs and excise duty. He had thus committed an offence in relation to the non-payment of duty and the jewellery was liable to forfeiture at any time. He claimed indemnity from the defendant insurers for the loss through theft at his home of the uncustomed jewellery and other items, which as part of the contents of his house were covered by three contracts of insurance with the defendants. They refused to indemnify the plaintiff in respect of the loss of the uncustomed items on the grounds of public policy and they claimed also that if they did indemnify the plaintiff they would be committing an offence under section 304 of the Customs and Excise Act 1952."

The claim failed in so far as it related to the uncustomed jewellery. The judgment of Talbot J. contains a lengthy and helpful citation of earlier authority. The judge's reasoning is, I think, set out, at p. 395:

> "to allow the plaintiff to recover under the policies would be to allow him to recover the insured value of the goods which might have been confiscated at any moment and which, therefore, were potentially without value to him … It seems to me from what Lord Denning M.R. said in *Mackender v. Feldia AG* [1967] 2 Q.B. 590 the policies would be unenforceable, provided that to *[*1381]* enforce them would conflict with public policy. So these smuggled articles are in the same category as the forbidden cargo in *Parkin v. Dick*, 11 East 502. No new area of public policy is involved here. The plaintiff is seeking the assistance of the court to enforce contracts of insurance so that he may be indemnified against loss of articles which he deliberately and intentionally imported into this country in breach of the Customs and Excise Act 1952 … where there is a deliberate breach of the law I do not think the court ought to assist the plaintiff to derive a profit from it, even though it is sought indirectly through an indemnity under an insurance policy."

Although the judge cited Lord Denning M.R. for the proposition that the policies were unenforceable, he did in fact give judgment for the plaintiff for £629.80, which was presumably the value of those items stolen which had been obtained innocently. Furthermore, in *Parkin v. Dick*, 11 East 502 it had been conceded that there could be no recovery in respect of the forbidden articles; the decision was that the claim in respect of the innocent goods also failed. Nevertheless I would, if I may say so, not disagree with the judge's conclusion on the facts of that case. It seems to me to be an application of what I shall later call the *Beresford* principle: see *Beresford v. Royal Insurance Co. Ltd.* [1938] A.C. 586.

Thirdly there is *Thackwell v. Barclays Bank Plc.* [1986] 1 All E.R. 676. The facts were complicated. For present purposes it is sufficient to say that the plaintiff sued for conversion of a cheque, payable to himself, on which his endorsement had been forged. The cheque represented part of the proceeds of a fraudulent financing transaction in which, as Hutchison J. found, the plaintiff was implicated. It was held that he could not recover, on the basis of the maxim ex turpi causa non oritur actio. The submission of counsel for the plaintiff, at p. 684, was that the defence is only available (i) where a plaintiff has to rely on his or another person's criminal, fraudulent or illegal activity to found his claim, or (ii) where the court, in finding for the plaintiff, will be indirectly assisting or encouraging the plaintiff in his criminal, fraudulent or illegal activity. The contrary argument is set out in the judgment, at p. 687:

> "Counsel for the defendants does not seek to meet these submissions head on. He contends that there are, running through the cases on this topic, two distinct but related lines of authority. The first is exemplified by the cases cited by counsel for the plaintiff, and he contends that, if exposed only to the test laid down by those cases, the plaintiff's claim once the statement of claim was amended became unexceptionable. However, counsel for the defendants contended that the other line of authority, which he described as laying down the 'conscience test', was fatal to the plaintiff's claim. That test, he suggested, involved the court looking at the quality of the illegality relied on by the defendant and all the surrounding circumstances, without fine distinctions, and seeking to answer two questions: first, whether there had been illegality of which the court should take notice and, second, whether in all the circumstances it would be an affront to the public conscience if by affording him the relief sought the court was seen to be indirectly assisting or encouraging the plaintiff in his criminal act."

*[*1382]*

Hutchison J. accepted that argument. He said, at p. 689:

> "I should state that, even had I found that Mr. Thackwell was innocent and that Mr. Sawford alone was the perpetrator of the fraudulent refinancing transaction, I should have denied Mr. Thackwell recovery. This is because I accept the correctness of the arguments advanced by counsel for the defendants and, adopting his approach, it seems to me first that it would indeed be difficult to find a case in which the criminal conduct relied on was more proximate, because as counsel for the defendants submits, the cheque alleged to have been converted constituted in reality the very proceeds of the fraudulent conduct … by permitting Mr. Thackwell to recover the proceeds of this cheque from the bank I should, as it seems to me, be indirectly assisting in the commission of a crime."

I too accept that there are two lines of authority. The first includes the decision of the Court of Appeal in *Bowmakers Ltd. v. Barnet Instruments Ltd.* [1945] K.B. 65, 71:

> "a man's right to possess his own chattels will as a general rule be enforced against one who, without any claim of right, is detaining them, or has converted them to his own use, even though it may appear either from the pleadings, or in the course of the trial, that the chattels in question came into the defendant's possession by reason of an illegal contract between himself and the plaintiff, provided that the plaintiff does not seek, and is not forced, either to found his claim on the illegal contract or

> to plead its illegality in order to support his claim."

See also *Chitty on Contracts* , 25th ed. (1983), p. 627, para. 1160:

> "It is not sufficient, in order to bring the plaintiff within the maxim, that he should merely be obliged to give evidence of an illegal contract as part of his case … for the rule applies only where the action is founded upon the illegal contract, and is brought to enforce it."

That is what I call the *Bowmaker* principle: a plaintiff fails if he has to found his claim on an illegal contract, or to plead its illegality in order to support his claim. A number of cases were cited which illustrate the operation of that principle: see *Cleaver v. Mutual Reserve Fund Life Association [1892] 1 Q.B. 147*; *Gordon v. Chief Commissioner of Metropolitan Police [1910] 2 K.B. 1080*; *Marles v. Philip Trant & Sons Ltd.* [1954] 1 Q.B. 29; *Singh v. Ali* [1960] A.C. 167; *Palaniappa Chettiar v. Arunasalam Chettiar* [1962] A.C. 294; *Pye Ltd. v. B.G. Transport Service Ltd.* [1966] 2 Lloyd's Rep. 300; *Belvoir Finance Co. Ltd. v. Stapleton* [1971] 1 Q.B. 210and the United States cases cited in *Geismar v. Sun Alliance and London Insurance Ltd.* [1978] Q.B. 383, 394, particularly *Brown v. New Jersey Insurance Co.* (1932) 14 P. (2d) 272, 274: "if he cannot open his case without showing that he has transgressed the law, a court will not assist him."

It is not always easy to apply the *Bowmaker* principle, and to decide whether, on the facts, a plaintiff needs to plead or prove illegality, or to show it in opening his case. But quite apart from that, the principle makes no provision for cases where, although the plaintiff can establish his title without any mention of illegality, it is based on the immediate ***[*1383]***
and direct proceeds of crime. Hence there is a need for something such as the conscience test adopted by Hutchison J. in *Thackwell's* case [1986] 1 All E.R. 676. Otherwise a plaintiff could, I suppose, recover from the insurers of his possessions if a quantity of heroin were stolen from him; he would not need to plead or prove that he was not an authorised possessor, such as a doctor or a policeman. Or a professional handler of stolen goods could recover in respect of their loss. I call this the *Beresford* principle by reference to the speech of Lord Atkin in *Beresford v. Royal Insurance Co. Ltd.* [1938] A.C. 586, 596:

> "There now arises the question whether such a contract is enforceable in a court of law. In my opinion it is not enforceable. The principle is stated in the judgment of Fry L.J. in *Cleaver v. Mutual Reserve Fund Life Association [1892] 1 Q.B. 147*, 156: 'It appears to me that no system of Jurisprudence can with reason include amongst the rights which it enforces rights directly resulting to the person asserting them from the crime of that person.' The cases establishing this doctrine have been fully discussed by Lord Wright M.R. in his judgment in the present case. I mention some of them in order to call attention to the fact that, while in the earlier cases different reasons have been given for the rule, the principle can now be expressed in very general terms."

Later he said, at pp. 598–599:

> "I think that the principle is that a man is not to be allowed to have recourse to a court of justice to claim a benefit from his crime whether under a contract or a gift. No doubt the rule pays regard to the fact that to hold otherwise would in some cases offer an inducement to crime or remove a restraint to crime, and that its effect is to act as a deterrent to crime. But apart from these considerations the absolute rule is that the courts will not recognise a benefit accruing to a criminal from his crime."

That is the principle which I believe to have been the basis of the decision in *Geismar's* case [1978] Q.B. 383, as well as *Thackwell's* case [1986] 1 All E.R. 676. It can be found elsewhere: see *Marles v. Philip Trant & Sons Ltd.* [1954] 1 Q.B. 29, 89, *per* Denning L.J.; *Chitty on Contracts* , 25th ed. (1983) p. 627, para. 1161; and particularly the judgment of Devlin J. in *St. John Shipping Corporation v. Joseph Rank Ltd.* [1957] 1 Q.B. 267. There the *Bowmaker* ([1945] K.B. 65) and *Beresford* 586) principles are recorded as separate arguments of counsel, at pp. 282–283, and separately considered, at pp. 291–294. The judge limits the *Beresford* principle to rights directly resulting from crime.

The precise degree of proximity between the plaintiffs' claim and criminal behaviour, which is necessary to bring the *Beresford* principle into force, will vary with the circumstance of a particular case. That is why Hutchison J. described it as a conscience test. The more remote the crime, the less reason to apply the principle. In *Bird v. Appleton* (1800) 8 Durn. & E. 562 it was argued that a contract of insurance on cargo was illegal because the cargo was bought with the proceeds of a former illegal cargo. Lord Kenyon C.J. said, at p. 566:

> "If this objection were well founded, it would go to an alarming extent. In deciding on a claim made on a policy of insurance, it would be necessary to examine and scrutinize the past conduct of the assured, in order to see whether or not, by their former ***[*1384]***

> transactions in life, they had illegally acquired the funds with which the particular goods insured were purchased: but we cannot enter into considerations of that kind; we must confine ourselves to the immediate transaction before us; …"

It may be that money in the shape of coins and notes, being negotiable, has a tendency to become cleansed of illegality more swiftly than other property. That, with other factors, may well be the explanation of *Gordon v. Chief Commissioner of Metropolitan Police [1910] 2 K.B. 1080*, where the plaintiff was able to recover from the Chief Commissioner of Metropolitan Police money which he had obtained by street betting.

So, in my judgment, a claim may be said to be tainted with illegality in English law by virtue of the *Bowmaker* principle if the plaintiff needs to plead or prove illegal conduct in order to establish his claim; or by virtue of the *Beresford* principle if the claim is so closely connected with the proceeds of crime as to offend the conscience of the court. On the facts of this case, I do not think that either principle would apply, even if the case were concerned only with English law. It would not be within the *Bowmaker* principle because the plaintiffs do not need to plead, or prove, or show in the course of opening their case, any of the illegal acts which I have found to be committed. They do not need to produce or prove the false invoice: see the judgment of Browne J. in *Pye Ltd. v. B.G. Transport Service Ltd.* [1966] 2 Lloyd's Rep. 300, 309, already cited. As to the *Beresford* principle, I do not consider that the claim in this case represents the proceeds of crime at all, let alone directly and immediately or proximately. *Geismar v. Sun Alliance and London Insurance Ltd.* [1978] Q.B. 383, is in my judgment distinguishable, for the illegality there went directly to the plaintiff's possession of the goods stolen, whereas here the title of the plaintiffs is not in any way affected by illegality. Nor do I consider that the conscience of the court would be affronted if the plaintiffs were to recover. For acts which were by English law criminal they might be convicted and sentenced. But those acts would have been at most incidental to their claim, if that. Public policy does not require that they be deprived of it. The claim is not tainted with illegality.

In the light of that conclusion, it is not, as will appear later, necessary for me to consider the second question under this head, whether the rules of conflict of laws justify reference to German law. But in case I am wrong on the first question, and as the point was argued at length, I shall do so.

In every case involving a foreign element it is necessary to consider three preliminary matters. First, what is the legal topic with which the case is concerned? Secondly, what is the connecting factor prescribed by the rules of conflict of laws for assigning cases on that topic to a particular system of law? Thirdly, what system of law does the connecting factor point to in the case before the court? See *Dicey & Morris, The Conflict of Laws* , 10th ed., pp. 26–27.

In the present case the topic in question is enforcement of a contract associated with illegality. The connecting factor, in general terms, may be one of three, as set out in the extempore judgment of Diplock L.J. in *Mackender v. Feldia AG* [1967] 2 Q.B. 590, 601:

> "English courts will not enforce an agreement, whatever be its proper law, if it is contrary to English law, whether statute law or ***[*1385]*** common law; nor will they enforce it even though it is not contrary to English law if it is void for illegality under the proper law of the contract. Furthermore, subject to one exception, the English courts will not enforce performance or give damages for non-performance of an act required to be done under a contract, whatever be the proper law of the contract, if the act would be illegal in the country in which it is required to be performed. The exception, the precise scope of which is unsettled and need not be determined in the present case, is where the illegality is a breach of a revenue or fiscal law of the foreign state."

There are thus overlapping conflict rules on the topic of contractual illegality, producing three connecting factors — the forum, the proper law, and the place of performance. I would, with the greatest respect, suggest two qualifications to that passage, which were not material then, and one of which is not material now. First, it is not always the case that an English court will refuse to enforce a contract which is valid by its proper law and the law of the place of performance, but invalid by English law: *Dicey & Morris, The Conflict of Laws* , 10th ed., pp. 85–86. Secondly, there is one limited class of contracts where a fourth connecting factor applies — exchange contracts affected by the Bretton Woods Agreements Order in Council 1946 (S.R. & O. 1946 No. 36), where the connecting factor is currency.

None of those connecting factors point to German law in this case. The forum is English, the proper law of the insurance contract English, the place of performance of that contract England, and the currency of it U.S. dollars. But the rules of conflict of laws which prescribe

those connecting factors have in the main been applied in cases where illegality was inherent in the contract sought to be enforced. How does one apply them when that contract is not said to be directly affected by illegality, but tainted with it? As to that, authority is sparse.

In *Mackender's* case [1967] 2 Q.B. 590, a policy of insurance on jewellery provided that it should be governed by Belgian law and that disputes should be exclusively subject to Belgian Jurisdiction. The plaintiffs, who were the insurers, claimed that the contract was affected by illegality and non-disclosure, in that the goods insured were intended to be smuggled into Italy. Consequently it was argued that the provisions as to proper law and jurisdiction were void; and that the plaintiffs were entitled to leave to effect service out of the jurisdiction in an action begun here. That was the issue which fell to be determined. The Court of Appeal rejected the plaintiffs' argument. It was held that illegality or non-disclosure would at most render the contract unenforceable or voidable, and would not destroy the Belgian Jurisdiction clause. Hence service out of the jurisdiction was set aside. But there is this important passage in the judgment of Lord Denning M.R., at pp. 598–599:

> "As to illegality, I would only say this: the underwriters were clearly innocent. The diamond merchants may have had an unlawful intention to smuggle goods into a friendly foreign country. But their illegality would not affect the formation of the contract. It would only make it unenforceable. It would mean that they could not recover on the policy. This dispute again comes within the foreign jurisdiction clause."

[*1386]

That might be thought to be a statement that an English court, considering a policy of insurance governed by English law, would hold it to be unenforceable if the assured intended to smuggle goods covered by the policy into Italy in breach of Italian law. But I doubt if Lord Denning M.R. intended to pronounce on that point; and it certainly was not necessary to the decision. It was sufficient to say that such a policy was at most unenforceable, rather than void.

Furthermore, Diplock L.J. in the passage, at p. 601, which I have already quoted, listed the connecting factors for a case of contractual illegality — forum, proper law and place of performance. None of them would render such a policy of insurance unenforceable if one considered the contract only. So I do not think that he at any rate necessarily agreed with a ruling to that effect, without further explanation. He said, at p. 605:

> "if the underwriters think that that defence is one which is worth persisting in, either as a matter of law or as a matter of business, they will have an opportunity of doing so under section 4(1)(*a*)(v) of the Foreign Judgments (Reciprocal Enforcement) Act 1933, if judgment on the assureds' claim is given against them in the Belgian courts and attempts are made to enforce it in this country. I have already indicated the nature of the facts which are said to give rise to this defence. Whether on further reflection the underwriters will wish to take it, I do not know."

That does not tend to show conviction on the part of Diplock L.J. that the policy of insurance would be unenforceable in England. Russell L.J., at pp. 605–606, had nothing to add on the topic of illegality. I must, however, quote in passing an observation made by him in the course of the argument, at p. 595: "Would Lloyd's be entitled to repudiate a policy on a car because it was sometimes used for poaching?" That is support for the conclusion I have reached that the claim in this case would not be tainted by illegality in English law.

In re Emery's Investments Trusts [1959] Ch. 410was concerned with United States securities belonging to a husband who lived with his wife in South America. They were registered in the name of the wife, in order to avoid liability to withholding tax under United States federal law. The husband was British but the wife a citizen of the United States. It was held, as stated in the headnote:

> "that the registration of the securities in the wife's name raised a presumption of advancement which could not be rebutted on the ground that the purpose of the registration in her name only was to enable the husband to avoid payment of American Federal tax, for equity would not grant relief in respect of a transaction carried out in contravention of law, albeit a foreign revenue law."

The claim there was based not on contract but on a trust. The decision, as it seems to me, is an application of the *Bowmaker* principle: in order to rebut the presumption of advancement the husband had to plead and prove his own illegal conduct; and that he could not be allowed to do.

It is however at first sight difficult to discern what conflict rule was applied so as to render the federal law of the United States relevant for consideration. The husband

was in South America, and some relevant connecting factor had to exist before he could be reproached for breaking the law of another country. But on examination of the facts it *[*1387]* appears that the securities were bought, registered and held by Irving Trust Company in New York, on the husband's instructions. From the conflict point of view the decision therefore amounted to this: a plaintiff fails for illegality if, in order to establish his claim, he must plead and prove conduct which is illegal by the law of a foreign country, and which occurred *in the territory of that country* .

The editor of the Law Reports considered that case to be a decision on the clean hands doctrine, as appears from the catchwords in the headnote. The Court of Appeal in *Tinker v. Tinker* [1970] P. 136agreed: see the judgment of Salmon L.J., at p. 143. That was a case concerned solely with English domestic law, and so of no relevance to the present inquiry. But it approves *Emery's* case [1959] Ch. 410, and to my mind interprets it as showing that the hands of a plaintiff in equity may be sullied by illegal conduct in a foreign country.

Lastly on this topic there is *United City Merchants (Investments) Ltd. v. Royal Bank of Canada* [1983] 1 A.C. 168. There a Peruvian company agreed to buy goods from an English company for a price in U.S. dollars f.o.b. London, payment to be by letter of credit in London. The price of the goods had been doubled by agreement between the parties in order to enable the buyers to export money from Peru unlawfully. That was the sale contract. But the contract on which the action was brought was another: it was between the Royal Bank of Canada, who confirmed the letter of credit in London, and the sellers as beneficiary of the letter of credit. That was the letter of credit contract, or rather the relevant contract out of two or more which arise when a letter of credit is opened.

The sale contract was illegal by the law of Peru. It was not governed by Peruvian law, nor to be performed in Peru, nor was action brought on it in Peru. But it was, in part, an exchange contract since one of its objects was to exchange the currency of Peru for U.S. dollars. Consequently the fourth of the possible connecting factors applied, as it involved the currency of Peru; and the sale contract would have been unenforceable in this country as to half the price stated in it. When action was brought on the letter of credit contract, it was held that this too was tainted or tarred and was unenforceable for half of its amount.

From those authorities I conclude that, when an English claim is said to be tainted by foreign illegality, one must first inquire whether, applying the appropriate connecting factor, the transaction from which the taint is said to arise would be enforceable here. If not, one has next to decide whether there is sufficient connection between that transaction and the claim to amount to taint within the *Bowmaker* or *Beresford* principle. If the answer to that second question is yes, the claim is unenforceable here.

One can test those conclusions by reference to the three cases cited. In *Mackender v. Feldia AG* [1967] 2 Q.B. 590, a contract to smuggle jewellery into Italy would, I suspect, now be regarded as unenforceable in England, because Italy would be the place of performance. That is subject to the exception about foreign revenue law which, as Diplock L.J. said, is unsettled and need not be determined in the present case. Was the insurance contract tainted by the intention to smuggle goods? It is not clear what proportion of the goods insured were to be smuggled. For my part, I doubt if that contract was tainted: it was not necessary for the assured to plead or prove their own illegality (*Bowmaker* principle), in order to recover in respect of a theft in Naples; nor did the *[*1388]* claim represent the proceeds of crime or, in my opinion, offend the conscience of the court (*Beresford* principle). I certainly do not regard the Court of Appeal as having decided that it was a case of taint. To judge from the observation of Russell L.J. in the course of the argument, he at least might well have held that it was not.

In *In re Emery's Investments Trusts* [1959] Ch. 410, a contract to register securities in New York in the wrong name in order to evade United States federal taxation would be unenforceable here, since New York would be the place of performance. Wynn-Parry J. must have considered that to be the case, as he referred to authority on the recognition of foreign revenue laws. He also held the claim before the court to be tainted, as it plainly was within the *Bowmaker* principle.

In *United City Merchants (Investments) Ltd. v. Royal Bank of Canada* [1983] 1 A.C. 168, the sale contract would have been unenforceable in part because it was in part an exchange contract, involving the currency of Peru, and was contrary to Peruvian exchange control regulations. The letter of credit contract was tainted within the *Beresford* principle, because to enforce it (as to half of the proceeds) would achieve a criminal

objective — not criminal by English law, but by a system of law which the court was bound to take notice of.

Applying my conclusions to the present case, I consider that an English court would not enforce a contract to deceive the German customs authorities in Germany, subject always to the point about foreign revenue law, since Germany would be the place of performance; nor, for that matter, would it enforce a contract by Mr. Bonim to reside in Germany without a permit, or to carry on business there without notifying the local authority, for the same reason. So this is indeed a case where German law is potentially relevant thus far. But the second stage of the inquiry is whether there is sufficient connection between the insurance claim and those activities to amount to taint. I have held that there is not. So German law is no obstacle to the success of the plaintiffs' claim.

Two other arguments were put forward by Mr. Gruder on behalf of the plaintiffs, which I mention only briefly as they are not in the event necessary to the decision of this case. He submitted that the claim should not be held to be tainted with illegality under the General Tax Code of Germany, for that would be to enforce a foreign revenue law. For my part, I remain unconvinced that this would be a case of enforcement rather than recognition: see *Attorney-General of New Zealand v. Ortiz* [1984] A.C. 1, 20, *per* Lord Denning M.R.

Mr. Gruder also submitted that, if the claim were tainted by illegality, that extended only to the part of the price which was not declared to the German customs authorites; so the plaintiffs could still recover a proportionate part of the value for insurance purposes of the diamonds stolen. He also contended that the plaintiffs could recover the full value of those few diamonds stolen which were not from the February parcel but from the November parcel, because there was no undervaluation in November. On those questions of partial recovery I express no opinion at all.

Public policy

The only separate argument under this head which has not already been considered arises from the European Community legislation. Mr. Malins for the insurers observes that the German law as to turnover ***[*1389]*** equalisation tax is maintained pursuant to the 6th Council Directive (77/388/E.E.C.) (Official Journal, 1977 L145, p1) of the European Community, with which all member states are bound to comply. Any failure to comply with it may be relied on by an individual in a dispute with the revenue authorities in his own country: *Direct Cosmetics Ltd. v. Customs and Excise Commissioners (Case 5/84)* [1985] 2 CML.R. 145. From those premises Mr. Malins makes the submission that it would be against public policy to treat a harmonised law in its application in one member state differently from its application in another member state.

I must admit that I am uncertain as to the impact of that submission on the present case. Nobody has suggested that the German law on turnover equalisation tax means anything different in England from what it means in Germany. To be of significance in the present case the submission would have to be that harmonised law of any member state should be both recognised and enforced in all other member states. As to that I make three observations. (i) It would make no difference in the present case. I have held that this court must consider German law, subject possibly to the exception of foreign revenue law. The claim of the plaintiffs nevertheless succeeds because the connection between activities which were illegal by German law and the insurance contract is not sufficient to render that contract tainted and therefore unenforceable.

(ii) The submission goes too far. It would mean that taxes payable under a harmonised law and penalties for breach of it could be recovered here. But the *Civil Jurisdiction and Judgments Act 1982,* enacted pursuant to Community law, applies to civil and commercial matters, and expressly excludes revenue, customs and administrative matters: see also the speech of Lord Templeman in *Williams and Humbert Ltd. v. W. & H. Trade Marks (Jersey) Ltd.* [1986] A.C. 368, 428: “at present the international rule with regard to the non-enforcement of revenue and penal laws is absolute.”

(iii) It is a matter for political decision whether harmonised laws of other member states should be directly enforceable here, and for legislation. I express no opinion whatever as to what the decision should be. But until that decision is taken and legislation enacted, these courts must employ the existing connecting factors recognised by the rules of conflict of laws in determining when effect will and will not be given to foreign law.

There must be judgment for the plaintiffs for $142173.88.

Judgment for the plaintiffs with costs.

Solicitors: Ince & Co.; Clyde & Co.

[Reported by ROBERT V. RAJARATNAM, ESQ.,
Barrister-at-Law]
