IN THE SUPREME COURT OF THE DEMOCRATIC SOCIALIST REPUBLIC OF SRI LANKA

In the matter of an application under and in terms of Section 5C of the High Court of the Provinces (Special Provisions) Act No. 19 of 1990 as amended by High Court of the Provinces (Special Provisions) (Amendment) Act No. 54 of 2006.

Union Bank of Colombo Limited,
64, Galle Road,
Colombo 03.

Plaintiff

SC Appeal No: 98/2017
DC Colombo Case No. DR/1147
WP/HCCA/COL 226/09(F)
SC/HCCA/LA/ 494/2014

Vs.

1. David Pedurupillai Dominique,
   Kings Court,
   No. 4/5, Havelock Road,
   Colombo 05.

2. Nallathambi Naguleswaran,
   No. 5/1, "F" Block,
   Government Flats,
   Colombo 04.

3. Jagathlal Abeysinghe Gunawardene,
   No. 3, Sarasavi Road,
   Nugegoda.

4. Surendra Nadan Ravindran,
   No. 24, Circular Road,
   Mabole, Wattala.

Defendants

AND

1. David Pedurupillai Dominique,
   Kings Court,
   No. 4/5, Havelock Road,
   Colombo 05.

2. Nallathambi Naguleswaran,
   No. 5/1, "F" Block,
   Government Flats,
   Colombo 04.

1st and 2nd Defendants-Appellants

Vs.

Union Bank of Colombo Limited,
64, Galle Road,
Colombo 03.

Plaintiff-Respondent

3. Jagathlal Abeysinghe Gunawardene,
   No. 3, Sarasavi Road,
   Nugegoda.

4. Surendra Nadan Ravindran,
   No. 24, Circular Road,
   Mabole, Wattala.

Defendants-Respondents

AND NOW BETWEEN

Union Bank of Colombo PLC,
64, Galle Road,
Colombo 03.
(Formerly Known as Union Bank of Colombo Limited)

Plaintiff-Respondent-Petitioner

Vs.

1. David Pedurupillai Dominique,
   Kings Court,
   No. 4/5, Havelock Road,
   Colombo 05.

2. Nallathambi Naguleswaran,
   No. 5/1, "F" Block,
   Government Flats,
   Colombo 04.

1st and 2nd Defendants-Appellants-Respondents

3. Jagathlal Abeysinghe Gunawardene,
   No. 3, Sarasavi Road,
   Nugegoda.

4. Surendra Nadan Ravindran,
   No. 24, Circular Road,
   Mabole, Wattala.

3rd and 4th Defendants-Respondents-Respondents

Before: **Justice Buwaneka Aluwihare, PC**

Justice Kumuduni Wickremasinghe

Justice A.L. Shiran Gooneratne

Counsel: Dr. Romesh de Silva, PC with Shanaka L. Cooray for the **Plaintiff-Respondent-Petitioners.**

Suren de Silva with Vinodh Wickremasooriya for the **1st and 2nd Defendants-Appellants-Respondents**.

Argued on: 28/10/2022

Decided on: **17/02/2023**

A.L. Shiran Gooneratne J.

By Plaint dated 31/05/2005, the Plaintiff-Respondent-Petitioner (hereinafter sometimes referred to as 'the Plaintiff Bank') filed this action No. D.C. Colombo DR/1147 against the 1st and 2nd Defendants-Appellant-Respondents ('the 1st and 2nd Defendants') and the 3rd and 4th Defendant-Respondent-Respondents ('the 3rd and 4th Defendants'), under the Debt Recovery (Special Provisions) Act No. 2 of 1990 and sought to recover a sum of Rs. 3,128,247.54 together with interest against the said four Defendants.

In paragraphs 3 and 4 of the Plaint, the Plaintiff stated that the Plaintiff Bank, at the request of Nu-Tech Engineering (Pvt) Ltd, (hereinafter sometimes referred to as 'the borrower Company'), by Agreement dated 02/09/1998, a copy of which is annexed to the Plaint marked 'P2', granted a banking facility in a sum of Rs. 2.5 million, to the borrower Company to finance working capital requirements and that at all times material to this action, the 1st and 2nd Defendants along with the 3rd and 4th Defendants were directors of the said company.

The relevant part of 'P2' is as follows:

"Banking Facilities

We, the Union Bank of Colombo, are pleased to offer the following banking facility on terms and conditions stipulated below:

Borrower: Nu-Tech Engineering (Pvt) Ltd.

1. Overdraft of Rs. 2,500,000/- (Rupees Two Million Five Hundred Thousand Only)

   Purpose: To finance working capital requirements.

   Interest rate: 20% p.a.

Security and other documentation

The following security documentation is required in connection with the facilities being offered and should be perfected prior to their use.

1. Personal Guarantee of Directors for Rs. 2,500,000/-
2. Demand Promissory Note for Rs. 2,500,000/-
3. Mortgage over motor vehicles for Rs. 2,500,000/- together with comprehensive insurance policies assigned to us covering the vehicles mortgaged and valuation reports issued by a reputed valuer.
4. Certified copy of resolution passed by your Board of Directors, authorizing the Company to borrow".

The borrower Company accepted the banking facility in 'P2' and at a meeting held on 03/09/1998 its Board of Directors passed a resolution authorizing such borrowing, and the 1st to 4th Defendants are said to have signed a Joint and Several Guarantee in respect of such banking facility, copies of which are annexed to the Plaint marked 'P2a' and 'P3' respectively. [The copy of the Guarantee (P3) does not show the signature of the 3rd Defendant, though an Attorney at Law has confirmed that the effects of renunciation in terms of Clause 16 was explained to all persons named in the Guarantee (P3)].

In paragraphs 8 and 9 of the Plaint, the Plaintiff Bank states that, on the request of the borrower Company, the Plaintiff Bank rescheduled the existing outstanding overdraft facility, in terms of document marked (P4) annexed to the Plaint, and that

the said Joint and Several Personal Guarantee (P3) signed by the Defendants securing the said facility remained valid and binding in law subject to and until the repayment of the outstanding monies due to the Plaintiff Bank by the said borrower Company.

The relevant part of 'P4' is as follows:

"Banking Facilities

We, the Union Bank of Colombo, are pleased to offer the following restructured banking facility on terms and conditions stipulated below:

Borrower: Nu-tec Engineering (Pvt) Ltd.

1. Facility: Term Loan

   Amount: Rupees Two Million Five Hundred Thousand Only. (Rs.2,500,000/-)

   Purpose: To reschedule the current overdraft outstanding.

   Repayment: Repayable in 35 monthly installments of 70,000/- and a final installment of Rs. 50,000/-. Interest should be serviced on a monthly basis.

   Rate: 20% p.a.

The following security documentation is required in connection with the facilities being offered and should be perfected prior to their use.

1. Mortgage for Rs. 1.6 million over machinery together with comprehensive insurance policies assigned to us, covering the machinery mortgaged. (**Already in place**).
2. Mortgage for Rs. 0.9 million over motor vehicles together with comprehensive insurance policies assigned to us, covering the vehicles mortgaged. (**Already in place**).
3. Personal guarantee of directors for Rs. 2.5 million.
4. On Demand Promissory note for Rs. 2.5 million."

(Emphasis is mine)

The borrower Company accepted the banking facility in 'P4' and at a meeting held on 12/05/2000 its Board of Directors passed a resolution authorizing such borrowing, a copy of which is annexed to the Plaint marked 'P4(a)'.

Claiming, in Paragraph 10 of the Plaint, that the borrower Company has made default in the repayment of the said banking facility, the Plaintiff Bank ("after giving credit for all payments made by the Debtor Company") has filed this action as aforesaid, for the recovery of the said sum of Rs. 3,128,247/54, together with interest at the rate of 32% p.a.

Being satisfied with the evidence placed before court, the learned District Judge issued decree nisi dated 27/07/2005 in favour of the Plaintiff Bank and required the Defendants to show cause as to why the said decree nisi should not be made absolute.

The 1st and 2nd Defendants filed their objections dated 06/10/2008 and stated *inter alia*, that Nu-Tech Engineering (Pvt) Ltd. obtained loan facilities in a sum of Rs. 2.5 million, subject to the terms and conditions set out in the document marked 'P2', and that the 1st and 2nd Defendants as Directors of the said borrower Company signed the said Guarantee marked 'P3'.

In paragraph 10 of the said objections, the Defendants state that the document marked 'P4' is a new agreement and, in terms and conditions set out in 'P4', the Plaintiff Bank *inter alia*, required the borrower Company to furnish a new Personal Guarantee of the Directors of the borrower Company, prior to the use of the said facility, as documentation required in connection with the new facility offered. The said Defendants further contended that by its own conduct the Plaintiff Bank is now estopped from stating that 'P3' covers the rescheduled agreement marked 'P4' and prayed for the dismissal of the Plaint.

Having considered the pleadings and the written submissions tendered by the respective parties, the learned Additional District Judge by order dated 25/09/2009, made the said decree *nisi* absolute.

Being aggrieved by the said order, the 1st and 2nd Defendants by their Petition of Appeal dated 11/11/2009 appealed to the High Court of the Western Province exercising civil appellate jurisdiction holden in Colombo ("the Appellate Court").

The Appellate Court by Judgment dated 22/08/2014, set aside the said order made by the learned Additional District Judge dated 25/09/2009 and *inter alia*, declared that the restructuring or rescheduling of the overdraft facility by converting it to a term loan (P4) comes within the interpretation of novation and that the Guarantee Bond marked 'P3' came to an end with the novation, therefore, a cause of action cannot be said to have accrued to the Plaintiff to sue the Defendants.

The Plaintiff Bank, by its Petition dated 03/10/2014, is before this Court, to set aside the said Judgment dated 22/08/2014, delivered by the Appellate Court.

By Order dated 22/05/2017, this Court granted leave to appeal on the following questions of law.

1. Has the learned High Court Judges failed to see that the 'principle of novation' is not applicable at all to the facts and circumstances of this case and thereby grossly misdirected themselves in facts and in law in deciding this matter?
2. Did the Judges of High Court failed to consider that the learned District Judge has correctly considered the fact that it is the same "facility" that was rescheduled and/or restructured at the request of the Defendants and there was no new grant of a facility to the said Company?

The learned Counsel for the 1st and 2nd Defendant-Appellant-Respondents raised the following consequential questions of law.

3. By the reason of the failure on the part of the Plaintiff to obtain a fresh guarantee in terms of the document 'P4', is the Plaintiff entitled to pray for judgment against the 1st and 2nd Defendants?
4. Is the judgment of this Court in the case of **Hatton National Bank Vs. Rumeco Industries Limited in SC. Appeal No. 99A/ 2009** applicable to the facts of the present case?

In this action, the main issue to be decided by this Court is, whether there is a novation of the overdraft facility granted to the borrower Company (P2), by the rescheduled facility (P4), and the applicability or the non-applicability of the Joint and Several Personal Guarantee (P3) to the rescheduled facility in 'P4'.

The 1st and 2nd Defendant's position is, that P4 was not a mere variation of the existing terms and conditions of repayment of the existing overdraft facility, but a completely different banking facility, which created new obligations, and which amounts to a novation of P2. And as such, the Defendants contend that P4 is a new agreement, a novation of the banking facilities already provided to the borrower Company in terms of P2. P4 offered the borrower Company a 'term loan' which was repayable through monthly installments.

The Plaintiff Bank takes up the position, that there was no novation and the parties intended to continue the same relationship with the same terms and obligations subject to the concession given to the Defendants to pay in installments and that a restructuring or a rescheduling does not amount to a change that is so fundamental that P4 stands independently to P2. It is also contended that, even if there was novation, the relevant guarantee together with the obligation to pay remained in force and applicable until the totality of what is due has been settled.

It is not in dispute that the Board of Directors of the borrower company resolved by its resolution (P2(a)), to obtain an overdraft facility up to a limit of Rs. 2.5 million from the Plaintiff Bank and, prior to the use of the overdraft facility a Joint and Several Personal Guarantee (P3) was signed by the Defendants securing the said facility. It is also not in dispute that due to financial difficulties, the borrower Company defaulted to settle the said facility as agreed, and that a term loan facility was granted to the borrower Company to be repaid within the time period, at the rate of interest, on the security and upon terms and conditions, as set out in the offer letter (P4) and the requirement to tender the security documentation prior to the use of the said facility, as also mentioned previously.

In regard to Novation, both the Plaintiff Bank, on the one hand, and the 1st and 2nd Defendants, on the other, have quoted extensively in the written submissions filed by them, in the Appellate Court and in this Court, and annexed pages from "The Law of Contracts" Volume 11, pages 718 to 720, (Sections 751 to 753) by C. G. Weeramantry, and therefore only the following quotations briefly, from "The Law of Contracts" are included herein –

(i) *"In its (Novation) wider sense it means the creation of a fresh contract by the extinction of a pre-existing one in whose room it stands,"*

(ii) "Novation in its wider sense is of four varieties –

(a) The substitution of a new debt for an existing debt.
This is known as "novation proper"

(iii) "Where there is a novation of a contract, there comes into existence in the eye of the law a new and independent contract,"

(iv) "A new obligation must be created which contains some element not found in the earlier obligation……. The grant by the creditor of an extended time to the debtor for payment thus does not constitute a novation, nor does the grant of an additional security or the mere conformation of an original agreement",

(v) "A novation discharges not only the original obligation but all obligations accessory to it. Interest, penal charges, suretyships and pledges, accessory to the original contract, are thus all discharged", (The Privy Council case of Palaniappa Vs. Saminathan 17 NLR 56, is cited in support of this contention; which judgement states at page58 that, "No matter what were the respective rights of the parties, inter se, they are abandoned in consideration of the acceptance by all of a new agreement. The consequence is, that when such an accord and satisfaction takes place the prior rights of the parties are extinguished. They have in fact been exchanged for the new rights; and the new agreement becomes a new departure and the rights of all the parties are fully represented by it"),

(vi) "Novation is never presumed, for the law considers that a contract once established retains its binding force, and that a creditor does not intend to surrender the rights he has acquired under the earlier contract. It follows that the law will incline to the view that a later contract co-exists with, rather than supersedes, a former contract, unless the court is satisfied of an intention on the part of the parties to supersede and extinguish the earlier contract."

In making the said Order, dated 25/09/2009, in D.C. Colombo case No. DR/1147, *inter alia*, holding that there was no Novation in the instant case, the learned Additional District Judge relied on the Court of Appeal Case of **Ran Banda and Others Vs. the People's Bank, (2004) 2 SLR 31** which held as follows.

"The first defendant- petitioner obtained a loan of Rs.20 million from the People's Bank. As the payments were not regular, the loan was rescheduled and the first

defendant-petitioner accepted the rescheduled programme. When the first defendant-petitioner failed to settle the loan in terms of the rescheduled arrangement, the bank filed action under and in terms of the provisions of the Debt Recovery (Special Provisions) Act. It was contended that the bank had no right to seek to recover any sum of money upon the rescheduled agreement and the guarantors (2nd and 3rd defendants) were not liable, as the original contract had become invalid".

The District Court granted the Defendant-Petitioners leave to defend on the Petitioners depositing Rs.10 million as security.

On leave being granted the Court of Appeal –

Held:

(i) Novation proper takes place if a new contract to take the place of the old is established between the same parties without the intervention of a 3rd party; When this happens the latter obligation extinguishes the former.

(ii) The rescheduled arrangement was made at the request of the debtor, the 1st defendant-petitioner, it merely gives him extended time for payment and a concessionary rate of interest in respect of the balance of the loan remaining unpaid.

Per Amaratunga, J

(i) This did not bring into existence anything unfavourable to the guarantors, in fact concessions granted to the debtor were beneficial to the guarantors as well.

(ii) Condition No.4 in the rescheduled agreement preserved the Bank's rights to have recourse to the conditions of the original agreement in the event of the failure of the debtor to act in accordance with the conditions of the rescheduled agreement.

(iii) This is not a new obligation extinguishing the existing contract".

Upon a comparison of the facts, referred to in the judgment in the case of **Ran Banda Vs. the People's Bank**, with those in the instant case, it would be observed that -

(a) The rescheduled arrangement in the case of Ran Banda Vs. the People's Bank is said to have granted the borrowing company (the 1st defendant-petitioner) an extended time to repay the money mentioned in the rescheduled arrangement. In the instant case, P2 dated 2/09/1998 referred to an overdraft facility, which was repayable on demand, which "facility will expire and be subject to review on 31/08/99" (that is, a period of about 12 months from the date of P2), and P4 dated 20/04/2000, in the instant case, referred to a term loan repayable in 35 monthly instalments of Rs.75,000/- and a final instalment of Rs.50,000/- (that is, a period of 36 months) but such "Facility" is subject to review on 30/09/2000", (that is, a period of about only 5 months from the date of P4). The Clause relating to "Repayment," in P4, states that "in the normal course, you may rely upon the facility being available until 30/09/2000 but we are sure you will appreciate that in accordance with normal banking practice, that the above facility is repayable on demand and that we reserve the right to ask for repayment if circumstances arise, which in our opinion justify our doing so". Consequently, P4 itself creates, at least, a doubt as to the period of repayment thereunder.

(b) The rescheduled arrangement in the case of Ran Banda Vs. the People's Bank is said to have granted the borrowing company a concessionary rate of interest. In the instant case, both P2 and P4 refer to the rate of interest as "20% p.a.," but the Plaintiff-Bank has reserved "the right to effect any changes in the rates of ….. or interest quoted herein if circumstances arise, which in our opinion justify our doing so".

It would be observed that the said Plaint dated 31/05/2005, filed by the Plaintiff Bank, in D.C. Colombo DR/1147, "(after giving credit for all payments made by the debtor company)", prayed for the recovery of a sum of Rs.3,128,247/54, together with interest at 32% p.a.

The Plaintiff Bank annexed to its Plaint, a Statement dated 08/04/2005, marked P9, which only stated that "The total amount due to the Union Bank of Colombo Ltd. as at 05th March 2005 is Rs.3,128,247/54 together with further interest thereon, all legal and other charges and expenses upto the date of settlement in full."

Such Statement, marked 'P9', does not contain other details, such as the payments made by the borrower company, the rates and amounts of interest levied by the Plaintiff Bank from time to time etc.

In the instant case, there does not appear to be "a concessionary rate of interest" levied by the Plaintiff Bank, as in the case of Ran Banda Vs. the People's Bank.

(c) The rescheduled arrangement in the case of Ran Banda Vs. the People's Bank is said to have, as Condition 4, provisions which preserved "the Bank's rights to have recourse to the conditions of the original agreement in the event of the failure of the debtor to act in accordance with the conditions of the rescheduled arrangement" and this, in the opinion of the Court, "completely negatives any intention on the part of the Bank to make the rescheduled arrangement to take the place of a new contract – a new obligation extinguishing the existing contract",

'P4', in the instant case, does not contain any similar provision.

Accordingly, it is clear that the facts in the case of Ran Banda Vs. the People's Bank can be differentiated from the facts of the instant case and that the learned Additional District Judge has erred in applying, in D.C. Colombo Case No. DR/1147, the decision in the case of Ran Banda Vs. the People's Bank, which is not applicable in the instant case.

In its Judgement dated 22/08/2014, the Appellate Court has considered the provisions in P2 and P4 (some of which have also been referred to earlier, in regard to the discussion relating to the case of Ran Banda Vs. the People's Bank) and come to the conclusion that *"On the face of these two agreements (that is, P2 and P4) it can in no sense be interpreted as a continuation of the earlier agreement" and, accepting the view of the learned Counsel for the 1st and 2nd defendants, agreed that "there is a novation of the earlier overdraft facility granted to Nu -Tec Engineering (Pvt) Ltd".*

The Appellate Court also referred to the agreement of the Plaintiff Bank to restructure the overdraft facility by converting it into a term loan on the terms stated in P4, quoted the relevant part of P4 (which has also been quoted earlier in this Judgment), regarding the relevant security documentation required in connection

with the facilities being offered (by P4), which should be perfected prior to their use, and referred to the use of the words "(Already in place)", in regard to the mortgage for Rs.1.6 M over machinery and the mortgage for Rs.0.9M over motor vehicles; and the non-use of the said words "(Already in place)" in regard to the "Personal guarantees of directors for Rs. 2.5M," and stated that, *"The Plaintiff has however agreed to continue with the existing two mortgages. Their intention is very clearly reflected on the document P4, because the plaintiff has at the end of the 1st and 2nd conditions stated the words "Already in place". For reasons best known to the Plaintiff Bank it has not included these words in the 3rd clause (relating to the personal guarantee of the directors). In the circumstances the only conclusion one could arrive at is that the plaintiff Bank expected the defendants to enter into a new guarantee bond before making use of the facility granted to the company of which they were directors". (In paragraph K of their further written submissions dated 14/07/2014, filed in the Appellate Court, the 1st and 2nd Defendants have also submitted that "The Plaintiff in their further submissions (as well as in the initial written submissions) have continued to avoid explaining to Court as to why the Bank did not place the words 'already in place' as done in items i and ii)".*

The Appellate Court for the reasons mentioned therein, held that *"the guarantee bond (P3) also came to an end with the novation of the overdraft facility and therefore a cause of action cannot be said to have been accrued to the plaintiff to sue the defendants. The appeal of the 1st and 2nd defendants-appellants is accordingly allowed and the action of the plaintiff is dismissed",*

In the case of **Hatton National Bank Limited Vs. Rumeco Industries Limited and two others, SC Appeal No. 99A/2009**, Hatton National Bank Limited (the Plaintiff-Appellant) granted a Term Loan, in 1992, to Rumeco Industries Limited (the 1st Defendant-Respondent), which was guaranteed by the 2nd and 3rd Defendants-Respondents. Thereafter, the said loan was rescheduled on 28/05/1995 and was secured by two mortgage bonds. The Plaintiff-Appellant filed action against the Defendants claiming the sum of money in default and also sued the 2nd and 3rd Defendants-Respondents as guarantors. (The 1st and 2nd Defendants-Respondents failed to appear before court and an ex parte judgement was delivered against them. The 3rd Defendant-Respondent filed answer).

The 3rd Defendant-Respondent took up the position that he had guaranteed the repayment of the term loan granted in 1992 and did not guarantee the repayment of the rescheduled loan of 1995 and therefore, was not liable to be sued on the guarantee.

The Plaintiff-Appellant tried to show that the guarantee given by the 3rd Defendant-Appellant, in 1992, was a continuing guarantee, which covered all facilities granted to the 1st Defendant-Respondent.

The learned District Judge dismissed the case of the Plaintiff-Appellant against the 3rd Defendant-Respondent on the basis that the transaction sued upon was the term loan granted in 1995 and that it had not been guaranteed by the 3rd Defendant-Respondent. The Plaintiff-Appellant appealed against the said judgment to the Provincial High Court. The Provincial High Court examined the law relating to novation of contract and arrived at the conclusion that there was a novation of the earlier loan granted by the Plaintiff-Appellant and that term loan was a new contract.

The Provincial High Court cited the Law of Contracts – by CG Weeramantry at page 719, which is quoted earlier in this Judgment, and also referred to the decision in **Palaniappa Vs. Saminathan (17 NLR 58)** which is also referred to in this Judgment. The Provincial High Court by its judgment dated 16/12/2008, dismissed the said Appeal.

Upon appeal to this Court, Suresh Chandra J. held that,

"On a consideration of the evidence, the documents, the proceedings and the judgments of the District Court and the High Court, it is quite clear that the action brought to court by the plaintiff specially against the 3rd defendant was based on the term loan granted in 1995 and that the guarantee given by the 3rd defendant in 1992 cannot be considered as a continuing guarantee. In view of this position, the grounds on which leave was granted by this Court have to be answered in the negative".

Accordingly, the Appeal to this Court was dismissed and the said Judgment of the High Court and that of the District Court were affirmed.

Referring to paragraph 6 of the Guarantee (P3), in its written submissions dated 16/11/2022 filed in this Court, the Plaintiff Bank claimed that the Guarantee (P3)

was a continuing guarantee and remained as security against the 1st and 2nd Defendants until the moneys borrowed by the borrower Company from the Plaintiff Bank remains unsettled.

Paragraph 6 of the Guarantee (P3) states as follows –

"This guarantee shall be binding on and remain in force and be enforceable at all times against and shall continue to be a security against each of us and the estate of each of us notwithstanding the death or disability of any of us until the whole of the moneys aforesaid shall have been fully liquidated and paid to you and shall be irrevocable by us or any of us or any of our heirs executors or administrators".

The Plaintiff Bank further states that –

(1) "The Plaintiff did not at any time, either by in writing or by act or deed, express any intention to relinquish their rights or discharge the Defendants from their obligation,"

(2) "The fact remains that the borrowed sum is still unsettled, and the Defendants are attempting to avoid this responsibility by hiding behind P4".

(3) "It is submitted that in the circumstances, even if there had been a "novation," this does not affect the Defendants obligation to pay the plaintiff", and

(4) "Therefore, it is submitted that the Civil Appellate High Court erred in law as it failed to consider this most vital fact, which is that even if there was a novation, the relevant guarantees together with the obligation to pay, remained in force and applicable up until the totality of what is due has been settled."

In this regard, it is observed that –

The first recital of the Guarantee (P3), which is addressed to the Plaintiff Bank, refers to the agreement by the Plaintiff Bank to grant to the borrower Company, a loan of Rs.2,500,000/-, "subject to the terms and conditions contained in your letter dated [the date of the letter is left blank in the copy of the Guarantee (P3)] addressed to the Obligor (the borrower Company) (hereinafter referred to as "the said Loan") and that the Guarantors therein, (that is, 1st to 4th Defendants, who are the directors of the borrower Company), "do hereby agree to furnish to you an undertaking for the payment of the said loan". (The undated letter, referred to in the above-

mentioned Guarantee dated 07/09/1998, is obviously the letter dated 02/09/1998 (P2), and cannot be a reference to the subsequent letter dated 20/04/2000 (P4).

Paragraph (6) of the Guarantee (P3), which is referred to by the Plaintiff Bank, and which is quoted above, states clearly that the liability of the first and second Defendants, thereunder remained until the whole of "the moneys aforesaid" shall "have been fully liquidated and paid to you ……".

The term "moneys aforesaid" has been defined in paragraph 1 of the Guarantee (P3), to mean "the said Loan together with interest thereon at such rate or rates as may be charged by you and all legal and other charges and expenses whether taxable or not occasioned by or incidental to the enforcement of this or any other security for the said Loan or the recovery thereof";

Therefore, it is clear that the liability of the 1st and 2nd Defendants, under the Guarantee (P3), related only to "the said Loan "which is defined, as above-mentioned;

Further, the 1st and 2nd Defendants were not parties to P4. The 1st and 2nd Defendants have not, in anyway, consented to be personally liable to the banking facility, referred to in P4. The significance of the absence of the words "Already in place", in P4, in respect of the "Personal guarantee of directors for Rs.2.5 M", [whilst such words "Already in place" have been included, in respect of the mortgages over the machinery and the motor vehicles, in (P4)], has already been commented upon earlier in this Judgment. P4 does not mention any liability of the 1st and 2nd Defendants, in respect of the banking facility referred to in P4.

The effect of a Novation, in regard to security documents executed in respect of the previous banking facilities, has also been discussed earlier in this Judgment. Therefore, the claims of the Plaintiff Bank that the Guarantee (P3) is binding on the 1st and 2nd Defendants until what is due from the borrower Company to the Plaintiff Bank has been settled, and that "even if there had been a 'novation', this does not affect the Defendants' obligation to pay the Plaintiff Bank, cannot be accepted.

Accordingly, I answer the 1st, 2nd and 3rd questions of law on which leave to appeal has been granted in the negative and the 4th question of law in the affirmative.

For these reasons, this Appeal of the Plaintiff Bank is dismissed; the Judgement of the Appellate Court is affirmed; and that of the District Court is set aside. No order for costs.

Judge of the Supreme Court

Buwaneka Aluwihare, PC. J

I agree

Judge of the Supreme Court

Kumuduni Wickremasinghe, J

I agree

Judge of the Supreme Court