RAN BANDA AND OTHERS
v
THE PEOPLE'S BANK

COURT OF APPEAL
AMARATUNGA, J. AND
ABEYRATNE, J.
CALA NO. 160/2003
D.C. POLONNARUWA 327/2/DR
SEPTEMBER 17, 2003

Debt Recovery (Special Provisioners) Act, No. 2 of 1990 – Conditional leave to appear and defend granted – Rescheduling of the loan – Is it a novation of the contract? – Was the former debt extinguished and a new debt created? – Is the former contract unenforceable?

The 1st 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 1st defendant-petitioner acceped the rescheduled programme. When the 1st 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 sought-

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 third 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 concessionery rate of interest in respect of the balance of the loan remaining unpaid.

Per Ameratunga, J.,

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

APPLICATION for leave to appeal from the order of the District Court of Polonnaruwa.

Jacob Joseph for defendant-petitioners.

Gamini Marapana, P.C., with *Navin Marapana* for respondent bank

Cur.adv.vult

January 12,.2004

GAMINI AMARATUNGA, J.

This is an application for leave to appeal against an order made 01
by the learned District Judge of Polonnaruwa directing that in order to grant leave to the petitioners to defend the action filed against

them by the respondent Bank, (the Bank) the petitioners should deposit a sum of Rs.10 lakhs in cash and provide certified security for another sum of Rs.10 lakhs.

The 1st defendant-petitioner has obtained a loan of Rs. 20 million from the Bank. The loan application is the document marked P2 along with the plaint. The 1st defendant has also signed a promissory note in favour of the Bank for the said sum of Rs. 20 million. The 2nd and 3rd defendant-petitioners were the persons who stood as guarantors for the amount obtained by the 1st defendant. It is not disputed that the 1st defendant has paid a part of the loan. This is reflected in the ledger sheet marked P5. By 18/10/2000, a sum of Rs. 59 lakhs was remaining as the sum due to the Bank. By document marked V2A, dated 17/10/2000, the Bank submitted a proposal to re-schedule this amount of the loan and the terms of document V2A indicate that this proposal was offered at the request of the 1st defendant. The 1st defendant accepted this re-scheduled arrangement. When the 1st defendant failed to settle the loan within the period of eighteen months in terms of the re-scheduled arrangement, the Bank filed this action under and in terms of the provisions of the Debt Recovery Act. The total amount claimed was a sum of Rs. 2,395,640/- together with the legal interest until the said sum was paid.

The defendant-petitioners in their joint application and in their affidavits took up the position that the Bank had no right to seek to recover any sum of money upon the agreement P2 and that the 2nd and 3rd defendants were not liable to pay anything to the Bank as the said document P2 had become invalid. The basis upon which the defendants claimed that the original written contract P2 had become invalid was that when the Bank re-scheduled the loan the former debt was extinguished and a new debt created by the re-scheduled agreement V2A has come into existence and that this new contract made the former written contract unenforceable. In short the contention of the defendants was that the new arrangement brought into existence by the re-scheduled arrangement amounted to what is known to the law of contract as 'novation'. This concept of novation, which is a part of the modern law of contract, both English and the Roman Dutch, had its origins in the Roman Law. To put it in the simplest possible way, in the modern

law, 'novation occures whenever an existing obligation is discharged in such a manner that another obligation is substituted in its place.' Wessels-Law of Contract Vol 2, 2nd Ed., 1951, page 658 para.2369. 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 third party. When this happens, the later obligation extinguishes the former.

The law presumes that once a contract is established, it retains its binding force and that a creditor does not intend to renounce rights which he has acquired. Hence where two parties to a contract make a later agreement, the law will presume rather, that they intended both agreements to have equal force than that the latter should supersede the former. A mere change in the method of payment does not affect the substance of the contract, though it may affect the manner of its execution. Mere extension of time to the debtor does not affect the substance of the obligation and will therefore not be construed to be a novation having the effect of releasing the sureties. Wessels-paragraphs 2396, 2411 and 2415.

Document V2A clearly indicates that the re-scheduled arrangement was made at the request of the debtor, the 1st defendant. It merely gave him extended time for payment and a concessionary rate of interest in respect of the balance of the loan remaining unpaid as at the date of the re-schedule agreement. It did not bring into existence anything unfavourable to the guarantors. In fact the concessions granted to the debtor were beneficial to the guarantors as well. Condition No 4 in the re-scheduled agreement preserves 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 re-scheduled arrangement, and this in my opinion completely negatives any intention on the part of the Bank to make the re-scheduled arrangement to take the place of a new contract - a new obligation extinguishing the existing contract. Further the absence of the participation of the guarantors for the re-scheduled agreement is significant. It is clear evidence that the Bank considered that the re-scheduled arrangement was an arrangement within the framework of the existing contract and not in substitution therefor.

For the reasons stated above, I hold that the defendants-petitioners' argument that this is a case where there is novation is misconceived in law. The 1st defendant-petitioner has not stated that the sum claimed from him was not due from him; nor has he pleaded any substantial defence to the action. Accordingly I uphold the learned District Judge's order and refuse leave to appeal and dismiss the application with penal costs in a sum of Rs.15000/-. 80

ABEYRATNA, J. - I agree.

Application dismissed.