IN THE SUPREME COURT OF
THE REPUBLIC OF VANUATU
(Civil Jurisdiction)

Civil
Case No. 15/59 SC/CIVL

BETWEEN: **Gianna Burgagni and Fabio Pignatoro as liquidators of San Marino Investment SpA (SMI)**
Claimants

AND: **United Investment Bank Limited (UIB)**
Defendant

Date of Trial:	8 September 2021
Before:	Justice V.M. Trief
In Attendance:	Claimant – Mr N. Morrison
	Defendant – Mr J.C. Malcolm
Date of Decision:	6 April 2022

JUDGMENT

A. Introduction

1. This is a claim seeking to enforce guarantees given by the Defendant United Investment Bank Limited (the 'UI Bank') against a number of loans made by San Marino Investment SpA (In liquidation) ('SMI'), a San Marino-registered trust company. Improper use of monies is also alleged against the UI Bank.

2. The Claim is brought by Mrs Gianna Burgagni and Mr Fabio Pignataro, SMI's liquidators.

3. The UI Bank operated as a bank registered under the *Banking Act* [CAP. 63]. It was struck off the Vanuatu Companies Register on 12 February 2018.

B. Background

4. Prior to June 2011, UI Bank and SMI were owned by a Mr Enrico Pasquini.

5. Prior to June 2011, SMI lodged 4.5 million Euros with the UI Bank to enable SMI to obtain a 9 million Euros loan from UI Bank which along with some of its own funds, it lent to 4 of its subsidiary companies.

6. Simultaneously, the UI Bank issued guarantees to SMI as to the repayment of the loans by the 4 companies.

7. The UI Bank's loan to SMI was covered by contractual agreements.

8. On or about June 2011, Mr Andrea Pavoncelli bought UI Bank from Mr Pasquini.

9. On 9 July 2012, SMI was placed in liquidation and Mrs Burgagni and Mr Pignataro were appointed liquidators.

10. SMI remains indebted to the UI Bank.

11. On 12 April 2012, UI Bank purported to cancel the guarantees in writing.

C. Issues

12. By the Amended Claim, SMI seeks judgment for 28,397,000 Euros being for 22,800,000 Euros on the guarantees given by UI Bank and 5,597,000 Euros arising from alleged unlawful use of client's money.

13. SMI asserts that on the date of liquidation, it owed a debt to UI Bank and was a creditor of UI Bank for the amounts deposited in its own name but on behalf of its customers in several separated accounts. SMI alleges that UI Bank unlawfully used clients' money to repay part of its credits due to SMI and so it seeks repayment of 5,597,0000 Euros of its clients' money against an amount outstanding of 9,744,386 Euros.

14. UI Bank is opposed to that, relying on its contractual arrangements with SMI as follows:

    a. That on or about 12 April 2012, Mr Pavoncelli cancelled the guarantees to SMI but continued the loan to SMI backed by the deposit SMI lodged with the UI Bank, and that the cancellation was accepted by UI Bank on or about 18 April 2012; and

    b. That the funds deposited by SMI to a sum of approximately 4.5 million Euros were contracted as part and parcel of an indivisible current account. Effectively in the event of default of the SMI loan, the funds were part of the same transaction and applied against the loan as contracted therefore there was no unlawful use of client's money.

D. Evidence

15. Fabio Pignatoro is one of the two Claimants, liquidators of SMI. His sworn statement became **Exhibit C1**. He stated that the general intent of the Claimants' claim is to seek

monetary judgment against UI Bank for failure to account for funds due and owing to SMI. As liquidators, he and Mrs Burgagni are bound to prove those funds.

16. He attached many documents including the 9 April 2014 letter from UI Bank to SMI [**Tab 13, Exhibit C1**]:

> *From UIB* *To SMI*
>
> *9 April 2014*
>
> ***Re: Your letter [Prot. N. 7/14] dated 14th March 2013***
>
> *This is to state again that the closure and payment of credit accounts in your name is subject to the simultaneous closure and payment of debit accounts also in your name, as established by the General Conditions, and in the various correspondences that occurred with you...*
>
> *Furthermore, as the deadline of the loans took place on 31.03.2014, and you didn't reimburse them, we will take action to compensate debits and credits according to Articles 7 and 8 of the General Conditions signed by you. Moreover we strongly urge you to repay the remaining outstanding debt within 15 days from the receipt of this letter.*

17. In cross-examination, Mr Pignatoro confirmed that prior to the sale of UI Bank in mid-2011, SMI deposited 4.5 million Euros in UI Bank and at the same time, UI Bank lent 9 million Euros to SMI. He stated that the 4.5 million Euros deposited was money belonging to SMI's clients. SMI used the 9 million Euros it borrowed from UI Bank and 20 million Euros of its own money to lend money to 4 companies: Whitener Overseas Limited, Star of India Inc., Dromin Investments SA and Area Investments Corporation. The UI Bank guaranteed those loans.

18. When put to him that on 12 April 2012, UI Bank cancelled those guarantees, he stated that that was a unilateral act as UI Bank wrote its letter but there was no cancellation. In re-examination, he stated that in Italy, when receiving a communication, the recipient hand-signs at the bottom with the date. This is the practice so that documents are not lost, but it does not mean that SMI accepted that the guarantees were revoked.

19. Additionally in cross-examination, he was asked to confirm that the documents at **Tab 8, Exhibit C1** were the loan documents for SMI's 4.5 million Euros payment into UI Bank. He stated that those were the current account documents. When asked if he accepted that clauses 7 and 8 of the General Conditions authorized UI Bank to forfeit the 4.5 million Euros deposited, he answered that those clauses applied to money owned by SMI, but the money deposited belonged to SMI's clients. UI Bank is entitled to be repaid 9 million Euros but not to take it from other people's money.

20. It was put to him that there is no mention anywhere in the documents that the money deposited belonged to third parties. He answered that the UI Bank statements at **Tab 7, Exhibit C1** each show a code, which showed which particular SMI customer the statement/account related to. Mr Pignatoro acknowledged that the contract was between SMI and UI Bank only but that UI Bank kept separate accounts with separate client codes

therefore UI Bank knew it was SMI's clients' money. UI Bank is entitled to the 9 million Euros owed to it by SMI, but cannot take that money from other people who are not SMI.

21. He confirmed that people who deposited money with SMI have made claims against SMI in Italy and San Marino.

22. When asked if SMI had made claims against the 4 companies, he said that those 4 companies were non-existent companies in tax havens, all connected to Mr Pasquini; SMI was just seeking payment of 5 million Euros of clients' money that UI Bank used to off-set the debt owed.

23. Lindsay Barrett is an accountant. His sworn statement, produced by consent, became **Exhibit D1**. He evidenced that before mid-2011, Mr Pasquini made loans from SMI to four offshore companies, which were also related to Mr Pasquini. At the same time, Mr Pasquini arranged guarantees from UI Bank, presumably to justify the borrowing and to provide a bank guarantee for the four companies. After Mr Pavoncelli purchased UI Bank in mid-2011, he with the consent of Mr Pasquini and SMI, cancelled the guarantees.

24. Mr Barrett evidenced that he understood that UI Bank acted as a bank operating at minimum exposure. Hence to obtain a loan from UI Bank there had to be a sufficiently large deposit to cover and reduce such exposure. Loans from UI Bank were also subject to contractual obligations, which SMI signed, including provisions that the deposit funds form part of an indivisible current account. When SMI defaulted on its loan arrangements with UI Bank, the deposit was forfeited to UI Bank pursuant to their agreement. Further, that the reality is that SMI is indebted to UI Bank for a far larger sum than the loans and interest from UI Bank.

25. Finally, Mr Barrett evidenced that the loan was between SMI and UI Bank however the liquidators (Claimants) refer to loans to four companies associated with Mr Pasquini. Those loans were separate transactions between those 4 companies and SMI. He stated that the liquidators are erroneously chasing UI Bank instead of the 4 companies and Mr Pasquini. UI Bank has no assets in Vanuatu or elsewhere to the best of his knowledge and it has been struck off in Vanuatu. The documents attached to Mr Pavoncelli's sworn statement proved his (Mr Barrett's) assertions.

26. Andrea Pavoncelli is a businessman, from Italy. His sworn statement was produced by consent, **Exhibit D2**. He evidenced that he purchased UI Bank in mid-2011. After that date, the relationship between SMI and UI Bank changed to one of a normal bank/client relationship. He evidenced that UI Bank had always acted as a bank operating without exposure therefore to obtain a loan from UI Bank, there had to be a sufficiently large deposit from the client to cover the loan. It seems strange to deposit enough funds to cover a loan but the simple explanation is that it was set up as Vanuatu was a tax haven at that time and the operation gave certain tax advantages to the Borrower. It avoided the need to pay tax on the interest payments.

27. The loan granted to SMI was made prior to his purchase of UI Bank. SMI had deposited 4.5 million Euros to guarantee the loan. SMI's letter dated 11 February 2005 to UI Bank [**annexure "G", Exhibit D2**] stated as follows:

> *To UIB*
>
> *11.02.2005*
>
> *Hereby we confirm that the current accounts showed into the attached letter grant the amounts lent to the current accounts 2110,2111, 2113 opened with you.*
> *So the balances of that's accounts will be available only by the reimbursement, even partially, of the loans to the accounts 2110, 2111, 2113.*

28. The loan was subject to General Conditions of Loan signed by SMI which contained clauses 7 and 8 as follows, [**annexure "B", Exhibit D2**]:

> 7. *By explicit agreement and whatever the currency in which they are recorded, any amounts held in custody by the Bank on behalf of a customer shall be utilized to guarantee any customer debt payable to the Bank. The Bank shall be entitled, whenever it deems it necessary and without any formalities, to compensate any customer debts to the Bank by means of the aforesaid amounts. This compensation may also occur when the customer is subject to bankruptcy procedures, taking into account the binding link between customer debt and bank credit items. Furthermore, securities collateral that the customer or guarantor have provided or may provide for transactions shall be deemed to fully cover all transactions and, generally speaking, any debts owed by customers to the Bank.*
>
> 8. *All accounts opened by the same customer, whether in domestic or foreign currency, and whatever the nature and type of these accounts, shall form part a single, indivisible current account; the Bank shall have the right at any time to transfer debt items to accounts with a surplus balance, simply by issuing a statement. If any of the latter are foreign currency accounts, the applicable exchange rate shall be the one recorded on the date of the transfer.*
>
> *(my emphasis)*

29. Mr Pavoncelli evidenced that at no stage did SMI negotiate or request that clauses 7 and 8 be deleted or amended. He understands the effect of those clauses to be that the funds paid by SMI to guarantee the loans could be claimed by UI Bank even when SMI was subject to bankruptcy procedures, and that is what has happened here.

30. UI Bank sent letters of guarantee to SMI in respect of each of the four companies (three letters dated 8 November 2006 and one letter dated 31 May 2010, [**annexure "M", Exhibit D2**]) in identical terms except as to the date, amount lent and company concerned (each of the 4 companies) as follows:

> *On UIB letterhead* *To SMI*
>
> *8 November 2006 [date]*
>
> *Dear Sirs,*
>
> *In order to guarantee the reimbursement of the loan of Euro 8,000,000.00 (Eight Million/00) [amount lent], granted by you to Mess.rs Star of India [company concerned], East 53rd Street, Marbella, Swiss Bank Building, Panama – Republic of Panama on 02 January 2003, we, UIB*

United Investment Bank Ltd, hereby irrevocably agree to repay you, at your first demand, independently from the validity and from the effects of the underlying contract and without the possibility to raise any of the exception and objection which may derive from the same, any sum up to Euro 9.600,000.000 (Nine Million Six Hundred Thousand/00) [guarantee amount] - principal sum, interests and costs included - upon presentation of your written demand of payment, signed by the proper authorized signatory to be sent via registered mail and containing the statement that Mess.rs Star of India Inc., Panama does not have reimbursed you on expiry (not specified if of the entire loan or of the single instalments) the sum of money that you are now requesting us under this guarantee.

...

Any payment performed under this guarantee will reduce our overall obligation towards you.

Our guarantee is valid up to 31 December 2020 and it may be renewed but will be automatically and entirely extinguished if your demand of payment is not received within the aforesaid date, whether or not it will be a working day.

This guarantee is governed by the law of the Republic of Vanuatu.

(my emphasis)

31. Following his mid-2011 purchase of UI Bank, on or about 12 April 2012, he sent a letter to SMI cancelling the guarantees because of the changes of shareholders and their relationship **[annexure "N", Exhibit D2]**:

To SMI

12 April 2012

Subject: withdraw provided surety

Sirs,

In reference to sureties given to you in favor of:
- *Whitener Overseas Ltd (amount of E4.800.000,00 – signed 31.05.2010),*
- *Star of India Inc. (amount E 9.600.000,00 – signed 08.11.2006)*
- *Dromin Investment SA (amount E 3.600.000,00 – signed 08.11.2006)*
- *Area Investment Corp. (amount E 4.800.000,00 – signed 08.11.2006)*

We inform you the will to withdraw the mentioned sureties, starting from the end of the month of April 2012, as a result of the changing relationship with these companies and the agreement made prior sale and change of shareholders of the writer.

Would you please sign a copy of this letter for your acceptance.

(my emphasis)

32. On 18 April 2012, Mr Pasquini as Chairman and Managing Director of SMI signed UI Bank's 12 April 2012 letter in acceptance of the cancellation **[annexure "O", Exhibit D2]**.

33. When SMI's liquidators by letter dated 3 May 2013 demanded payment under the guarantees **[annexure "P", Exhibit D2]**, UI Bank responded by letter dated 29 May 2013 that the guarantees had been revoked **[annexure "Q", Exhibit D2]**. It repeated that response in its letter dated 13 July 2014 **[annexure "R", Exhibit D2]**.

34. On 1 December 2012, SMI asked UI Bank for a renewal of its accounts 202110 (6 million Euro) and 202111 (14.5 million Euro) both with a deadline of 31 March 2014. The request

was confirmed. He understood the request from SMI was to finance its own loans to the 4 companies.

35. On 9 April 2014, UI Bank wrote to SMI asking for payment and advising that clauses 7 and 8 would be invoked as agreed and the funds would be off-set against the loan.

36. SMI still owes UI Bank the balance on UI Bank transferring the 4.5 million Euros deposited against the debt due to UI Bank of 9.5 million Euros plus interest. UI Bank owes no money to SMI and given it is struck off, there is no available money in any event.

37. The liquidators' request for insolvency dated 7 October 2014 stated that, "the letter of guarantee issued by UI Bank is not enforceable". In addition, each guarantee letter provided that the beneficiaries would notify UI Bank of the failure on each of the companies to pay the loan. The beneficiaries made no such notification to UI Bank.

E. Findings

38. Mr Pignatoro was the only witness cross-examined. I was able to make an assessment of his veracity and accuracy as a witness. He answered questions without hesitation. He did not change his evidence in cross-examination and explained his answers in re-examination. I accept that he was a witness of truth and accept his evidence.

39. The other witnesses' evidence was not challenged before me therefore I accept their evidence.

40. Between all 3 witnesses, the relevant documentary evidence was put into evidence. Besides internal consistency in a witness' account, I also looked for consistency between a witness' account and the documentary evidence, and considered the inherent likelihood, or not, of their accounts.

41. Mr Barrett and Mr Pavoncelli evidenced that the loans were by SMI directly to the 4 companies. This is consistent with the wording of UI Bank's letters of guarantee to SMI (three letters dated 8 November 2006 and one letter dated 30 May 2010) which stated, "In order to guarantee the reimbursement of the loan... granted by you to [named company]...". I accept therefore that the loans were by SMI to the 4 companies.

42. The 4 companies were all connected to Mr Pasquini.

43. The UI Bank's guarantees to SMI in respect of its loans to the 4 companies were by their terms "irrevocable until expiry" on 31 December 2020. They did not contain any provision for cancellation of the guarantees.

44. However, by letter to SMI dated 12 April 2012, UI Bank purported to cancel the guarantees. Mr Pasquini signed at the bottom of the letter. Mr Pignatoro evidenced that the hand-signing was in accordance with the practice in Italy that when receiving a

communication, the recipient hand-signs at the bottom with the date. This is the practice so that documents are not lost. Mr Pignatoro's explanation is consistent with the hand-writing on the letter therefore I accept as more likely than not that was why Mr Pasquini signed at the bottom of the letter rather than in acceptance of the cancellation of the guarantees.

45. I find therefore that the UI Bank guarantees were not cancelled.

46. The guarantees were payable "upon presentation of your written demand of payment... containing the statement that [the named company] does not have reimbursed you on expiry [sic]".

47. By letter dated 3 May 2013, SMI's liquidators demanded payment under the guarantees. The letter did not contain any statement that one or other of the 4 companies had not repaid its loan when required.

48. I find therefore that no valid demand was made for payment under the guarantees.

49. I now consider the inherent likelihood of the witnesses' accounts as to the guarantees themselves. Both Mr Barrett and Mr Pavoncelli evidenced that UI Bank acted as a bank operating at minimum exposure therefore to obtain a loan from the Bank, there had to be a sufficiently large deposit from the client to cover the loan. The fact is that SMI lodged just 4.5 million Euros with the UI Bank to enable it to obtain its 9 million Euros loan. Further, only 4.5 million Euros was deposited yet UI Bank issued guarantees totalling over 22 million Euros.

50. Mr Pavoncelli evidenced that it seems strange to deposit enough funds to cover a loan but the simple explanation is that the Bank was set up as Vanuatu was a tax haven at that time and the operation gave certain tax advantages to the Borrower (SMI). It avoided the need to pay tax on the interest payments. Mr Barrett evidenced that the UI Bank's guarantees were made presumably to justify the borrowing and to provide a bank guarantee for the 4 companies. Mr Pignatoro evidenced that the 4 companies were non-existent companies in tax havens.

51. The accounts of the 3 witnesses together point to a sham arrangement. Accordingly, it would be contrary to public policy to allow enforcement of the guarantees.

52. For the reasons given, the aspect of the Claim seeking to enforce the guarantees fails.

53. The remaining aspect of the Claim alleged unlawful use of client's money.

54. Mr Pignatoro acknowledged in cross-examination that the contract was between SMI and UI Bank only but that UI Bank kept separate accounts with separate client codes therefore UI Bank knew it was SMI's clients' money. However, there is no evidence in all of the

documentary evidence filed that the 4 companies had any contract with UI Bank or that they were customers of UI Bank.

55. I find therefore that UI Bank's customer was SMI and that the 4 companies that SMI loaned money to were not customers of UI Bank. Further, SMI had a number of different accounts with UI Bank which were identified by different codes relating to different customers of SMI but UI Bank's only customer was SMI.

56. SMI and UI Bank's relationship was governed by contract, which included the General Conditions set out in SMI's account opening forms.

57. Clauses 7 and 8 of the General Conditions expressly provided that the funds paid by SMI could be claimed by UI Bank even when SMI was subject to bankruptcy procedures.

58. By clause 7, UI Bank could use the deposited funds "to compensate any customer debt payable to the Bank." It was entitled to do so "whenever it deems it necessary and without any formalities" and "when the customer is subject to bankruptcy procedures, taking into account the binding link between customer debt and Bank credit items".

59. By clause 8, all accounts opened by SMI formed part of "a single, indivisible current account" and UI Bank had the right at any time to transfer debt items to accounts with a surplus balance, simply by issuing a statement.

60. Accordingly, the monies whether placed on deposit to guarantee the loan to SMI or lent to SMI, in however many separate accounts, all formed a single, indivisible current account.

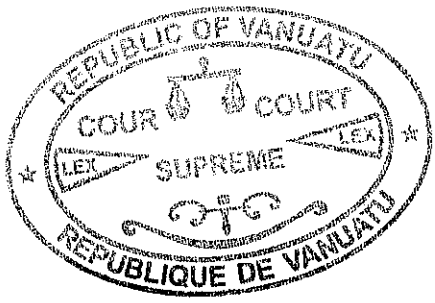
61. SMI did not ever negotiate or request that clauses 7 and 8 be deleted or amended.

62. The monies loaned to SMI in relation to the four companies were due on 31 March 2014. They were not paid. On 9 April 2014, UI Bank wrote to SMI asking for payment and advising that clauses 7 and 8 would be invoked as agreed and the funds would be off-set against the loan. It subsequently did so.

63. Therefore, when SMI defaulted on its debt with UI Bank, and even though SMI had been placed in liquidation (the time of commencement of winding up is deemed to correspond to the date of adjudication in bankruptcy), UI Bank properly applied the 4.5 million Euros on deposit against the unpaid debt pursuant to clauses 7 and 8 of the General Conditions of their contract.

64. Accordingly, there was no unlawful use of client's money as alleged.

65. For the reasons given, the Claim fails.



F. Whether or not costs be paid on an indemnity basis

66. A high threshold must be passed for costs to be awarded on an indemnity basis. The Court of Appeal stated in *Air Vanuatu (Operations) Ltd v Molloy* [2004] VUCA 17 that the awarding of indemnity costs arises only in "very extreme" cases.

67. Rule 15.5(5) of the *Civil* Procedure *Rules* provides:

> *15.5 The court may also order a party's costs be paid on an indemnity basis if:*
>
> *(a) the other party deliberately or without good cause prolonged the proceeding; or*
>
> *(b) the other party brought the proceeding in circumstances or at a time that amounted to a misuse of the litigation process; or*
>
> *(c) the other party otherwise deliberately or without good cause engaged in conduct that resulted in increased costs; or*
>
> *(d) in other circumstances (including an offer to settle made and rejected) if the court thinks it appropriate.*

68. I do not consider that the circumstances of this case fall within rule 15.5 or otherwise merit an indemnity costs order hence costs are ordered on the standard basis.

G. Result

69. For the reasons given, the Claim is dismissed.

70. Costs are to follow the event. I set them at VT250,000. The Claimant is to pay those within 21 days.

DATED at Port Vila this 6th day of April 2022
BY THE COURT

.....
Justice Viran Molisa Trief