

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

S.C. (CHC) Appeal No. 36/2004  
CHC Case No. 169/2002(1)

CIC Feeds (Pvt) Limited (formerly)  
Known as Nutrena (Pvt) Limited of  
No. 252, Kurunduwatta Road, Ekala.

**PLAINTIFF**

Vs.

Pan Asia Bank Limited of No. 450,  
Galle Road, Colombo 3.  
And having a branch office at 1334,  
Kotte Road, Rajagiriya.

**DEFENDANT**

**AND NOW**

CIC Feeds (Pvt) Limited (formerly)  
Known as Nutrena (Pvt) Limited of  
No. 252, Kurunduwatta Road, Ekala.

**PLAINTIFF-APPELLANT**

Vs.

Pan Asia Bank Limited of No. 450,  
Galle Road, Colombo 3.  
And having a branch office at 1334,  
Kotte Road, Rajagiriya.

**DEFENDANT-RESPONDENT**

**BEFORE:** S.E. Wanasundera P.C., J.  
Priyantha Jayawardena P.C. J. &  
Anil Gooneratne J.

**COUNSEL:** Prasanna Jayawardena P.C., with Milinda Jayatilleke  
For the Plaintiff-Appellant

S.A. Parathalingam P.C., with Varuna Senadheera  
For the Defendant-Respondent

**ARGUED ON:** 17.09.2015

**DECIDED ON:** 16.03.2016

**GOONERATNE J.**

This was an action filed on or about 28.03.2001 against the Defendant Bank by the Plaintiff Company, carrying on business of manufacturing and marketing Animal Feed, for the recovery of a sum of Rs. 8,000,000/- with interest thereon upon the 1<sup>st</sup> cause of action/the five alternative causes of action as pleaded in the plaint. Learned High Court Judge of Colombo dismissed the plaint with costs on 24.3.2004. This appeal to the Supreme Court arise from the Judgment of the said date of the Colombo High Court.

The Attanagalla Livestock Development Company (Pvt) Limited was

a customer of the Plaintiff Company who purchased animal feed from the Plaintiff Company on credit. The above named purchasing company was not a party to the suit. (hereinafter referred to as ALDC). ALDC was a customer of the Defendant Bank, and the Plaintiff Company was a customer of Citibank and Citibank provided facilities to the Plaintiff Company such as post-dated cheque discounting and purchasing facility. This facility enabled the Plaintiff Company to present post-dated cheques (issued in favour of Plaintiff Company) to Citibank and the Bank gave immediate credit upon these post-dated cheques. However if the post-dated cheques were dishonoured on the due date, Plaintiff was liable to pay the value of such cheque to the Citibank. ALDC who was a customer of the Plaintiff Company having purchased animal feed from the Plaintiff Company, gave post-dated cheques to Plaintiff Company, who presented the cheque to Citibank and obtained credit for same.

The above method of transacting business was not disputed by either party. At the hearing of this appeal both learned President's Counsel admitted certain basic facts, and referred to correspondence between parties and letters written and received by ALDC. The real issue arose on or about June 1999, when ALDC was called upon to make arrangements with the Defendant

Bank to issue a bank guarantee for Rs. 8,000,000/- in favour of Citibank NA. This would secure Citibank against any dishonour of post-dated cheques, presented by ALDC, and enable Citibank to recover payment upon the guarantee.

I would at this point of this judgment refer to the case of the Plaintiff-Appellant based on oral and written submissions of learned President's Counsel for Plaintiff-Appellant, notwithstanding the fact that the plaint filed in the original court disclose several causes of action. It was submitted that, if and when cheques issued in favour of the Plaintiff-Company by ALDC were dishonoured, Plaintiff Company would be liable to pay the value of the cheque to Citibank NA (Plaintiff bank). As such ALDC would make arrangements for the Defendant-Bank to issue a Bank guarantee for Rs. 8,000,000/- in favour of Citibank N A which would enable such guarantee to secure Citibank against dishonoured cheques. In order to enable ALDC to obtain this guarantee from the Defendant Bank, Plaintiff Company would pay the Defendant Bank. Rs. 8,000,000/- so that this sum of Rs. 8,000,000/- would be held by the Defendant Bank as security for the issue of the aforesaid guarantee.

The way the facts were presented by learned President's Counsel for the Plaintiff-Appellant, who rely heavily on the requests to issue a guarantee as stated above, to make the Defendant-Respondent liable in the transaction, the following matters are also noted by this court.

- (a) Plaintiff-Appellant issued a cheque for Rs. 8,000,000/- in favour of the Defendant Bank ('A' filed with plaint).
- (b) By 17.06.1999 Plaintiff Company sent the cheque 'A' to Defendant Bank along with the format of the intended Bank Guarantee and a request to the Defendant Bank to issue the Bank Guarantee (B1 & B2).
- (c) By letter marked 'C' dated 18.06.1999, Defendant Bank acknowledged receipt of cheque 'A' and letter and the format of guarantee, marked B1 and B2. Letter 'C' also states Bank Guarantee could be issued on realisation of cheque and subject to completion of documents.
- (d) The above cheque 'A' realised for payment on 21.06.1999 and the Defendant Bank received payment of a sum of Rs. 8,000,000/-.
- (e) By letter marked 'D' dated 20<sup>th</sup> July 1999 by Defendant to Plaintiff Company the Defendant Bank informed the Plaintiff Company that the Bank is unable to issue a guarantee since ALDC has not completed relevant documentation. In the written submissions of the Appellant it is stated that as at the date of filing action Defendant Bank had not issued the requested Bank Guarantee, and had also not returned the sum of Rs. 8,000,000/- which had been paid by the Plaintiff Company to the Defendant Bank on 02.08.1999, had advised the Plaintiff Company that the Defendant Bank released the said sum of Rs. 8,000,000/- to ALDC. The ALDC had not paid the said sum to Plaintiff.

The main argument presented based on the first cause of action was that there was an implied or express agreement and or undertaking or contact between the Plaintiff Company and the Defendant Bank as the Defendant Bank would retain the said sum of Rs. 8,000,000/- to provide security for the guarantee and when such guarantee was not issued by the Defendant Bank, there was a breach of an undertaking or contract as the Bank failed to retain the said sum and issue a guarantee, and thus also failed to return the said sum to the Plaintiff Company. I will also refer to the other alternate causes of action relied upon by the Plaintiff Company, in a gist as follows:

- (1) Plaintiff Company is entitled to recover the said sum of Rs. 8,000,000/- and the Defendant Bank has completely failed to carry out its obligation and as such there is a total failure of consideration.
- (2) Defendant Bank was in breach of its duty. When monies were received as aforesaid by the Defendant Bank, it had a duty to retain the amount received and issue the guarantee or return the said sum to Plaintiff Company. Failure to do so amounts to a neglect to perform its duty, and caused a loss of Rs. 8,000,000/- to the Plaintiff Company.
- (3) In breach of duty of care and negligently/wrongfully failed to retain the said sum which sum was under the control of the Defendant Bank and thereby caused a loss of Rs. 8,000,000/-.

(4) Defendant Bank held the said sum for the benefit of the Plaintiff Company as a trustee and or constructive Trust.

(5) Defendant Bank had been unjustly enriched.

At the hearing of this appeal, it also transpired that evidence was led as regards agreement marked P5 between, the Plaintiff Company and ALDC.

Clause 3:2 of P5 reads thus:

The Company shall provide a further loan of Rupees Eight Million (Rs. 8,000,000/-) in the form of a cheque to be issued in favour of Pan Asia Bank Ltd. The interest charged on this loan shall be 18% per annum.

The said agreement P5 refer to an Arbitration Clause (Clause 7). It was also submitted by learned President's Counsel for Defendant-Respondent-Respondent that Arbitration proceedings have been initiated to recover the said sum from ALDC by the Plaintiff Company. However the Arbitration proceedings were pending and not concluded as at the date of conclusion of the trial in the High Court.

The learned President's Counsel for the Defendant-Respondent-Bank in his submissions emphasised the relationship between the Plaintiff-Company and ALDC with reference to agreement P5 which was entered

between the said parties on or about June 1999, and crucial to the case in hand. By P5 Plaintiff Company agreed to sell animal feed to ALDC upon credit facilities. Defendant-Bank was not a party or privy to the agreement P5. I have already discussed the arrangement to give post-dated cheques by ALDC to Plaintiff Company. Even this fact was emphasised by learned President's Counsel with the consequences that would result in such arrangement. He also referred to certain items of evidence that transpired from the Plaintiff witness who was the only witness at the trial, before the High Court. In pursuance of above arrangement Plaintiff requested ALDC to provide a Bank guarantee for Rs. 8,000,000/- from ALDC banker, who was the Defendant Bank. Evidence reveal that Plaintiff agreed to give ALDC a loan for Rs. 8,000,000/- to enable ALDC to arrange the issue of a Bank guarantee with ALDC. Plaintiff company based their case according to learned President's Counsel on the cheque (P6) drawn by Plaintiff and that it was common ground that it furnished Rs. 8,000,000/- to ALDC according to Agreement P5. He draw the attention of this court to clause 3.2 of P5, referred to above.

The only witness who gave evidence inter alia stated the following:

It was agreed between the Plaintiff Company and ALDC to grant a loan of Rs. 8,000,000/- at the rate of 18% on the loan until payment in full apart from other facilities granted to ALDC by Plaintiff Company. Witness also

admitted that the said sum was advanced by the Plaintiff Company for and on behalf of ALDC, and referred to the letter P7 to confirm that Citibank cheque for Rs. 8,000,000/- was given on behalf of ALDC.

P6 & P7 taken together explains that the cheque had been forwarded on behalf of ALDC and proceeds of the cheque were collected by the Defendant Bank in the ordinary course of business to the credit of the account of ALDC maintained with Defendant Bank (P8 confirm same) It is also clear that cheque P6 was a loan extended by Plaintiff Company to ALDC as per agreement P5. Witness of the Plaintiff Company admitted this fact. The proceeds of the loan is money belonging to the recipient the ALDC. Only ALDC is entitled to utilise the money received by the Bank to utilise it for the agreed purpose.

I have also noted the submissions of learned President's Counsel on another point that the sum of Rs. 8,000,000/- is a debt owing from ALDC to Plaintiff Company. Learned President's Counsel also submitted that Defendant Bank never gave any undertaking and/or entered into a contract with the Plaintiff Company and/or ALDC to issue a Bank guarantee unconditionally, upon the receipt of the money. It was also submitted that Plaintiff Company had suppressed the fact of proceeding to arbitration against ALDC, prior to institution of this action.

One of the matters that need to be kept in mind is that the contract of guarantee which is described as an 'accessory contract', and which is an universally acceptable meaning of payment equivalent to cash in trade and commerce, on the basis that the promise of the issuing bank to pay was wholly independent of the underlying contract between parties. Although that could be taken as the simplest explanation to a contract of guarantee, in the case in hand the Defendant Bank never issued a guarantee in favour of ALDC, for the reason adduced by the Defendant Bank. Plaintiff Company no doubt, attempts to establish their case based on an undertaking and or express or implied agreement to issue a guarantee by the Defendant Bank to claim the relief prayed for as per the plaint filed of record. I have to accept that the Bank did not issue the guarantee due to the reason that the required documentation was not forthcoming from ALDC. As such the issue of the guarantee was conditional upon the receipt of proper documentation. It is fundamental to this type of transaction that the Banker need to take all necessary precautions, and be satisfied for cogent reasons, upon the guarantor's ability to pay when called upon and the willingness to settle. Banks will be cautious to enter into such a guarantee unless it is based on confidence and trust of the client. Banker's point of view need to be considered since it is more appropriate to take all

precautions, to avoid any doubt and make sure that clients follow proper procedures before accepting or issuing a guarantee.

It is also necessary to consider the following matters which need to be taken note, to ascertain as to whether a cause of action accrued to the Plaintiff Company to sue the Defendant Bank to recover the sums of money referred to in the plaint. Does the set of facts placed before court indicate an emergence of a separate agreement other than P5? (Based on P6, P7, P7A & P8) or whether there had been a total failure of consideration or want of consideration.

I note the following.

- (1) Agreement P5 as stated above (clause 3:2) Plaintiff Company to provide a loan of Rs. 8,000,000/- in the form of a cheque issued in favour of Pan Asia Bank Limited
- (2) As in P5 (clause 4:1) customer (ALDC) agrees, covenants and undertake to provide a Bank guarantee in favour of the Company for Rs. 8,000,000/- from Pan Asia Bank Ltd. Within three working days of issuing the above cheque.
- (3) Plaintiff Company wrote, by letter of 17.06.1999 (P7) to Defendant Bank requesting for a Bank guarantee. It is worded as .... Citi Bank cheque for Rs. 8,000,000/- on behalf of ALDC enclosed. Please issue a Bank guarantee for the same amount using enclosed format.
- (4) Cheque (P6) dated 18.06.1999 Payee – Pan Asia Bank Ltd. Amount Rs. 8,000,000/- Bank guarantee on behalf of ALDC.
- (5) P8 letter of 18.06.1999 by Defendant Bank to Plaintiff Company acknowledging receipt of cheque which was placed to credit of ALDC Informing Plaintiff Company that requested Bank guarantee to be issued on realisation of cheque and subject to completion of documentation. Letter issued on request of ALDC.

- (6) P9 letter of 16.07.1999 by Plaintiff Company to Defendant Bank. Request to issue Bank guarantee before 22.07.1999 or refund the sum of Rs. 8,000,000/-.
- (7) P10 letter of 20.07.1999 by Defendant Bank to Plaintiff Company stating unable to issue guarantee as ALDC has not completed documentation.
- (8) P11 letter of 21.07.1999 by Plaintiff Company to Defendant Bank requesting the Bank to inform the required documents. If guarantee cannot be issued calling upon the Bank to refund the money.
- (9) P12 letter of 02.08.1999 informing Defendant Bank that there was no response to several letters referred to therein
- (10) Letter P13 clearly set out the Defendant Bank's petition on the request for a bank Guarantee, 1 – 14 in P13 reflects good part of Defendant-Bank's position in this case. By P13 Defendant Bank denies liability and indicates that the Bank cannot exceed its authority or ignore instructions of their customers (ALDC)
- (11) On the question of completeness of documentation letter P14, P14A, P15 & P16, despatched. Letter P14 & P14A seems to suggest the Plaintiff-Appellant's position that the question of documentation has been fulfilled by ALDC and attempts to establish same with P14A. However the Defendant Bank insists Plaintiff to contact ALDC regarding this issue (P15 & P16).
- (12) Further communication by Plaintiff Company by P17 & P18. However Bank does not appear to retract from that stance as stated in P13, P19 & P21.

It is very apparent that, as gathered from the material made available to this court, good part of the factual position and situations discussed above are not in dispute. What is material to the primary issue is whether in fact and in law, parties expressly or impliedly agreed to enter into a contract of guarantee. All that took place within the available facts are that the Plaintiff Company had an arrangement/dealings with ALDC who was not a party to the suit. Each of the dealings of both Plaintiff Company and ALDC surface on post-dated cheques. In

the event of default to secure and ensure guarantee of such payment Plaintiff Company and ALDC by agreement P5 included clauses 3:2 and 4:1 which is more or less a conduit or path to obtain a guarantee from the Defendant-Bank who was not even a party to the agreement P5. I have referred to the above clauses 3:2 and 4:1 and it only contemplates to issue a cheque in favour of Defendant-Bank to enable the bank to issue a contract of guarantee in favour of the Plaintiff-Company. Issue of a guarantee is a separate arrangement for which ALDC is responsible as per agreement P5.

The agreement P5 by clause 7:1 provides an arbitration clause which enable the Plaintiff-Company and ALDC to settle their obligations and duties. Further as observed by the learned trial Judge even though the cheque of Rs. 8 million was issued in favour of the Defendant Bank it is issued on behalf of ALDC a customer of the Defendant-Bank. As such whatever obligation based on the cheque would be between the ALDC and Defendant-Bank. I observe that In these circumstances there is no express or implied agreement between the Plaintiff Company and the Defendant-Bank. A term will not be implied merely because it would be reasonable to imply it, contracts being made by the parties themselves and not by courts. Further the correct factual position is that no contract of guarantee was entered or issued in favour of the Plaintiff Company for the reasons adduced in the several correspondence had between the

Plaintiff Company and the Defendant Bank which material was made available to this court and discussed in this judgment. However if a Guarantee Bond was issued the position would have been different. I would mention just a few instances where a bank was held liable but based on a proper agreement. Vide *Adaicappa Chetty Vs. Thomas Cook and Sons Ltd.*, 31 NLR 385. S.C. This is a case where both Supreme Court and the Privy Council held that Bank must bear the loss. This case no doubt is no comparison to the case in hand.

If the emergence of a contract of guarantee was established the universal application of contract of guarantee and or documentary credit would apply which was discussed in *Hemas Marketing (Pvt) Ltd. Vs. Chandrasiri 1994 – (2) SLR 181*, which case also does not apply to the case in hand.

I have no hesitation to agree with the views of the learned trial Judge i.e no cause of action accrued to the Plaintiff to sue the Defendant Bank. As such there is no basis to consider and proceed to grant relief on the alternate causes of action pleaded in the Amended Plaint.

I will add to the position of the Defendant Bank, that there was an absence of intention of creating legal relations. I find that such an intention to create legal relations cannot be gathered or inferred from the available facts between the Plaintiff Company and the Defendant Bank. It is elementary that for the formation of a contract or agreement the intention to create legal

relations is an element necessary for the formation of a contract. Both parties must have this intention. Further what matters is not what they had in mind when concluding the contract or at the stage of discussion, but whether reasonable person would draw the conclusion from the words and actions that they wanted it to be legally bound. If such an intention to create legal relations cannot be gathered courts need to accept and respect the position that both or one of them had no intention. The Bank was vehemently objecting to issue a guarantee as ALDC had not complied with the required documentation, which was essential to formation of the guarantee. Bank rejects any liability on its part with the Plaintiff Company. A request for documents by the bank would be its normal business, to ensure smooth banking operations. The Bank in no uncertain terms makes it clear that it cannot disclose facts to the detriment of the customer (ALDC). Further based on P5 the matter had to be resolved as per agreement P5 and not with Defendant Bank who was not a party to agreement P5. The issuance of a guarantee would always be conditional upon happening of events, in the case in hand, it is the demand by the Bank for proper documentation, especially where a party is not a customer of the Bank. The Bank need to safeguard its own interest. Such a demand cannot be construed to give effect to create legal relations. Nor can a fiduciary relationship arise in the absence of some discretion or power.

In all the facts and circumstances of this case the cheque relied upon by the Plaintiff Company was in favour of the Defendant Bank to be utilised on behalf of ALDC (as per P5). It is in evidence that the cheque was realised and credited to the account of the banks customer namely ALDC. It is for the Plaintiff Company to advise themselves the proper course of action to be adopted based on the given facts as the bank does not take over liability in the manner pleaded by the Plaintiff Company. If at all the only agreement that surfaced is based on P5 and nothing else. Plaintiff Company was never a customer of the Defendant Bank. There is no implied agreement that emerged as contemplated by law or fact. I affirm the Judgment of the learned High Court Judge and dismiss this appeal with costs.

Appeal dismissed.

JUDGE OF THE SUPREME COURT

S. E. Wanasundera P.C., J

I agree.

JUDGE OF THE SUPREME COURT

Priyantha Jayawardena P.C.,

I agree.

JUDGE OF THE SUPREME COURT

