7/84

IN THE PRIVY COUNCIL No.42 of 1981

ON APPEAL

FROM THE FEDERAL COURT OF MALAYSIA (APPELLATE JURISDICTION)

IN THE MATTER OF THE RULES OF THE SUPREME COURT ORDER 14 RULE 1

AND

IN THE MATTER OF THE CONTRACTS ACT 1950

BETWEEN :

(1) OOI BOON LEONG
(2) PETER KOK SIEW FATT
(3) HIRAOLD KOWADA — (Defendants) Appellants

- AND -

CITIBANK N.A. — (Plaintiff) Respondent

CASE FOR THE APPELLANTS

1. This is an Appeal by the above-named Appellants, pursuant to leave given on 29th September 1980 by the Federal Court of Malaysia (Appellate jurisdiction (Raja Azlam Shah, acting Lord President and Syed Othman and Salleh Abas, Judges of the Federal Court) from the order on 2nd July 1980 of The Federal Court of Malaysia (Appellate Jurisdiction) (Raja Azlam Shah acting Lord President and Chang Min Tat and Salleh Abas Judges of the Federal Court) allowing the appeal of the above-named Respondent from the Order of Mr. Justice Wan Hamzah of 8th January 1979 allowing the Appeal of the Appellants from the decision of the Senior Assistant Registrar granting the Respondent leave to sign judgment against the Appellants for the amount claimed in the Writ and Statement of Claim with interest and costs. The Federal Court restored the Order of the Senior Assistant Registrar and granted the Respondent leave to sign judgment against the Appellants for the amount claimed in the Writ and Statement of Claim together with interest and costs.

Pages 61-62
Pages 48-49
Pages 37-42
Pages 1-5

2. The issues arising in this appeal are as follows:-

(1) The extent to which a court hearing an application for summary judgment under the Rules of the Supreme Court Order 14 Rule 1 ought to determine disputed questions of fact or law instead of leaving such questions to be determined by the Trial Judge by granting of the Defendant unconditional leave to defend the action.

(2) Whether and if so to what extent the terms
Pages 29-32 of the contract of loan ("the loan contract") made between the Respondent and the principal debtor, Leisure Industries Sdn. Bhd. ("the Company") were incorporated into the contract of guarantee ("the
Pages 8-16 guarantee") made between the Appellants and the Respondent.

(3) Whether and if so to what extent there was a collateral contract between the Appellants and the Respondent whereby in consideration of the Appellants entering into the guarantee, the Respondent would enforce its rights against the Company under the loan contract.

(4) Whether and if so to what extend a party to a contract can validly waive rights conferred by the
Act 136 Contract Act 1950 ("the Act") in the absence of a provision to that effect in the section conferring any such right, having regard to the provisions of Section 1(2) of the Act.

(5) Whether a creditor by express words in a contract of guarantee can validly bind a guarantor to consent in advance to any subsequent variation of the contract between the creditor and the principal debtor for the purposes of Section 86 of the Act.

(6) Whether, notwithstanding any provisions of the contract of guarantee, a guarantor can be held to have consented to a variation of the contract between the creditor and the principal debtor subsequent to the guarantee where the guarantor has not been informed or consulted about such variation.

(7) Whether, in order to discharge to surety from his obligation pursuant to Section 86 of the Act, the variation in the contract between the creditor and the principal debtor must be material or substantial and, if so, whether the test to be applied when determining whether the variation is material or substantial is a subjective or objective test.

(8) Whether, if such a variation must be material or substantial to discharge the surety pursuant to Section 86 of the Act, the burden is upon the surety to establish this or upon the creditor to negative it.

(9) Whether the failure of the Respondent to obtain a valid and fully enforceable debenture on the assets of the Company and to obtain the letters of

undertaking from the holders of 40% of the Company's shares either severally or mulatively amounted to such a variation of the terms of the contract between the Respondent and the Company as to discharge the Appellants from the guarantee pursuant to Section 86 of the Act.

(10) Whether, if the creditor does an act which is inconsistent with the rights of the surety or omits to do any act which his duty to the surety requires him to do and the eventual remedy of the surety against the principal debtor is thereby impaired the surety can lose his right to discharge pursuant to section 92 of the Act by consenting either in advance in the guarantee document or subsequently to all or any acts or omissions of the creditor.

(11) Whether the failures of the Respondent as set out in (9) either severally or cumulatively amounted to such acts or omissions as would discharge the Appellants under Section 92 of the Act.

(12) Whether a creditor by express words in the contract of guarantee can validly bind a guarantor to consent in advance to the loss, variation or parting with possession of any security which the creditor has against the principal debtor for the purposes of Section 94 of the Act.

(13) Whether and if so what extent the Respondent's failures as set out in (9) either severally or cumulatively amounted to a loss or parting with possession of a security without the consent of the Appellants so as to release the Appellants pro tanto of liability to the Respondent pursuant to Section 94 of the Act.

(14) Whether the disclosure of the terms of the loan contract to the Appellants amounted to a representation for them by the Respondent of an intention to enforce its rights under the loan contract and whether, if so, the Respondent not having had such intention, this amounted to such a misrepresentation by the Respondent as to invalidate the guarantee pursuant to Section 95 of the Act.

(15) Whether the guarantee upon its true construction was conditional upon the Respondent obtaining letters of undertaking from all the shareholders, whether such letters would, upon their true construction, amount to a further contract of surety of the indebtedness of the Company to the Respondent and whether, the Respondent having failed to obtain the said letters of undertaking, the guarantee was discharged pursuant to Section 97 of the Act.

(16) Whether and if so to what extent a clause in a guarantee providing that a certificate of an officer of the creditor shall be conclusive as between the creditor and the guarantor as to the amount of the indebtedness of the principal debtor precludes or is capable of precluding the guarantor from raising any defence as to the validity

or enforceability of the guarantee or of any provision thereof.

(17) Whether in the circumstances the Appellants ought to have been granted unconditional leave to defend the action.

3. The facts relevant to this appeal are set out in the Affidavits (affirmations) of the following deponents:

Pages 6-8 — Tan Loong Pung (Affidavit of 20th January 1978)

Pages 22-23 — Peter Kok Siew Fatt (Affidavit of 22nd March 1978)

Pages 23-24 — Hiroald Kowada (Affidavit of 2nd May 1978)

Pages 25-28 — Ooi Boon Leong (Affidavit of 22nd March 1978)

Pages 34-35 — Tan Loong Pung (Affidavit of 23rd May 1978)

4. There having been no decision by any of the Courts considering this matter that any of the facts set out in those Affidavits was so inherently incredible that the Court was entitled to disregard it even though it was deposed to on affirmation, the Appellants will submit that the facts disclosed in those Affidavits are to be taken as agreed or decided facts for the purposes of this Appeal.

5. The material facts disclosed by the said Affidavits are as follows:

(1) The Company was a company limited by shares incorporated in Malaysia pursuant to the Companies Act and at the times material to this action the Appellants were each directors of the Company and between them held 60% of the issued shares

(2) In March 1975, the Company, acting through the Appellants and in particular, the first-named Appellant, Ooi Boon Leong, negotiated with the Respondent for a loan by the Respondent to the Company. Terms were eventually agreed for such loan and were incorporated into the loan

Pages 29-32 — contract made between the Company and the Respondent on 24th March 1976.

(3) The loan contract provided for a two year term loan of M $500,000 and local guarantees of M $100,000, making a total of M $600,000. The following were the express conditions of the loan contract material to this Appeal:

"Security:

(a) A Registered first fixed and floating charge stamped for M$600,000 over all fixed and current assets, both present and future.

(b) Joint and several guarantees M $600,000 signed by Messrs H. Kowada, Ooi Boon Leong and Peter Kok Siew Fatt.

.....

Conditions of disbursements:

Conditional upon the following terms:

(a) Satisfactory completion of securities and documentations.

(b) Letter of undertaking signed by all shareholders not to divest their respective shareholdings without the Bank's prior written consent and to inject additional capital into the Company in the event of cash shortfall as long as the term loan is outstanding.

.....

This commitment is conditional upon the preparation, execution and delivery of legal documentation in form and substance satisfactory to us and to our Solicitors incorporating substantially the terms set forth above.

(4) Following the loan contract, the Appellants executed the guarantee dated 24th March 1975. Pages 8-16

(5) By the guarantee, the Appellants jointly and severally guaranteed payment on demand of all moneys and liabilities then or thereafter owing or incurred to the Respondent from or by the Company on any current or other account or with any manner whatsoever.

The guarantee was limited to M $600,000. The following were the express terms of the guarantee relevant to this Appeal:

> "7. The Bank may at all times without prejudice to this guarantee and without discharging or in any way affecting our liability hereunder and without notice to any of us:
>
> .....
>
> (2) Grant to the customer or to any other person at any time or indulgence
>
> .....
>
> (5) Deal with exchange release modify or abstain from perfecting or enforcing any securities or other guarantees or rights which the Bank may now or hereafter have from or against the customer or any other person;

(6) Compound with the customer or with any other person or guarantor.

8. The liability of any of us hereunder shall not be affected by any failure by the Bank to take any security or by any invalidity of any security taken or by any existing or future agreement by the Bank as to the application of any advances made or to be made to the customer.

.....

16. No one of us shall be discharged or released from this guarantee by any arrangement made after this guarantee or any dealing between the customer and the Bank without our knowledge or consent or by any variation or alteration with our knowledge or consent in the agreement between the customer and the Bank for the making of advances or otherwise giving creditor affording banking facilities to the customer by the Bank.

In order to give full effect to the provisions of this guarantee each of us hereby waive all rights inconsistent with such provisions and which we might otherwise as sureties be entitled to claim and enforce and we declare that the Bank shall be at liberty to act as though we or each of us were principal debtors or principal debtor to the Bank for all payments guaranteed by us as aforesaid to the Bank.

.....

19. ..... A certificate by an Officer of the Bank as to the money and liabilitites for the time being due or incurred to the Bank from or by the customer shall be conclusive evidence in any legal proceedings against us or any one of us or our personal representatives.

20. This guarantee shall be in addition to and shall not be in any way prejudiced or affected by any collateral or other security now or hereafter held by the Bank for all or any part of the money hereby guaranteed ....."

(6) Each of the Appellants entered into the guarantee on the basis that the Respondent would obtain the additional securities provided for by the loan contract and, in particular, on the basis that the Respondent would obtain a valid debenture from the company and would obtain the necessary undertakings from all the shareholders.

Pages 22, 23 + 25

(7) On 6th May 1975 the Company executed a document purporting to be a debenture and delivered it to the Respondent. Page 26

(8) The debenture was not a good and valid debenture and was defective in that it did not empower a receiver appointed by the debenture holder to get in and sell the assets of the Company charged by the debenture. The debenture was therefore without any effective means of enforcement without recourse to the Courts. Page 26

(9) The Respondent obtained letters of undertaking from each of the Appellants as shareholders of the Company but failed or neglected to obtain any letter of undertaking from any other shareholder. The shareholders from whom no undertaking was obtained held an aggregate of some 40% of the issued share capital. Page 27

(10) The advances were made by the Respondent to the Company and the Company defaulted. Demands were made on the Appellants pursuant to the gurantee in the sum of M$302,152.67 and interest by letters dated 23rd September and 8th October 1977. Pages 17 to 21

(11) By letter dated 17th October 1977, the first-named Appellant, Ooi Boon Leong, through his Solicitors, denied liability under the guarantee. Page 21

(12) At some time in January 1978, receivers were appointed pursuant to the debenture and on discovering that they had no powers of enforcement of the charge, the receivers had to apply to the High Court by an Originating Summons dated 4th February 1978. It was not until 21st March 1978 that an Order was made granting the power of sale to the receivers. That order was subject to an appeal at the date of the hearing before the Senior Assistant Registrar Pages 33+34 Page 40

6. By a Writ endorsed with a Statement of Claim issued in the High Court of Malaya on the 13th December 1977 and numbered 3631 of 1977, the Respondent claimed against the Appellants jointly and severally the sum of M$331,731.32 together with interest and costs. On 21st January 1978, the Plaintiff issued a summons for judgment under the Rules of the Supreme Court Order 14 Rule 1. The application was heard by the Senior Assistant Registrar on 26th May 1978 and leave was granted to the Respondent to sign judgment against the Appellants for the sum claimed in the Statement of Claim together with interest and costs. The reasons of the Senior Assistant Registrar were set out in written "Grounds of Decision." Pages 5-6 Pages 37 to 42

Page 43

7. By a Notice of Appeal of 31st May 1978, the Appllants appealed to the Judge in Chambers against the decision of the Senior Assistant Registrar. The appeal was heard before the Honourable Mr. Justice Wan Hamzah on 8th January 1979. The Learned Judge found that there were several triable issues raised by the Appellants' Affidavits and he set aside the order of the Senior Assistant Registrar and granted the Appellants

Pages 48-49

unconditional leave to defend the action.

8. By a Notice of Appeal of 22nd January 1979 and a Memorandum of Appeal of 19th February 1979,

Pages 51-53

the Respondent appealed against the decision of Mr. Justice Wan Hamzah to the Federal Court of Malaysia (Appellate Jurisdiction). On 2nd July 1980, the Federal Court of Malaysia (Appellate Jurisdiction) (Raja Azlam Shah, acting Lord

Pages 60 and 61

President and Chang Min Tat and Salleh Abas, Judges of the Federal Court) allowed the Respondents' appeal and gave the Respondents leave to sign judgment for the sum claimed together with interest and costs. In its judgment, the Court decided that none of the matters raised in the said Affidavits disclosed a triable defence

Pages 53-59

to Respondent's claim.

9. By a Notice of Motion dated 27th August 1980, the Appellants sought the leave of the Federal Court of Malaysia to appeal to His Majesty the Yang Di-Pertuan Agong in Council ("the Privy Council") and on the 29th September 1980, the Federal Court of Malaysia (Appellate Jurisdiction) (Raja Azlam Shah, acting Lord President, and Syed Othman and Salleh Abas, Judges of the Federal Court) granted the Appellants leave to appeal to the

Pages 63+64

Privy Council against the order of the Federal Court of Malaysia (Appellate Jurisdiction) of 2nd July 1980.

10. The statutory provisions relevant to this Appeal are as follows:

Act 136

<u>The Contract Act 1950</u>

"1 (2) Nothing herein contained shall affect any written law or any usage or custom of trade, or any incident of any contract, not inconsistent with this Act.

86. Any variance made without the surety's consent in the terms of the contract between the principal debtor and the creditors, discharges the surety as to transactions subsequent to the variance.

92. If the creditor does any act which is inconsistent with the rights of the surety, or omits to do any act which his duty to the surety

required him to do, and the eventual remedy of the surety himself against the principal debtor is thereby impaired, the surety is discharged.

94. A surety is entitled to the benefit of every security which the creditor has against the principal debtor at the time when the contract of suretyship is entered into, whether the surety knows of the existence of such security or not; and if the creditor loses or, without the consent of the surety, parts with the security, the surety is discharged to the extent of the value of the security.

95. Any guarantee which has been obtained by means of misrepresentation made by the creditor, or with his knowledge and assent, concerning a material part of the transaction, is invalid.

97. Where a person gives a guarantee upon a contract that the creditor shall not act upon it until another person has joined in it as co-surety, the guarantee is not valid if that other person does not join".

The Rules of the Supreme Court Order 14

"Rule 1 - Where in an action to which this rule applies a statement of claim has been served on a defendant and that defendant has entered an appearance in the action, the plaintiff may on the ground that defendant has not defence to a claim included in the writ, or to a particular part of such claim, or has no defence to such a claim or part except as to the amount of any damages claimed, apply to the Court for judgment against that defendant.

(2) Subject to paragraph (3), this rule applies to every action begun by writ in the Queen's Bench Division (including the Admiralty Court) or the Chancery Division other than -

(a) an action which includes a claim by the plaintiff for libel, slander, malicious prosecution, false imprisonment or seduction.

(b) an action which includes a claim by the plaintiff based on an allegation of fraud, or

(c) an Admiralty action in rem.

(3) This Order shall not apply to an action to which Order 86 applies.

11. The Appellants contended and now contend as hereinafter set out.

12. A. The Function of the Court under RSC Order 14 Rule 1

The Appellants contend that the function of the

Court hearing an application for summary judgment under RSC Order 14 Rule 1 is to determine whether, on the evidence filed, the Defendants have a triable defence to the Plaintiff's claim. Leave to defend should be refused only in cases where the matters raised by way of defence are clearly unarguable. "The summary jurisdiction conferred by this Order must be used with great care. A Defendant ought not to be shut out from defending unless it is very clear indeed that he has no case in the action under discussion" per Lord Esher M.R. in Sheppards & Company v Wilkinson & Jarvis. The power to award summary judgment is "intended only to apply to such cases where there is no reasonable doubt that a Plaintiff is entitled to judgment and where therefore it is inexpedient to allow a Defendant to defend for mere purposes of delay." Per Lord Halsbury L.C. in Jones v Stone.

(1889) 6TLR 13.

(1894) AC122 at p.124

13. Where a case involves a difficult point of law, then, unless the Court is satisfied that the point is really unarguable, leave to defend should be given automatically "I do not think that Order 14 providing for summary judgment, applies to cases like this, raising what might turn out to be a difficult question of law. It was never intended to throw on the Judges in Chambers such a burden. It is impossible such questions could be satisfactorily delat with at Chambers". per Wills J. in The Electrical and General Contract Corporation v The Thomson-Houston Electric Company.

(1893) 10 TLR 103

14. It is not necessary for a Defendant to show that his intended defence must necessarily succeed but merely that it is arguable. "If there is a fair probability of a defence, a Defence ought to be allowed," per Wills J. in Ward v Plumbley

(1890) 6 TLR 198

15. The Appellants contend that the Federal Court approached the matter in the wrong way in saying: "We have often said in this Court many times that where all the issues are clear and the matter of substance can be decided once and for all without going to trial there is no reason why the Assistant Registrar or the Judge in Chambers or, for that matter this Court, shall not deal with the whole matter under the RSC Order 14 procedure."

Page 59

16. In the Appellants' contention, the correct approach was that adopted by Mr. Justice Wan Hamzah who ennumerated the issues raised by the Appellants, decided that these issues were triable and gave leave to defend accordingly.

Pages 46-48

17. This is a case which clearly raises difficult and fundamental questions of law. In particular, the question of whether a guarantor could, in effect, "contract out of" sections of the Act was a fundamental question and, to a large extent, a novel question. In the argument of Counsel for the Appellants before Mr. Justice Wan Hamzah, it was specifically argued that the case raised a "new legal point" and there is no record that this submission was rebutted by Counsel for the Respondent or rejected by Mr. Justice Wan Hamzah. Page 45

18. B. Were the Terms of the Loan Contract incorporated into the Guarantee?

On the evidence before the Court, it was and is arguable by the Appellants that the loan contract and the guarantee, which were executed by the same persons on the same day (albeit that the Appellants executed the loan contract in their representative capacity and the guarantee in their personal capacity) were so closely linked that the guarantee incorporated the terms of the loan contract so as to place upon the Respondent the obligation to the Appellants to obtain securities provided for by the loan contract. It was the evidence of all three Appellants that they entered into the guarantee on that basis. Pages 22,23 25

19. There can be no objection in law to a guarantee being concluded in more than one document or a guarantee being made partly orally and partly in writing. Under Malaysian law (as opposed to English law) a contract of guarantee may be either oral or written - Section 79 of the Act.

20. Although the guarantee was in general terms and guaranteed all the indebtedness of the Company to the Respondent, it was in fact executed for the immediate purpose of guaranteeing a specific loan, being the loan provided for by the loan contract. It would not therefore be inconsistent with the business efficacy of the guarantee were the essential terms of the loan contract to be incorporated into it.

21. The Court should look at the substance rather than the form of the transaction and if the Court were to be satisfied, at the trial of the action, that notwithstanding the express words of the printed guarantee, the transaction between the Respondent and the Appellants was such that the contract of guarantee incorporated the obligations of the Respondent under the loan contract, then the Court would be entitled and bound to give effect to the true nature of the transaction rather than merely to the words of the document.

22. Whether and to what extent the terms of the loan contract were incorporated into the guarantee

by the words or conduct of the parties would be a matter to be determined, almost certainly upon the hearing of oral evidence, at the trial of the action. It is the Appellants' contention that, on the material before the Court, the Court could not properly have ruled (as, by inference, it must have ruled) that there was no reasonable possibility of the Appellants persuading the Court of trial that the guarantee incorporated some or all of the conditions of the loan contract.

23. If the Appellants were successful in establishing that the guarantee incorporated the terms of the loan contract with regard to security, then a breach of such a fundamental condition by the Respondent could properly be treated by the Appellants as a repudiation of the contract between the Appellants and the Respondent and that such repudiation had been effectively accepted by the Appellants by the
Page 21 denial of liability of 17th October 1977.

24. C. A Collateral Contract?

It must be accepted that it was not argued in terms before any of the lower Courts that there had been a collateral contract between the Appellants and the Respondent that, in consideration of the Appellants executing the guarantee, the Respondent would enforce its rights under the loan contract and, in particular, would obtain the various forms of security therein set out. The Appellants contend, however that it is open to them to raise this argument before the Privy Council for the following reasons:

(a) The argument that there was a collateral contract is dependent upon the same averments as the argument that the terms of the loan contract were incorporated into the guarantee itself. The evidence of the Appellants as to the basis upon which they entered into the gurantee is equally consistent with the terms of the loan contract being incorporated into the guarantee and a collateral contract to the same effect. The essentials of the argument have therefore been before the lower Courts even though the argument may not have been unequivocally spelled out.

(b) The Appellants will contend that the rule against raising arguments on appeal that were not raised at the lower Courts either has no application or should not be so strictly applied in cases where a Defendant is seeking to establish a triable defence under Order 14. The Appellants contend that it should be sufficient if they can establish at any stage in

the original or appellate proceedings under Order 14 that they have a triable defence, any questions of whether or not the argument should have been raised below being adequately dealt with by orders as to costs. "If the Divisional Court has shut out a Defendant from defending an action, then the Court (of Appeal) considering the rule (Order 14) a hard one, would look if there were any plausible defence to the action." Per Lord Esher M.R. in Wardens of St. Saviour's v Gery (1887) 3 TLR 667 at p.668.

25. If the Appellants were able to establish, by oral evidence or otherwise their contention that they entered into the guarantee in reliance upon the Respondent's promise to take the security provided by the loan contract, then it should be open to the Court to hold that there was a collateral contract between the Appellants and the Respondent. If such a collateral contract existed, the Respondent is in breach of that contract and the loss flowing from such breach would be the difference between the claim under the guarantee and the moneys that would have been recovered from the Company if proper security had been taken and enforced. Such relief would be available to the Appellants by way of set-off and Counterclaim in the action.

26. D. Can a Party to a Contract validily waive rights conferred by the Act?

The general rule is to be found in Section 1(2) of the Act. The Act does not affect any incidentof any contract which is not inconsistent with the Act and it is submitted that it must follow from that that, in respect of any incident of a contract which is inconsistent with a provision of the Act, the Act must prevail. Were it otherwise, the rule would be that the Act was to apply save where the parties agreed to the contrary.

27. The Appellants will contend that the policy of the Act and of the Indian Contracts Act 1870 ("the Indian Act") was that, where parties were to be entitled to contract for obligations inconsistent with the provisions of the Act, this would be specifically provided for in the relevant section. There is therefore a distinction between sections, such as 86, 92, 94, 95 and 97 which do not provide the right for parties to contract in a different sense and sections such as 105 and 116 which do so provide by use of such words as "in the absence of any special contract" or "in the absence of any contract to the contrary".

27. The Appellants contend that Section 1 (2) of the Act and the identical section of the Indian Act have always been treated as invalidating any

inconsistent provision in a contract save where a specific right to contract in a contrary sense has been conferred by the Act: see KR Chitguppi and Company v Khadilkar and in particular the judgment of Hayward J.

A.I.R. 1921 Bombay 164 at p.166

28. It was and is, therefore, the Appellants' contention that the words in Clause 16 of the Guarantee "in order to give full effect to the provisions of this guarantee each of us hereby waive all rights inconsistent with such provisions and which we might otherwise as sureties be entitled to claim and enforce" cannot as a matter of law operate as a waiver by the Appellants of any of the rights conferred on them by Sections 86, 92, 94, 95 and 97 of the Act.

29. The Appellants will further contend that the Federal Court failed even to consider the question of whether Section 1(2) of the Act rendered void or unenforceable any purported waiver of rights conferred by other sections in the Act where those sections did not themselves provide a right to contract out of their provisions.

30. The Appellants will therefore contend that the question of whether Section 1(2) invalidates any purported waiver of rights conferred by the Act was a difficult and fundamental question of law, applicable not only to the dispute before the Court but to many other contracts and disputes, that such authority as there was on the question was in favour of the Appellants' contentions (and in particular Chitguppi and Company v Khadilkar, supra) and that this question was neither properly considered nor correctly decided by the Federal Court.

31. E. Can a guarantor consent in advance to a variation of the contract between the creditor and the principal debtor?

Section 86 of the Act applies only where there has been a variance in terms of the contract between the principal debtor and the creditor which have been made without the surety's consent. It was not argued on behalf of the Respondent that, if there had been a variation of the contract between the Respondent and the Company, the Appellants had been consulted about such variation and had given actual consent to it. The case for the Respondent was that, by the express words of the guarantee, the Appellants contracted in advance to consent to any variation which the Respondent might subsequently make in the loan contract.

32. It is the Appellant's contention that a general consent given in a guarantee to any future variation of the contract between the creditor and the principal debtor cannot be a valid consent for the purpose of Section 86.

33. Firstly it is argued that to uphold such a general consent would be to defeat the purpose of Section 86 of the Act. The purpose of this section is clearly to protect sureties from oppressive conduct by creditors arising from the fact that in the overwhelming majority of cases, the fact that a creditor is entitled to insist on having the loan guaranteed by the surety is a clear indication of the dominant position of the creditor in the transaction. If a debtor is in a dominant position, he can insist on the loan being without surety. To hold, therefore, that, by general words in a standard form printed guarantee, a creditor can compel the guarantor to consent to all variations of the principal contract loan it would be to render Section 86 of the Act nugatory, particularly as experience shows that most professional lenders (e.g. banks, finance companies and the like) insert a consent clause into their standard form guarantee documents.

34. Secondly, the Appellants will say that the word "consent" must mean a genuine consent and that such a consent can only be given by someone who has knowledge of the thing to which he is consenting. Although, therefore, a contract of guarantee might on its face purport to give the "consent" of the guarantor to the variation in the principal loan contract, this is not a genuine "consent" but is merely a power conferred on the creditor. If that power is exercised without the genuine consent of the surety, it is contended that this does not protect the creditor from Section 86 of the Act.

35. Thirdly, in so far as there is any decided authority on Section 86 of the Act or Section 133 of the Indian Act, which is its equivalent, that authority is in support of the Appellants' proposition. The Appellants again cite Chitguppi & Company v Khadilkar supra, and will say that the ratio of that case has been adopted by the Malaysian Courts in the case of Heng Cheng Swee v Bangkok Bank Limited (1976) 1 MLJ 267 although, on the facts in that case, the Judge at first instance and the Federal Court held that there had not been any variance of the principal loan contract.

36. Fourthly, the Appellants contend that the Federal Court was wrong to approach the question as if the law of Malaysia were the same as the law of England. The law of England with regard to the release of a surety by variation in the principal loan contract is a matter of common law contained in the decided authorities and is thus capable of expansion or

modification by the Courts in the light of changing social conditions and to the overruling by a higher Court of a decision of a lower Court which may have stood for many years. The question in this case, however, is one of the interpretation of the provisions of a particular statute. The Appellants will therefore contend that the approach of the Federal Court in treating the common law of England and the statute of Malaysia as identical was fundamentally wrong.

Pages 57-59

37. Fifthly, even if were permissible to have regard to English authorities, regard should be had mainly to those authorities which stated the law as it existed at or about the time of the Indian Act (i.e. 1870) in that, even if the Indian Act, upon which the Malaysian Act was based) was intended to enshrine any existing law, it can only have intended to enshrine the law as it existed at the time when it was passed, being intended as a codifying Act.

38. Accordingly, if one has regard to the law existing at the time when the Indian Act was passed and in particular to the case of Holme v Brunskill the Appellants will contend that those cases support the proposition that consent must be given genuinely and after consultation. The passage from the judgment of Cotton L.J. in Holme v Brunskill cited by the Federal Court is clearly indicative of the view of the English Court of Appeal that "if there is any agreement between the principals with reference to the contract guaranteed, the surety ought to be consulted."

(1878) 3 QBD 495

Pages 56 & 57

39. The Appellants therefore maintain that both on principle and on authority, a general consent given in advance in a contract of guarantee cannot amount to such a "consent" as to take a variation of the principal loan contract out of the provisions of Section 86 where there has been no genuine consent given to the variation at the time it was made.

40. F. Is Consultation Essential to a Valid Consent?

The Appellants will contend that, irrespective of whether a guarantor may validly consent in advance to subsequent variations in the principal loan contract, the law imposes on the creditor a duty to inform the guarantor of any proposed change and to consult him about it. The purpose of such a duty to consult would be to enable the guarantor to reconsider his position in the light of the proposed change of circumstances and in particular, to decide whether he wished to continue with the guarantee or to terminate it in accordance with its provisions.

41. In support of the contention that there is a duty to consult, the Appellants will rely upon the judgment of cotton L.J. in Holme -v- Brunskill, supra and the speech of Lord Loughborough L.C. in Rees v Berrington (1795) 2 BFS. 540 at P.543

42. G. Must a variance be substantial or material to discharge the Surety under Section 86 and what is the onus of proof on this issue?

The Appellants concede that there are dicta in several English authorities to the effect that a variation in the principal loan contract must be substantial. The Appellants contend, however, that the Federal Court was wrong both in having regard to those authorities rather than to the words of Section 86 of the Act and in the interpretation place upon the authorities themselves.

43. The Appellants contend that the Federal Court did not purport to construe Section 86 of the Act nor did it give any consideration as to whether the words of the Act might lead to a different result from a consideration of the decided English cases. The Federal Court treated the English cases as being declaratory of Malaysian law rather than approaching the matter by way of interpretation of the Section itself.

44. In any event, the Appellants will contend that the English authorities do not necessarily establish the principle that the variation in the principal loan contract must be material to discharge the surety. In Polak -v- Everett Blackburn J. said: (1876) 1QBD 669
"It has been established for a very long time .....that on the principles of equity a surety is discharged when the creditor, without his assent, gives time to the principal debtor, because by so doing he deprives the surety of part of the right he would have had from the mere fact of entering into the suretyship, namely, to use the name of the creditor to sue the principal debtor, and if this right be suspended for a day or an hour, not injuring the surety to the value of one farthing, and even possibly benefitting him, nevertheless, by the principle of equity, it is established that this discharges the surety altogether". Mellor J. said "..... the surety is entitled not to be affected by anything done by the creditor, who has no right to consider whether it might be to the advantage of the surety or not. The Surety is entitled to remain in the position in which he was at the time when the contract was entered into" Quain J. said: "I think that convenience and policy of the matter .....is that the contract of the surety should not be altered without his consent .....". At pages 673 & 674 At pages 676 & 677 Page page 677

(1876) 2CPD 46

45. In Croydon Gas Co. v Dickinson, Bramwell J.A. said: "There are three ways in which the surety might be discharged. First, by time being given to the debtor; secondly by an alteration in the contract between the principal; and, thirdly, by the principals dealing together so as to effect the position of the surety to his prejudice."

At page 49.

46. As to the dictum already cited of Cotton L.J. in Holme v Brunskill supra, the Appellants will say that the dictum is to be read in its context and in particular in the light of the words of Cotton L.J. later in the same judgment: "the Plaintiff .....relied on various dicta to the effect that any material change in the contract between the principals will discharge the surety. Even if by these expressions the Judges intended to state that to have the effect of releasing the surety the alteration must be material, it does not follow that they intended to lay down no alteration would discharge the surety unless the Jury in an action to enforce his liability held it to be material, or to express an opinion at variance with the rule laid down by me. The case of Sanderson v Aston was specially relied on by the Plaintiff ..... If the decision is to be considered as based on the reason given by Pollock, B. that the Court was entitled to consider whether the alteration was material, it cannot, in our opinion, be sustained."

~~At page~~ 506

47. Further, if it were the rule that a variation in the principal loan contract must be material to discharge the surety, the Appellants contend in the light of the judgment of Cotton L.J. supra, that, in so far as there is any onus upon a party in the matter, the onus is upon the creditor to demonstrate that it is self-evident that the variation is either unsubstantial or of benefit to the surety.

48. The Appellants contend, however, that the Federal Court ought to have approached the matter as one of statutory interpretation and that in Section 86 of the Act, the words "any variance" must be read literally. There is no authority for reading into the express words of Section 86 any qualification such as "material" or "substantial". The Appellants will contend that the legislature intend to lay down an absolute rule that a surety is discharged when there has been any variation of the principal loan contract without a Court inquiry as to the effect of that variation upon the surety. Furthermore, this would be in accordance with the law as expressed by the Judges in Pollack v Everett, supra.

49. H. Was there in this Case a variation of the Loan Contract without the consent of the Appellants so as to discharge the guarantee?

The Appellants will contend firstly that the affect of the guarantee, upon its true construction, is not that the Appellants consent or bind themselves to consent to any further variation in the loan contract. The only relevant clause, in the submission of the Appellants, is Clause 16, which clearly contemplates that variations may be made without the knowledge or consent of the surety. The effect of the Clause, upon its true construction, is not that the guarantors consent to the variation but that they waive the rights that the variation would give them. If, therefore, a waiver is impossible by reason of Section 1(2) of the Act, then the Clause will not take effect as a consent for the purposes of Section 86 of the Act.

50. The Appellants therefore contend that, upon the true construction of the guarantee, they cannot be taken to have consented to any variation in the loan contract.

51. The Appellants maintain that the failure of the Respondent to obtain a valid debenture and to obtain letters of undertaking from the remaining shareholders is, on its face, a variation of the loan contract. The Company was bound to give a valid debenture and to procedure the undertakings of the shareholders and the Respondent had the right to enforce that obligation. By waiving those obligations or by deliberately deciding not to enforce them, the Respondent had varied the loan contract.

52. If, as the Appellants contend, it is necessary for a guarantor to be consulted prior to such a variation, there is no allegation that in this case there was any such consultation.

53. If, contrary to the Appellants' contentions, a variation must be material, then the Appellants will say firstly that in their judgment the variations are material and that this should be sufficient and secondly, in the alternative, that the variations are material when viewed objectively.

54. The failure to take a valid debenture meant that, when receivers were appointed, they could not get in and sell the property of the Company for some two months and there is no evidence before the Court to the effect that the assets and liabilities of the Company remained static during that period of delay. It is the Appellants' case that, if the debenture had been a proper and valid debenture, the receivers would have been able to act much more swiftly to preserve the assets of the Company with the result that the deficit might not have been so large.

Page 58.

55. As to the failure to get letters of undertaking, it is the Appellants' contention that the Federal Court failed to appreciate the significance of the argument that was being advanced. The main value of the letters of undertaking was not the restriction on the disposal of the shares but the undertaking of the shareholders" to inject additional capital into the Company in the event of cash shortfall as long as the term loan is outstanding."

Page 31

56. The letters of undertaking, therefore, were intended to be a form of further surety by the shareholders agreeing to put money into the Company, thereby preserving the assets charged by the debenture.

57. The Appellants therefore submit that it was not "self-evidence" that the variations were immaterial or insubstantial.

58. The Appellants therefore contend that they have a strongly arguable defence under Section 86 of the Act.

59. <u>I. Is the Consent of the Guarantor relevant to Section 92 of the Act?</u>

It is the Appellants' case that the Federal Court failed to give any consideration to the effect of Section 92 on the obligations of the Appellants and wrongly treated the case as if Section 86 and 92 were in pari materia.

60. As is shown by the examples to Section 92, the effect of this Section is not confined to breaches by the creditor of a term of the contract of guarantee. A Court must therefore have regard to the wider rights of the surety and obligations of the creditor.

61. As to the illustrations to Section 92 of the Act show, the Section intends to reproduce the rule of common law that the creditor is under an obligation not to do anything which will diminish the eventual remedies of the guarantor against the principal debtor. The Appellants contend that a creditor cannot divest himself of this obligation by express words in the contract of guarantee.

62. Firstly, were a creditor able to do so, the Section would be rendered nugatory as virtually all guarantees by professional lenders contain wide clauses empowering the creditors to do acts which would have the effect of diminishing the surety's rights against the principal debtor. Irrespective, therefore, of whether parties can

contract out of rights and obligations created by the Act in the light of Section 1(2) of the Act, the Appellants will contend that Section 92 creates rights and obligations which are external to the contract of guarantee and cannot be effected by it.

63. Secondly, unlike other Sections of the Act (for example Section 86 supra) this Section does not import any concept of the surety's consent. In view of the introduction of the consent of the surety into the other Sections, the appellants will argue that the silence of Section 92 on this point means that the Section must be interpreted as discharging the surety in the event of any act or omission within the Section, irrespective of the consent of the surety or at least irrespective of any consent given in advance in the guarantee document.

64. J. Do the Appellants have a Triable Defence under Section 92?

The Appellants will contend that, in so far as the Federal Court dealt with the Appellants' case under Section 92 (which is not admitted), the Court applied the incorrect test. The test which ought to have applied is whether the matters set out in the Affidavits raised a triable defence under Section 92, Only if it was self-evident that they could not amount to such a defence ought leave to defend have to have been refused.

65. It is impossible, in the Appellants' contention, to say that the matters raised in the Affidavits cannot properly be argued to be acts inconsistent with the rights of the guarantor or omissions by the creditor. That these failures impaired the Appellants' rights against the Company must, in the Appellants' submission, be clear. A failure to obtain a proper debenture must prejudice a surety who is entitled to the benefit of securities under Section 94. Similarly, a failure to obtain an undertaking by the remaining shareholders to put money into the Company must impair the Appellants' rights against the Company in that the assets of the Company are diminished.

66. K. Can the Guarantor, by words in the Guarantee Document consent in advance to the loss of a security for the purpose of Section 94?

The Appellants will contend that this matter also was one which was not given adequate or separate consideration by the Federal Court.

67. As to the question whether in principle a surety can be compelled to consent in advance to a loss of the security by express words in the guarantee documents, the Appellants will say that the matter is governed by the same considerations that governed the

consent of the surety to a variation of the principal loan contract under Section 86 and the Appellants therefore repeat mutatis mutandis the contentions set out in the paragraphs dealing with that Section.

68. L. Do the Appellants have a Triable Defence under Section 94?

The Appellants' first contention is that, irrespective of whether a guarantor can validly consent in advance to parting with a security in the guarantee document, the guarantee in this case does not, on its true construction, operate as a consent by the Appellants. The Appellants contend that the true constructions of Clauses 7, 8 and 16 is that they contain a purported waiver by the Appellants of their rights against the Respondent as created by the Act and not a consent to the loss or parting with the security. In particular, Clause 7 contemplates various acts will be done "without notice" and hence, the Appellants would argue, without consent. Clause 8 is, on its face merely a waiver of rights. Clause 16 is expressly applicable to acts taken by the Bank "without our knowledge or consent". The Appellants therefore contend that, upon their true construction, these Clauses do not give any consent to the failures complained of.

69. Secondly, it cannot be and has not been contended that the Appellants gave any real consent to the two failures complained of.

70. Thirdly, the Appellants contend that both the debenture, if fully valid, and the letters of undertaking, if exacted from the other shareholders, would have constituted security for the loan and the creditor had the right to those securities before the contract of guarantee was entered into. The effect of subsequently taking a defective debenture from the company was to lose or part with the value of the debenture, turning it from a remedy which was instantly exercisable upon default to one which could be exercised only after considerable delay and an application to the Court. By failing to take the letters of undertaking from the remaining shareholders, the creditor effectively abandoned that security altogether.

71. There was no material before any of the Courts upon which it could properly have been held that the diminution in the value of the two securities was either non-existent or minimal so as to force the Court to the conclusion that, even if the surety were discharged to the extent of the value of the

security, such discharge would either be of no amount whatsoever or for an amount so small as not to justify granting leave to defend. It was therefore not open to the Federal Court to apply the rule "de minimis non-curat lex." Page 57.

72. The Appellants will contend that the proper course to take with regard to Section 94 is to grant the Appellants unconditional leave to defend so that, if they can establish that a security has been lost or parted with without their consent, there can then be an inquiry as to the value of such a security.

73. M. Can the Appellants invoke Section 95 of the Act?

It is accepted that this point was not raised in the lower Courts. As to whether the Appellants are entitled to raise this matter in the Privy Council, the Appellants repeat the contentions made under C. supra.

74. It is the Appellants' contention that the loan contract obliged the creditors to obtain a valid debenture over the company's assets. If it was the intention of the Respondent to use its standard form debenture and that debenture did not give effective powers to the receiver, then there must have been an intention on the part of the Respondent at the time when the loan contract and guarantee were executed to procure a debenture fundamentally different from the debenture which the Appellants were entitled to expect in the light of the loan contract. It is therefore open to the Appellants to argue that by entering into the loan contract, the terms of which were disclosed to and known by the Appellants, the Respondent effectively represented that it had the present intention of obtaining a valid debenture from the Company whereas the intention was to obtain a debenture which would be ineffective.

75. It is also open to the Appellants to contend that, notwithstanding the express provisions of the loan contract, the Respondent did not at that time or subsequently have any intention of obtaining letters of guarantee from the shareholders other than the Appellants.

76. In the circumstances, there were representations of present intention which were not correct. The Appellants will therefore contend that they entered into the guarantee in reliance on misrepresentations as to the genuine intentions of the Respondent and that they would not have entered into the guarantee had they known the Respondent did not intend to obtain a valid debenture or obtain letters of undertaking from the other shareholders.

Such a contention, if correct, would invalidate the guarantee under Section 95.

77. The question of whether the terms of the guarantee oust the rights of the Appellants under Section 95 does not here arise because the terms of the guarantee do not purport to exclude liability or misrepresentation or any other consequences flowing from a misrepresentation.

78. N. Can the Appellants invoke Section 97 of the Act?

Again, this was not a point raised in the lower Courts and the Appellants will repeat their arguments as to whether it is open to them to raise the matter at this stage.

79. The Appellants contend that the letters of undertaking which were to be obtained under the loan contract were, upon their proper construction, guarantees by those shareholders of the Company's indebtedness to the Respondent. The Appellants will say that there is no difference in principle between a contract to pay the creditor on default by the principal debtor and the contract with the creditor to pay money to the principal debtor on demand by the creditor in order to enable the principal debtor to pay the creditor.

80. If, therefore, the contract between the Respondent and the Appellants, upon its true constructions, obliged the Respondent to obtain the letters of undertaking from the remaining shareholders, then, if the Respondent failed to obtain such letters, the guarantee is rendered invalid by Section 97.

81. O. Does Clause 19 of the guarantee preclude the Appellants from raising any defences as to the validity or enforceability of the guarantee?

Page 15

The Appellants contend that, upon its proper construction, clause 19 of the guarantee provides that a certificate by an officer of the Respondent shall be conclusive evidence as between the Respondent and the Appellant of the indebtedness of the principal debtor, namely the Company. The clause does not purport to make the certificate of the Respondent's officer conclusive evidence of the indebtedness of the guarantors, namely the Appellants. Although the Judgment of the Federal Court may be said to be ambiguous upon this point, as making the certificate conclusive evidence of the indebtedness of the guarantors, thereby precluding the guarantors from raising any defence as to the validity or enforcibility of the guarantee. The judgment contains the following sentence:

'In the present case the guarantee contains a clause which enables the Bank by producing a certificate of indebtedness by its officer to dispense with legal proof of the actual indebtedness of the Respondents.' Page 59

82. Although, therefore, the Appellants will contend that, reading the Judgment as a whole, the Federal Court went no further than to hold that such a certificate was conclusive evidence of the indebtedness of the principal debtor, the Appellants will seek to have any ambiguity in the Judgment resolved because the Judgment of the Federal Court is being widely accepted by Courts in Malaysia as authority for the proposition that a clause such as Clause 19 of the guarantee does preclude a guarantor from raising any defence as to the validity or enforcibility of the guarantee.

83. The Appellants argue first that the clause, upon its true construction, makes the certificate conclusive evidence only of the indebtedness of the principal debtor. In support of that contention, the Appellants cite and rely upon the authorities cited by the Federal Court in its Judgment, namely Dodds v. National Bank of Australasia Limited* and Bache & Company (London) Limited v. Banque Vernes et Commerciale de Paris S.A.**

*(1935) 53 Clr 643
**(1973) 2 Ll. Rep.437

84. Secondly the Appellants will contend that, even if a clause such as clause 19 of the guarantee could be construed so as to preclude defences being raised as to the validity or enforcibility of the guarantee, the Appellants will argue that such a clause could not preclude the guarantor from relying upon the rights created by the Act and that those rights must override the conclusiveness of any clause such as clause 19. In this context, the Appellants repeat the contentions raised in section D, above.

85. Thirdly, the Appellants will argue that, whereas a clause such as clause 19 would not be contrary to public policy if it merely made the certificate conclusive evidence of the indebtedness of the principal debtor - see Bache's case (above) - such a clause would be contrary to public policy if it purported to exclude the guarantor from raising any defence as to the validity or enforcibility of the guarantee. The Appellants argue that such a clause will be contrary to public policy firstly because it would permit a creditor effectively to "contract out of" the Act and all the provision in the Act designed to protect guarantors, secondly because such a clause would directly aid wrongdoers in that, if taken literally, it would preclude the guarantor raising any defence even defences of fraud and duress and thirdly because the clause purports to oust the jurisdiction of the Courts.

86. P. Conclusion

In the premises, the Appellants submit that the judgment of the Federal Court was wrong and that the Order of the Federal Court should be set aside and that the Order of Mr. Justice Wan Hamzah should be restored and that the Respondent should be ordered to pay the Appellants' costs of the appeal to the Federal Court and to the Appeal, for the following amongst others.

R E A S O N S

(1) BECAUSE the Federal Court failed to apply the correct principles for the determination of an application under the Rules of the Supreme Court Order 14 Rule 1.

(2) BECAUSE the Contract of Guarantee between the Respondent and the Appellants incorporated the terms of the contract of loan between the Respondent and the principal debtor and the Respondent is arguably in breach of its obligations under the Loan Contract and hence the guarantee.

(3) BECAUSE the Respondent was in breach of its obligations under a collateral contract between the Appellants and the Respondent that the Respondent would fulfill its obligations under the Loan Contract.

(4) BECAUSE the Federal Court was wrong in holding that it was open to parties to contract out of rights and obligations conferred by the Contracts Act 1950.

(5) BECAUSE the Federal Court was wrong in holding that a guarantor could in law and that the Appellants had in fact consented to variation of the Loan Contract so as to deprive the Appellants of their rights under Section 86 of the Act.

(6) BECAUSE the Federal Court was wrong to hold that for the purposes of Section 86 of the Act a variation in the Loan Contract must be material and substantial and that, in the circumstances of this case, the variations had not been material and substantial.

(7) BECAUSE the Federal Court was wrong in not giving consideration to the Appellants' defence under Section 92 of the Act and in deciding that a guarantor could in law consent and that the Appellants in fact had consented to the acts and omissions complained of.

(8) BECAUSE the Federal Court was wrong in failing to consider the Appellants' Defence under Section 94 of the Act and in deciding that a guarantor

could in law consent and that the Appellants had in fact consented to the loss or parting with possession of the securities by the Respondent.

(9) BECAUSE the Appellants have triable defences under Section 95 and 97 of the Act.

(10) BECAUSE the Federal Court was wrong to hold that clause 19 of the guarantee precluded the Appellants from raising any of the above defences to the claim under the guarantee.

10 (11) BECAUSE in all the circumstances, the Appellants did have and do have several triable defences to the Respondent's claim.

(12) BECAUSE the judgment of the Federal Court was wrong and should be reversed and the judgment of Mr. Justice Wan Hamzah was right and the order made by him restored.

RICHARD B. MAWREY

IN THE PRIVY COUNCIL No.42 of 1981

ON APPEAL

FROM THE FEDERAL COURT OF MALAYSIA
APPELLATE JURISDICTION

BETWEEN:

(1) OOI BOON LEONG
(2) PETER KOK SIEW FATT (Defendants)
(3) HIRAOLD KOWADA Appellants

- AND -

CITIBANK N.A. (Plaintiff)
Respondent

CASE FOR THE APPELLANTS

DOUGLAS GOLDBERG & CO.,
1 Holly Hill,
Hampstead,
London NW3 6UB

Solicitors for the Appellants