

**HATTON NATIONAL BANK LIMITED**  
**v.**  
**SELLERS SPORTS (PVT) LTD AND OTHERS**

SUPREME COURT  
S. N. SILVA, CJ.  
P. R. P. PERERA, J. AND  
WEERASEKERA, J.  
SC APPEAL (CHC) NO. 6/97(F)  
CHC NO. 92/96(1)  
JANUARY 24<sup>TH</sup>, 2000

*Civil Procedure Code - Cause of action - Section 5 of the Code - Bank facilities secured by a mortgage by the principal debtor and guaranteed by an agreement of sureties - Prescription of action - Sections 5, 6 and 7 of the Prescription Ordinance.*

The plaintiff Bank is the successor to the Emirates International Bank Ltd., whose rights were assigned to the plaintiff Bank by Deed of Assignment No. 603 dated 17. 09. 92.

The plaintiff instituted an action against the defendants on 21. 05. 96 jointly and severally to recover the sum of Rs. 12,413,814/46 being the total liability of the 1<sup>st</sup> defendant company as at 08. 01. 96 on credit facilities provided by the plaintiff's predecessor Bank by way of overdraft, time loan, packing credit and pledge loans. This was the total amount due on 30. 09. 89 plus interest thereafter. By way of security for the due re-payment of the accommodation granted to the 1<sup>st</sup> defendant by the Bank, the 1<sup>st</sup> defendant executed a Mortgage Bond dated 04. 09. 86 pledging the machinery, movables and book debts described in the agreement.

A statement of accounts was filed with the plaint. The Mortgage Bond was filed with the plaint and paragraph 6 of the plaint stated that it is pleaded part and parcel of the plaint and that the action is filed to enforce the obligation created thereby. The 2<sup>nd</sup> to the 5<sup>th</sup> defendants had entered into a Guarantee Agreement with the Bank, dated 22. 08. 86 to pay the Bank the money due from the 1<sup>st</sup> defendant upto a limit of Rs. 11,200,000/- By Clause 2 of the Guarantee they agreed to pay the Bank in Colombo, the money therein mentioned 10 days after demand in writing is made. Such demand was made by writing dated 26. 04. 96.

**Held :**

In the light of the definition of "cause of action" contained in section 5 of the Civil Procedure Code and the averments in the plaint, the action

against the 1<sup>st</sup> defendant was not one for the recovery of money lent without written security or money lent "upon account stated" where the period of prescription is 3 years in terms of section 7 of the Prescription Ordinance which period has to be computed from the date of the default namely, 30. 09. 89. The action was filed to enforce the obligation created by the Mortgage Bond. The applicable section would be section 5 of the Prescription Ordinance which relates to instances where the action is for the recovery of any sum due upon any mortgage of property or upon any bond conditioned for the payment of money. The action was not prescribed as it was filed within 10 years from the date of the mortgage as provided by that section.

2. As regards the Guarantee of the 2<sup>nd</sup> to 5<sup>th</sup> defendants, the applicable section is section 6 of the Prescription Ordinance which relates to amounts due on a written promise or other written security and the period of prescription is 6 years. That period should be computed not from the date of the default on the principal obligation namely, 30. 09. 89 but from the date on which the payment upon the Guarantee became due namely, 10 days after demand in writing was made, as stated in clause 2 of the agreement. The demand for payment was made on 26. 04. 96; and the breach took place upon the failure to make payment 10 days after that demand. As such, the action which was filed on 21. 05. 96 against the 2<sup>nd</sup> to 5<sup>th</sup> defendants was not prescribed in terms of section 6 of the Prescription Ordinance.

**Case referred to :**

*Croos v. Goonewardena Hamine* 5 NLR 259 at 261

**APPEAL** from the Judgment of the Commercial High Court Colombo.

*Romesh de Silva P.C.* with *Palitha Kumarasinghe* for the appellant.

*S.A. Parathalingam P.C.* with *Faizer Musthapha* for the 1<sup>st</sup>, 2<sup>nd</sup>, and 5<sup>th</sup> defendants-respondents.

*Cur. adv. vult.*

September 12, 2000.

**S. N. SILVA, C.J.**

This is an appeal from the judgment of the High Court dated 24. 04. 97. By that Judgment the High Court dismissed the action of the Plaintiff on the ground that it was prescribed.

The Plaintiff being a licensed commercial bank instituted the action against the Defendants jointly and severally to

recover a sum of Rs. 12,413,814.46. The principal cause of action is against the 1<sup>st</sup> Defendant being a private company. The other Defendants are sued on the basis of a guarantee given by them in respect of the liability of the 1<sup>st</sup> Defendant.

The 1<sup>st</sup> Defendant was a constituent of the Union Bank of Middle East Ltd., which was later renamed as the Emirates International Bank Ltd. The liability in respect of the action has been filed was contracted with the said Bank. The rights of this Bank were thereafter assigned to the Plaintiff Bank by Deed of Assignment No. 603 dated 17. 09. 92 filed with the plaint.

According to the statement of Accounts (filed with the Plaint) the 1<sup>st</sup> Defendant availed of the credit facilities of the predecessor Bank by way of an overdraft, time loan, packing credit and pledge loans. The amount stated above in respect of which the action has been filed is the total liability on the aforesaid lines of credit as at 08. 01. 1996.

The 1<sup>st</sup> Defendant entered into an Agreement in writing dated 04. 09. 96 with the predecessor Bank in the form of a Mortgage, placing as security the machinery, movables and books debts described in the Agreement for the due repayment of the accommodation granted to the 1<sup>st</sup> Defendant by the Bank, under a drawing limit of Rs. 7,500,000/-. This Mortgage has been registered under the Registration of Documents Ordinance and has been filed with the Plaint. The 2<sup>nd</sup> to 5<sup>th</sup> Respondents entered into a Guarantee Agreement with the Bank, dated 22. 08. 86 to pay the Bank the money due from the 1<sup>st</sup> Defendant upto a limit of Rs. 11,200,000/-.

The execution of the Mortgage and the Guarantee referred to above are not denied. According to the answer, the Defendants appear to dispute the statement of accounts. But, this matter has not been gone into. The action has been dismissed as stated above on the preliminary issue of prescription.

The High Court has accepted the submission of the Defendants that the action has not been filed to enforce the Mortgage and as such it should be taken as being one for the recovery of money lent without written security. It is the finding of the Court that the money is due "upon an account stated" where the period of prescription is 3 years in terms of section 7 of the Prescription Ordinance. The court has held that this period of 3 years should be computed from the date of default being 30. 09. 89, according to the statement of accounts. Therefore it was held that the cause of action against the 1<sup>st</sup> Defendant is prescribed.

As regards the Guarantee of the 2<sup>nd</sup>, 3<sup>rd</sup>, 4<sup>th</sup> and 5<sup>th</sup> Defendants, the Court held that the liability arises on the written Guarantee and that the applicable period of prescription would be 6 years in terms of section 6 of the Prescription Ordinance, which should be computed from the date of the default of the principal obligation, namely 30. 09. 89 (as stated above) and not from the date of demand as contended by the Plaintiff.

On the said basis it was held that the action filed on the 21. 05. 96 is prescribed in relation to the liability of all the Defendants and should be dismissed.

The submission of Counsel for the Plaintiff Appellant is that the Court has erred in not taking into account the Mortgage Bond and failing to consider section 5 of the Prescription Ordinance as the applicable section. In terms of this section the period of prescription is 10 years. It was contended that since the Mortgage Bond dated 04. 09. 86 the action filed on 21. 05. 96 is within the period of 10 years. As regards the Guarantee on which the other Defendants have been sued it was contended that the breach of the Guarantee took place only upon the failure of the Defendant to pay the money that was demanded by the Bank on the Guarantee. On that basis it was contended that the period of prescription should be computed from 26. 04. 96 being the date of the letter

of demand sent to the Defendants by the Bank. Counsel for the Defendant supported the judgment on the grounds stated therein as outlined above.

Upon a consideration of the several averments of the Plaintiff and the documents that have been filed with the plaintiff it is clear that the action against the 1<sup>st</sup> Defendant has been filed to recover the amount outstanding on the accommodation granted by the Bank by way of an overdraft and other lines of credit. The High Court has not stated any specific reason for the rejection of the Mortgage Bond which has been produced as being the basis of the action against the 1<sup>st</sup> Defendant. It appears that since the statement of accounts has been produced annexed to the plaintiff, the High Court has considered that to be the sole basis of liability. In this respect the court has erred in failing to take into account the nature of the obligation of the 1<sup>st</sup> Defendant in respect of which the action has been filed. The Court has totally ignored the cause of action as pleaded in the plaintiff and has looked into only the document which sets out the quantum of the liability.

Section 5 of the Civil Procedure Code defines a cause of action "as being the wrong for the prevention or redress of which an action may be brought and includes the denial of a right, the refusal to fulfill an obligation, the neglect to perform duty and the infliction of an affirmative injury."

The present action is based on a wrong which relates to the refusal to fulfill an obligation. The obligation is primarily of the 1<sup>st</sup> Defendant who was granted accommodation by the Bank in the form of an overdraft and other lines of credit as stated above. In the case of *Croos v. Goonewardena Hamine*<sup>11</sup> Wendt J stated as follows "I think that the word "obligation" in this definition is to be understood not in the narrow sense in which a parole promise to pay, a promissory note and a mortgage, although given for the same debt may be described as three different "obligations", but in the more general understanding sense of a liability to pay that sum of money."

The High Court has fallen into error of not looking at the obligation in the manner noted above. The court has merely looked at the statement of accounts and drawn the inference that the obligation arises solely upon the account so stated. In this instance the account stated is the quantification of the liability incurred by the 1<sup>st</sup> Defendant on the different lines of credit granted to him. It sets out the total due under each head as at 30. 09. 89 and the interest debited thereon from 30. 09. 89 to 31. 12. 95 except in the case of the pledge loan where the interest is computed upto 19. 10. 90. The obligation which forms the cause of action is the liability which arises upon the total accommodation granted to the 1<sup>st</sup> Defendant by the Bank and secured by the Mortgage Bond. It has been clearly stated in paragraph 6 of the plaint that the Mortgage Bond is pleaded as part and parcel of the plaint and that the action is filed to enforce the obligation created thereby. The Mortgage Bond that has been produced narrates that the Bank being an approved credit agency has agreed to grant accommodation to the borrower by way of Overdraft, Loan, Cash, Credit Account or otherwise under a drawing limit of Rs. 7,500,000/-. It is further stated that the accommodation is granted on the agreed security consisting of machinery; movable property and the book debts set out in the bond. The Mortgage Bond is thus the legal framework within which the obligation to repay the debts contracted under different items, is constituted. In the circumstances it cannot be said that the accommodation has been granted "without written security," so as to attract the provisions of section 7 of the Prescription Ordinance. The applicable section in my view would be section 5, which relates to instances where the action is for the recovery of any sum due upon any mortgage of any property or upon any bond conditioned for the payment of money. The Mortgage Bond produced clearly falls within that description. In the circumstances the action would not be prescribed if it is filed 10 years from the date of the mortgage. As noted above the action has been filed within that period and the claim against the 1<sup>st</sup> Defendant would not be prescribed.

As regards the Guarantee it is common ground that the applicable section is section 6 of the Prescription Ordinance, which relate to amounts due on a written promise or other written security and the period of prescription is 6 years. The question to be decided is whether the period of 6 years should be computed from the date of the Guarantee being 22. 08. 86 or, from the date on which there was a default in respect of the principal obligation or, the date from which the payment upon the Guarantee became due.

The liability in respect of the Guarantee is specifically stated in clause 2, whereby the 2<sup>nd</sup> to 5<sup>th</sup> Defendants agreed to pay the Bank in Colombo, the money therein mentioned, 10 days after demand in writing is made on them provided always that the total liability ultimately enforceable under the Guarantee shall not exceed the sum of Rs. 11,200,000/.

It is thus seen that although the Guarantee of the 2<sup>nd</sup> to 5<sup>th</sup> Respondents is valid from the date of its execution, payment thereon becomes due only upon a demand being made. It is on a failure on the part of the guarantors to make payment upon the demand that a breach of the Guarantee takes place. In terms of Section 6 of the Prescription Ordinance an action is not maintainable unless it is brought within 6 years of such breach.

It is not disputed that the demand for payment on the Guarantee was made on the 2<sup>nd</sup> to 5<sup>th</sup> Defendants by writing dated 26. 04. 96. Therefore the amount stated in the guarantee became due upon such demand and a breach takes place when there is a failure to make payment ten days after such demand is made. It could not be contended that the action filed on 21. 05. 96 against the 2<sup>nd</sup> to 5<sup>th</sup> Respondents is in any way prescribed by the application of the provisions of Section 6 of Prescription Ordinance.

The High Court has held, that a breach of the guarantee takes place on the date the principal debtor (1<sup>st</sup> Defendant)

stopped making payment which has, been taken as 30. 09. 89 from the statement of accounts. Once again the High Court has failed to examine this question from the standpoint of the cause of action pleaded against the 2<sup>nd</sup> to 5<sup>th</sup> Defendants. The obligation of the 2<sup>nd</sup> to 5<sup>th</sup> Defendants although intrinsically connected with that of the 1<sup>st</sup> Defendant rests on a distinct and different legal basis. A default on the part of the 1<sup>st</sup> Defendant to pay the sum due on the accommodation granted does not per se, (in the absence of a specific provision to that effect in the Guarantee) amount to refusal on their part to fulfill an obligation so as to constitute a cause of action against these Defendants. As noted above the obligation on their part to make payment on the Guarantee becomes effective only when the demand is made. It is only at that stage the refusal to fulfill the obligation and the concomitant breach of Guarantee takes place so as to attract the provisions of Section 6 of the Prescription Ordinance. The basis on which the High Court has computed the period of prescription is therefore untenable.

For the reasons stated above I uphold the submissions of the Plaintiff Appellant and set aside the Judgment dated 24. 04. 97. The case is referred back to the High Court for trial to proceed in respect of other issues before any Judge.

Plaintiff would be entitled to the costs of this appeal fixed at Rs. 15,000/-.

**PERERA, J.** - I agree.

**WEERASEKERA, J.** - I agree.

*Appeal Allowed.*