FIRST DIVISION, INNER HOUSE, COURT OF SESSION

[2019] CSIH 47
CA64/18

Lord President
Lord Brodie
Lord Drummond Young

OPINION OF THE COURT

delivered by LORD DRUMMOND YOUNG

in the Reclaiming Motion by

BRITISH OVERSEAS BANK NOMINEES LTD AND OTHERS

Pursuers and Respondents

against

STEWART MILNE GROUP LTD

Defender and Reclaimer

Pursuers and Respondents: DM Thomson QC; Brodies LLP
Defender and Reclaimer: GJ Walker QC, AN McKenzie; Anderson Strathern LLP

10 September 2019

[1] The parties' dispute relates to the construction of a collateral warranty granted by a design and build contractor in favour of purchasers of a development from the original developer. The development, which was situated at Souterford Road, Uryside South, Inverurie, comprised the construction of eight new retail units together with a garden centre slab, tenant fit-out works and associated car parking, service yards and related external works. The developer, who was the employer in the design and build contract, was Northburn Developments Ltd ("Northburn"). The defender was the design and build

contractor. The construction contract between Northburn and the defender was dated 20 and 21 August 2008, and was in the form of the SBCC Design and Build Contract for use in Scotland (DB/Scot), 2005 Edition, October 2007 Revision, as amended by a document entitled "Amendments to the SBCC Design and Build Contract for use in Scotland 2005, incorporating Amendment 1 (issued April 2007) and October 2007 Revision".

[2] The contract between Northburn and the defender imposed obligations on the defender to use, in general terms, proper skill and care in the design and construction of the works. It further contained an obligation on the defender to grant collateral warranties in favour of any person who might subsequently acquire an interest in the development as a purchaser or tenant. The pursuers are nominees for National Westminster Bank plc, which operates as a depositary of the Janus Henderson UK Property PAIF. In June 2013, the pursuers, acting in that capacity, and Northburn concluded missives for the sale of the site and development to the pursuers. The pursuers took entry on 27 June 2013. In terms of those missives, Northburn was obliged to deliver to the pursuers various collateral warranties, including a collateral warranty in the pursuers' favour executed by the defender as the design and build contractor. A collateral warranty by the defender in favour of the pursuers was in due course executed and delivered to the pursuers; it was dated 24 June and 28 August 2013.

[3] The development had been constructed during 2009. It subsequently became apparent that the car park at the site, which had been designed and constructed by the defender, suffered from flooding at its northern boundary. The present action relates to the alleged flooding. The pursuers aver that the defender was in breach of obligations that it had undertaken in the collateral warranty to carry out and complete the building works, to perform all of its duties under the building contract, and to design the works and select

materials with reasonable skill and care such as would be expected of a prudent and experienced designer of the relevant discipline. The flooding, it is averred, resulted from defective design and construction of the car park by the defender. The pursuers aver in particular that if the car park had been properly designed and installed it would not suffer from flooding in ordinary course; that the gradient of the car park as constructed was inadequate to manage ordinary surplus water; and that standard remedial measures had not been taken. They claim the cost of remedying those alleged defects. For present purposes it is unnecessary to consider the details of the pursuers' claim. What is material is that the pursuers' averments refer to an investigative report on flooding in the car park prepared by Colliers International, a consultancy firm, dated May 2013. Both the pursuers' averments and the terms of that report disclosed that that the flooding was apparent by that date.

[4] The present action was raised on 21 June 2018, more than five years after Colliers' report. The defender has tabled a plea of prescription, to the effect that under specific clauses of the collateral warranty, clauses 2.3 and 3.1, any liability arising under the duties in the building contract had been extinguished by operation of prescription by the time that the present action was raised. The collateral warranty in favour of the pursuers is of course a separate contract from the design and build contract between the defender and Northern. The collateral warranty is dated 24 June and 28 August 2013, and the present action was raised within five years of the granting of the collateral warranty. Consequently, if the relevant prescriptive period runs from the date when the collateral warranty was granted, the present action was raised within the prescriptive period. The defender contends, however, that under the terms of the collateral warranty it was subject to the same prescriptive period as applied under the original design and build contract. The existence of the flooding in the car park was known by the time of Colliers' report, and the prescriptive

period must therefore run from no later than May 2013. According to the defender, the fact that the collateral warranty was only granted in June and August 2013 is immaterial, because it is the prescriptive period incorporated into the design and build contract that is applicable, not the period that would have been imposed under the statutory law of prescription. Put shortly, the defender's contention is that its obligations under the collateral warranty are subject to a contractual time limitation rather than the general law.

[5] The action proceeded to a debate before the Commercial Judge on the question of whether the defender is correct in its argument based on the application of a conventional period of time limitation. The Commercial Judge held that the pursuers' construction was correct and that the defender's plea of prescription accordingly fell to be repelled. The defender has reclaimed against her interlocutor to that effect.

Contractual construction

[6] The fundamental issue in the present case turns on the construction of the Collateral Warranty Agreement granted by the defender in favour of the pursuers. A collateral warranty is a contract in its own right, distinct from (although dependent on) the building contract to which it relates. Consequently the terms of a collateral warranty should be construed in the same way as contracts generally. The correct approach is described in a substantial number of cases; for present purposes it is perhaps sufficient to note the decisions in *Rainy Sky SA* v *Kookmin Bank Co Ltd*, [2011] 1 WLR 2900, *HOE International Ltd* v *Andersen*, 2017 SC 313, *Midlothian Council* v *Bracewell Stirling Architects*, [2018] PNLR 25, and *Wood* v *Capita Insurance Services Ltd*, [2017] 2 WLR 1095.

[7] The result of these cases is that contractual provisions must be construed in accordance with the objective intention of the parties: the intention that reasonable persons

would have had in the parties' position had they possessed the same background knowledge. It is also appropriate to rely on commercial common sense. The exercise of construction should be both purposive and contextual. Purposive interpretation means that the court should attempt to give effect to the primary purposes that, objectively, the parties intended at the time of the contract. Determining those purposes will obviously turn on the wording used, but that wording must be considered in in such a way as to give effect to the primary objectives of the contract rather than giving undue influence to minor provisions or niceties of wording. In our opinion the underlying commercial purpose of a collateral warranty is of importance in the present case. The fundamental purpose of the collateral warranty is to place the beneficiary and the contractor in an equivalent position to the original developer and the contractor, not to extend the obligations of the contractor to the beneficiary of the warranty beyond those undertaken in favour of the original developer. Details of the wording used should not obscure that basic objective.

[8] Contextual construction means that the wording used in the contract must be construed against the background known to the parties at the time. Context can take many forms. First, with building projects, the roles of the various persons involved, in the totality of the contracts governing the project, including subcontractors, are an important component. Secondly, the collateral warranty itself, like any other contract, must be construed as a whole. Thirdly, the general legal context will usually be relevant. In the present case that includes the rules of prescription, and also the rules of law relating to contractual defences and limitations. It also includes the primary legal reasons that collateral warranties are used: the principle of privity of contract, the impact of the decision in *Murphy* v *Brentwood Council*, [1991] 1 AC 398, and the consequent need to prevent loss caused by the failure of a contractor or a member of the design team to use proper care and

skill from falling into a so-called "black hole", so that the person suffering the loss is unable to obtain compensation.

Collateral warranties

[9] The development of the collateral warranty, and the reasons for its use, are discussed in some detail in *Scottish Widows Services Ltd* v *Harmon*, 2010 SLT 1102, at paragraphs [1] and [17]-[18]. Collateral warranties are now widely used in all major construction projects. They were developed following the decision of the House of Lords in *Murphy* v *Brentwood Council*, *supra*. Prior to that decision it was clear that, by virtue of the doctrine of privity of contract, a contractual duty of care could only arise as between persons who were in a direct contractual relationship with each other. Thus the contractor in the building contract would owe contractual duties of care to its original employer, but would not owe any such duty to persons such as a subsequent purchaser or tenant of the development. It had been thought on the basis of decisions of the House of Lords in cases such as *Anns* v *Merton London Borough Council*, [1978] AC 728, and *Junior Books Ltd* v *Veitchi Co Ltd*, 1982 SC (HL) 244, that a delictual duty of care might arise in such circumstances. In *Murphy*, however, it was held that, while contractors and others engaged in building projects might be liable in delict or tort to third parties who are injured or whose property is injured in consequence of the negligent performance of work, that duty does not extend to an owner of the property on which the work was carried out or any person whose rights in the property are derived from the owner, such as a tenant. The loss sustained by the owner or tenant is classified as pure economic loss, and the House of Lords held that compensation for such loss is not recoverable in delict or tort; common law duties to use reasonable skill and care did not extend to such loss. Consequently, if the owner of the building or any person deriving title

from the original owner were to have any right to recover damages for the negligent design or construction of the building, that right must be founded in contract.

[10] Among those involved in building contracts it was thought that it was generally reasonable that the duties of care incumbent on a contractor or a member of the design team in favour of their original employer should extend to those such as purchasers and tenants who acquired an interest from the employer. After the property was sold or let, the loss arising from defective design or workmanship, usually in the form of payment for remedial work, was likely to fall on the owner or tenant for the time being. The purchaser or tenant, however, had no contractual relationship with the contractor or design team. The original employer had such a relationship, but as it had sold the property it suffered no loss. If no action were taken, therefore, the loss was likely to fall into a so-called "black hole": the party with a right of action against the negligent contractor or designer (the original employer) had suffered no loss, and the party that suffered the loss (the purchaser or tenant) had no right of action. It has been remarked that in a well regulated legal universe black holes should not exist; the reasons are obvious. It was to deal with this problem that collateral warranties came into general use.

[11] The purpose of a collateral warranty, which is important in the present case, is accordingly to create an express contractual provision whereby the contractor or a subcontractor or a member of the design team undertakes a duty of care to persons such as a purchaser of an interest in the development from the original employer, or a person who has obtained a tenancy or security right in the development from the employer. The collateral warranty is an independent contractual undertaking between on one hand a contractor or subcontractor or member of the design team and on the other hand persons who acquire an interest in the property from the original developer, who will normally have been the

employer in the main building contract or in contracts for architectural and engineering services.

> "The purpose of a collateral warranty… is to provide a right of action between parties who, under the standard legal structures used in construction contracts, would not otherwise be in any contractual relationship; it thus confers title to sue on the grantee of the warranty. A collateral warranty constitutes a contract between the granter and the grantee. Under that contract, the granter undertakes that it will perform specified works to a standard of competent workmanship (in the case of a contractor), or will provide specified services and observe proper professional standards of skill and care (in the case of an architect or engineer). If the granter fails to perform its duties to the required standard, the grantee can raise an action to compel such performance…. Alternatively, if the grantee suffers financial loss as a result of the defective performance, it may raise proceedings against the granter in order to recover the amount of that loss": *Scottish Widows* at paragraph [17]

[12] The foregoing legal and commercial context in which collateral warranties have come to be used demonstrates an important feature of their purpose. This is to provide persons such as a purchaser or tenant or security holder with rights against the contractor, or a subcontractor or member of the design team, that are equivalent to the rights that were enjoyed by the original employer under the building contract and the ancillary contracts with architects, engineers, subcontractors and others. The notion of equivalence is central. The purpose of the warranty is not to provide purchasers, tenants and security holders with rights greater than those held by the original employer; to do so would make no commercial sense. Equivalence accordingly requires not merely that the beneficiary of the warranty should have the same affirmative rights of action as the original employer; it also requires that those rights of action should be subject to the same qualifications, limitations and defences as were available to the contractor in respect of the original building contract.

[13] The present action relates to a design and build contract, and consequently a single person, the design and build contractor, is responsible for both the works of construction and the design of the development. Obviously the design works may be subcontracted by

the design and build contractor, to architects or various types of engineer, but it is the design and build contractor who is responsible to the original employer (the developer) for the work of such subcontractors. Nevertheless, the fundamental purpose of the warranty remains that of placing purchasers, tenants and others who acquire an interest in the development in an equivalent position to the employer of the design and build contractor. As already noted, that purpose is in our opinion of fundamental importance in construing the terms of any collateral warranty.

[14] Construction contracts and contracts with professionals in the building industry are almost invariably governed by standard forms. In these, it is normal to find that express duties of skill and care are set out. At the same time, however, those duties will invariably be qualified by a range of limitations or defences. These may include, for example, limitations on the standards of care and standards of workmanship that are required, or provisions that qualify the right to payment. An arbitration clause is almost invariably found. The limitations may also include express time-bar provisions. In the present case an example of this is found in clause 3.2 of the Collateral Warranty Agreement, discussed below at paragraph [24], which provides that no proceedings for breach of the agreement may be commenced against the contractor after 12 years from issue of the final statement of practical completion. In addition to such express provisions, however, the general statutory law of prescription applies to every building contract.

[15] The reasons for imposing a time bar on rights of action are well known. Three reasons are of particular importance in relation to construction contracts. First, with the passage of time, there is an obvious risk that evidence will be lost; the contractual documentation may have been destroyed or mislaid, and the recollection of witnesses will inevitably deteriorate. Thus it may be impossible to reconstruct the circumstances of the

original project. This may obviously prejudice the building owner's presentation of a claim, but it may also prejudice the ability of the contractor or member of the design team to present an effective defence. Secondly, there must come a point in the conduct of affairs when finality is achieved, so that the persons involved can move on without the risk of latent claims against them. This is particularly important when potential liabilities are the subject of insurance. For example, an architect or engineer will invariably have professional indemnity insurance, and must be able to say with certainty that before a certain point there are no possible claims against it. Thirdly, in relation to construction contracts, buildings typically have a long life, and there is therefore a significant risk that claims for negligence might be made in respect of latent defects that only appear many years after the work was carried out. By that time, of course, the danger of loss of evidence may be acute, and the risk to an insurer is also serious.

[16] Because of the importance of time-bar provisions to contractors and designers, we are of opinion that a collateral warranty should normally be subject to the same time bar as applied to the original building contract. By the "same" time bar, we mean a time bar that has effect on the same date. We cannot conceive of any policy reason to the contrary. Obviously it is possible for the parties to a collateral warranty to agree on a different time bar from that under the building contract, subject to the mandatory nature of the statutory law of prescription, but in construing contractual provisions the norm must, we think, be that the same time bar should apply to all the potential liabilities of the contractor and the design team.

The Design and Build Contract between Northburn and the defender

[17] The importance of contractual defences and limitations of liability is illustrated by

the facts of the present case. The design and build contract between Northern and the defender is governed by the SBCC Design and Build Contract for use in Scotland (DB/Scot), 2005 Edition, October 2007 Revision, amended as indicated in paragraph [1] above. This is one of the standard forms of contract developed (and revised periodically) by the Scottish Building Contracts Committee, which represents the various commercial and professional groups that are interested in building contracts and ancillary contracts for matters such as architectural and engineering services and has the benefit of expert legal advice. The SBCC generally aims at striking a balance among the various parties involved in a building contract, although inevitably it does so at a general level having regard to normal or typical features of the type of contract in question rather than specific features of a particular project. Nevertheless, the balance that is struck in the standard forms of building contract includes not merely the affirmative duties and responsibilities but also a range of limitations and defences on liability. These features of the contract must in our opinion be considered as a totality.

[18] Section 2 of DB/Scot deals with the carrying out of the Works (a defined term, which refers to the works particularly described in the Contract Documents, including any changes that are made). Clauses 2.1 and 2.2 set out the contractor's obligations. The basic obligation is found in paragraph 2.1.1, which provides as follows (words with capital letters being defined terms):

> "The Contractor shall carry out and complete the Works in a proper and workmanlike manner and in compliance with the Contract Documents, the Construction Phase Plan, and the Statutory Requirements and for that purpose shall complete the design for the Works including the selection of any specifications for the kinds and standards of the materials, goods and workmanship to be used in the construction of the Works so far as not described or stated in the Employer's Requirements or Contractor's Proposals, and shall give the notices required by the Statutory Requirements".

Clause 2.2, which deals with materials, goods and workmanship, provides that these should be of the standards described in the Employer's Requirements or the Contractor's Proposals. Both the Employer's Requirements and the Contractor's Proposals are typically lengthy documents which reflect the enormous amount of detail, at a practical level, that is required in any building project other than the simplest. Clause 2.11.1 (as amended in April and October 2007) provides that the Contractor accepts entire responsibility for the design of the Works, all designs contained in the Employer's Requirements and Contractor's Proposals, and all design work prepared before or after the date of the Contract and whether carried out by or behalf of the Employer or the Contractor. Clause 2.11.2 (as amended) then provides as follows:

> "The Contractor warrants and undertakes to the Employer that the Works will, when completed, comply with any performance, specification or requirement included or referred to in the Employer's Requirements and/or the Contractor's Proposals or any Changes".

[19] The obligations of the design and build Contractor are, however, subject to important limitations. Some of these are found in the contract; for example if a particular component is specified in the Employer's Requirements but turns out not to be fit for purpose, the design and build contractor will not be liable because it is obliged by the terms of section 2 of DB/Scot to follow those Requirements. Other limitations on liability are found in the general law. For example, a material failure to perform by the employer may justify use of the general contractual defence of retention. Set off and other similar defences will also apply. The same applies to the statutory defence of prescription.

[20] The contract between Northburn and the defender, in the amendments issued in April 2007 and pursuant to the revision of October 2007 (see paragraph [1] above) contains a section, section 10, dealing with assignation, third-party rights and collateral warranties.

This section inserts a new clause 7.4 into the standard form of contract DB/Scot in the following terms:

> "The Contractor shall within 21 days of a written notice given by or on behalf of the Employer provided to the Employer, in the form set out in Schedule Part 11, duly executed in a self proving matter collateral warranty agreements from the Contractor in favour of:-
>
> 7.4.1 each Funder;
>
> 7.4.2 each Purchaser; and
>
> 7.4.3 each Tenant".

The expression "Purchaser" is defined (clause 5.23 of the Amendments) as "each first and second purchaser of the whole or each part of the Works". The collateral warranty in the present case was granted pursuant to clause 7.4.2, in favour of the pursuers as a Purchaser of the whole of the development.

Terms of the Collateral Warranty Agreement

[21] The Collateral Warranty Agreement is a contract between the defender, described as "the Contractor", and the pursuers, described as "the Beneficiary". It begins, in recital (A), by referring to the Building Contract between Northburn and the defender and in recital (B) to the fact that the Beneficiary had entered into an agreement with Northburn to purchase the Development. In recital (D) it is narrated that the pursuers, as Beneficiary, had relied on and would continue to rely upon the defender's reasonable skill, care and attention in respect of all matters covered by the warranty insofar as they related to the Works to be carried out under the Building Contract.

[22] Clause 2 of the Collateral Warranty Agreement is headed "Contractor's obligations". Clause 2.1 narrates that the Contractor "warrants and undertakes to the Beneficiary that it has carried out and completed and will carry out and complete the Works in accordance

with and subject to the terms of the Building Contract". Clause 2.2 contains a warranty as follows:

> "The Contractor further warrants and undertakes to the Beneficiary that the design of the Works and the selection of goods, materials, plant and equipment for incorporation in the Works have been or will be designed or selected with all the reasonable skill, care and attention to be expected of a prudent and experienced, properly qualified and competent designer of the relevant discipline with experience of developments of a similar size, scope, complexity and value to the Development all to the same effect as if the Contractor had been appointed by the Beneficiary".

The closing words of that clause demonstrate the fundamental intention underlying a standard collateral warranty that the beneficiary of a warranty should be placed in the same position as the employer under the building contract to which the warranty relates; that is the fundamental principle of equivalence.

[23] The principle of equivalence is made more explicit in clause 2.3, which provides:

> "The Contractor shall have no greater duty to the Beneficiary under this Agreement than it would have had if the Beneficiary had been named as the employer under the Building Contract".

Clause 2.3, particularly in juxtaposition with clause 2.2, is in our opinion important. It indicates that the defender's duties to the pursuers as Beneficiary of the Collateral Warranty Agreement are to be restricted to the duties incumbent on the defender in terms of the building contract. The clear intention is that the liabilities undertaken by the defender under the Warranty are to be equivalent to, but no greater than, the defender's liabilities under the Building Contract. This is hardly surprising; indeed, for reasons discussed previously, it represents obvious commercial common sense. The Collateral Warranty is designed to place the Beneficiary in the same position as if it were the employer under the building contract, and thus to avoid the risk that loss will fall into a "black hole" because of the absence of any contractual relationship between the contractor and the beneficiary. It is not, however, intended to place the Beneficiary in a more favourable position than the original employer.

There is no commercial reason for doing so, and if the Collateral Warranty had the effect of conferring greater rights on the Beneficiary it could readily be regarded as unfair to the contractor who grants the Warranty.

[24] The Collateral Warranty Agreement goes further in ensuring that defences that would be available to the contractor under the Building Contract remain available as against the Beneficiary of the Warranty. Clause 3 of the Agreement, headed "Limitation of Liability", is in the following terms:

> "3.1 The Contractor shall be entitled in any action or proceedings by the Beneficiary to rely on any limitation in the Building Contract and to raise the equivalent rights in defence of liability as it would have against the Employer under the Building Contract (other than counterclaim, set-off or to state a defence of no loss or a different loss has been suffered by the Employer than the Beneficiary).
>
> 3.2 No action or proceedings for any breach of this Agreement shall be commenced against the Contractor after the expiry of 12 years from the date of issue of the final statement of practical completion or the equivalent under the Building Contract".

Once again, it is apparent that the intention, construed objectively, of the Collateral Warranty Agreement is to place the parties to the Warranty in an equivalent position to that of the employer and contractor under the design and build contract between Northburn and the defender. That means that the beneficiary obtains the rights that Northburn had against the defender but subject to the defences and limitations that the defender would have had against Northburn. The objective is clearly to achieve equivalence; that follows from both the purpose of the Collateral Warranty, considered in context, and commercial common sense, applied to the parties' relationships.

Prescription and the Collateral Warranty Agreement

[25] As already indicated, the critical question is whether clause 3 of the collateral warranty, which imposes limitations on the liability of the defender, incorporates a

contractual prescriptive period that corresponds to the prescriptive period that applied to the defender's liabilities to Northburn, or whether the general law of prescription operates in such a way that a new prescriptive period runs from the date when the collateral warranty was granted, on the basis that that is a new and distinct contract. If the former is the correct interpretation, the pursuers' claim is barred by a conventional time-bar provision; if the latter, only the statutory period of prescription is relevant, running from the date when the Collateral Warranty was granted, and that had not expired when the action was raised. As a matter of principle we are of opinion that parties should be at liberty to agree in their contract to impose a time limit on claims that is shorter than the statutory prescriptive period. The statutory prescriptive period is essentially a default provision; if parties choose in their contract to have claims under that contract cut off after a shorter period they may do so. Indeed, that is a potential result of clause 3.2 of the Collateral Warranty, which imposes a time limit of 12 years from the date of practical completion on any claims that may arise. A period of 12 years from practical completion may expire before a latent defect becomes manifest, or within five years after the date on which it becomes manifest, in which case the contractual time bar will operate before the statutory time bar. That clause is clearly designed to provide a long-stop bar against any claims against the defenders. The policy reasons for doing so are obvious: it provides the parties with closure, and avoids any risk arising from the loss of evidence as a result of the passage of time.

[26] Similar considerations apply to clause 3.1 of the collateral warranty. This entitles the Contractor, the defender, in any proceedings by the Beneficiary "to rely on any limitation in the Building Contract and to raise the equivalent rights in defence of liability as it would have against the Employer under the Building Contract". As we have already indicated, that wording must be read in the context of the structure of contracts applying to the

development, and in the legal context: this includes both the general principle of privity of contract and the restrictions placed on delictual claims for the defective construction or design of a building. The fundamental purpose of the present collateral warranty appears from that context. The collateral warranty is intended to deal with the "black hole" problem by providing a purchaser of the development (or a tenant or a funder of the development: see paragraph [21] above) with rights against the defender, the design and build Contractor, that are equivalent to the rights enjoyed by the original developer, Northburn. The notion of equivalence, however, requires that the rights transferred should be subject to all defences and limitations that applied to Northburn. The intention of clause 3.1 was to incorporate those defences and limitations into the relationship between the defender and any Beneficiary such as the pursuers, to provide equivalence between the rights available to Northburn and the rights available to the Beneficiary.

[27] When the wording of clause 3.1 of the Collateral Warranty Agreement is read in the light of the context and the underlying purpose of a collateral warranty, it is clear in our opinion that it incorporates a conventional prescriptive period that corresponds to the statutory period of prescription that applied to Northburn in any claim under the original building contract. Clause 3.1 entitles the defender "to rely on any limitation in the Building Contract" and "to raise the equivalent rights in defence of liability" as it would have had under the building contract. Those words must be given a purposive meaning. Their purpose is clearly to achieve equivalence between the obligations and liabilities undertaken by the defender under the building contract with Northburn and the obligations and liabilities undertaken under the collateral warranty. The right to plead that a claim has prescribed is plainly a right "in defence of liability": that is the function of prescription. It might also be regarded as a "limitation" in the Building Contract, as it restricts the rights of

the original developer, Northburn, to make claims against the contractor. In either event, the wording of the clause is plainly sufficient to include a defence of prescription. On a contextual and purposive interpretation, and having due regard to commercial common sense, the effect of clause 3.1 is to incorporate the same prescriptive period as applied to any claim by Northburn, albeit that that prescriptive period is created by the parties' contractual arrangements rather than by the operation of statutory prescription under the Prescription and Limitation (Scotland) Act 1973, as amended. If further confirmation were required, clause 2.3 of the Collateral Warranty Agreement incorporates the principle of equivalence in express terms, by providing that the Contractor is to have "no greater duty to the Beneficiary ... than it would have if the Beneficiary had been named as the employer under the Building Contract". That provision puts matters beyond doubt.

[28] In clause 3.1 the words in parentheses (see paragraph [24] above) contain a list of exceptions. These relate to rights of counterclaim or set-off, or the right to state "a defence of no loss or a different loss has been suffered by the Employer than the Beneficiary" (*sic*). The reason for excluding these three categories of defence is that they are personal to the party against whom the defence is asserted; in other words, they depend upon certain specific aspects of the relationship between the Contractor on one hand and the original Employer on the other hand. Counterclaim is only relevant if the Contractor and the Employer have claims against each other, as it requires that these claims should be litigated or processed and ultimately set off against each other. The fact that the Contractor and the Employer may have had claims against each other is not relevant to the rights that a Beneficiary might have against the Contractor, as the Contractor does not have the claim against the Beneficiary that it might have had against the original Employer. The same is true of rights of set-off; once again these can only arise if the Contractor and the original Employer had claims against

each other that may be set off, through the right of retention or the assertion of a counterclaim.

[29] The third exception is the defence that either the Employer has suffered no loss or it had suffered a different loss from the Beneficiary of the Collateral Warranty. Once again, such a defence is personal to the Employer, and does not extend to the Beneficiary. So far as no loss is concerned, if a latent defect only becomes apparent after the property has been sold to a purchaser, the Employer will not suffer any loss because it has transferred the property and obtained what must be presumed to be the market price for it. So far as a different loss is concerned, if the Employer makes a claim in respect of a defect that has become apparent during his period of ownership, and subsequently transfers the property to a purchaser, which then becomes aware of a defect that was previously latent, the Employer and the purchaser will have suffered different losses. Neither can make a claim in respect of the loss suffered by the other. This is all that the third exception is designed to achieve; it is based on the fact that a loss may be personal (or specific) to either the Employer or the purchaser from the Employer, the Beneficiary, and in such a case neither of those parties can recover for the loss suffered by the other.

[30] It follows that the exceptions in parentheses in clause 3.1 have no bearing on the basic proposition that the clause is intended to ensure that, as against the Contractor, the Beneficiary of the Collateral Warranty is provided with equivalent rights to the original Employer. Those exceptions are cases where there is no equivalence between the Employer and the Beneficiary, and consequently they are expressly excluded. If anything, that affirms the general proposition, that a collateral warranty is intended to achieve equivalence of rights as between the original owner of a development and any purchaser or tenant or funder who derives rights from the original owner.

Conclusion

[31] For the foregoing reasons we are of opinion that the Collateral Warranty Agreement is intended to confer on the defender as Contractor the same defences against a Beneficiary as would be available against the original Employer, Northburn. For the reasons already given, that means that any claim by the pursuers as Beneficiary under the Collateral Warranty Agreement must be subject to the same prescriptive period, with the same terminus, as would have applied to a claim made by Northburn. That prescriptive period operates by virtue of the parties' contract, as embodied in the Collateral Warranty Agreement, rather than the general statutory law of prescription, but as we have indicated that appears to be the clear meaning of the contract, properly construed.

[32] The defender's liability to the original Employer, Northburn, was extinguished by prescription at latest five years after the report obtained from Colliers International, which described the drainage problems in the car park and attributed them to fault on the part of the defender as Contractor. The effect of clause 3.1 of the Collateral Warranty Agreement is therefore to extinguish any claim by the pursuers against the defender based on the drainage problem.

[33] We are accordingly of opinion the defender's construction of the Collateral Warranty Agreement is correct. We will allow the reclaiming motion, recall the interlocutors of the Commercial Judge, dated 8 January 2019 and 16 January 2019 in so far as dealing with the expenses of the debate, sustain the defender's first plea-in-law to the extent of excluding from probation the pursuers' averments relating to the construction of clause 3.1 of the Collateral Warranty (found in article 6 of condescendence, from "Clause 3.1 of the Collateral Warranty on its proper construction" to the end of the article). We will further repel the

pursuers' first plea-in-law (to the relevancy of the defender's averments), insofar as it relates to issues that were the subject of the present reclaiming motion, and the pursuers' second plea-in-law, which challenges the relevancy of the defender's averments relating to clause 3.1 of the Collateral Warranty. Thereafter we will remit the case to the Commercial Judge to proceed as accords.