SHERIFFDOM OF SOUTH STRATHCLYDE DUMFRIES AND GALLOWAY

A358/98

		JUDGMENT OF SHERIFF PRINCIPAL J C McINNES, QC
		in the cause
		THE GOVERNOR AND COMPANY OF THE BANK OF IRELAND
		Pursuers and Respondents
		BRIAN MORTON
		Defender and Appellant

Act: Lindsay, Advocate, Messrs Munro

Alt: Olson, Advocate, Messrs Sinclair McCormick & Giusti Martin

AIRDRIE: 18 April 2000

The Sheriff Principal having resumed consideration of the appeal recalls the interlocutor of the Sheriff dated 8 December 1999; allows the parties before answer a proof of their respective averments; remits the cause to the Sheriff to assign a diet of proof; finds the respondents liable to the appellant in the expenses of the appeal and of the debate as taxed; allows an account of expenses to be given in and remits the same, when lodged, to the Auditor of Court to tax and to report; sanctions the employment of counsel in connection with the appeal.

NOTE:

1. The factual background

1.1 This is an action in which the Bank of Ireland ("the Bank") sue Brian Morton for payment by him to them of the sum of £244,565.48. There is a claim for an additional sum in respect of interest accrued. The former sum is said to be due by Mr Morton, the appellant, in terms of a guarantee executed by him on 5 December 1996 whereby he guaranteed to make payment to the Bank of all sums then due and all sums to become due to the Bank by a company known as Lewis Lloyd Holdings Limited ("LLH"). That company is now in receivership. It is accepted that the guarantee was granted by Mr Morton, who was managing director of LLH. The guarantee was granted by him in connection with the acquisition of a property known as Hazelburn Business Centre, Hazelburn Business Park, Campbeltown. In connection with the proposal to acquire this asset the Bank granted

loan facilities to LLH to the extent of £250,000. In addition to the guarantee by Mr Morton the Bank obtained a standard security over that property. At that time there were in existence two floating charges over the assets of LLH, one in favour of the Royal Bank of Scotland and the other in favour of Bass Brewers Limited. The Bank accepts that it sought and obtained the consent of the holders of these floating charges to the granting of a standard security by LLH in their favour. In their pleadings the Bank aver that, in a letter dated 14 November 1996, they:

> "stipulated for *inter alia* a "First Standard Security" over Hazelburn and a "Third Standard Security" over premises known as Club 2000".

That is admitted by the appellant.

1.2 The Bank did not obtain a first standard security (or as it is called elsewhere in the pleadings a "first ranking standard security"). When LLH went into receivership the floating charges became fixed and both had priority over the standard security which had been granted in favour of the Bank. It was said that the result of that priority is that no sums will be recovered in terms of the standard security. The Bank avers that no security was granted in their favour in respect of the Club 2000 premises.

1.3 The position of the appellant in his pleadings is that:

> "The defender granted the personal guarantee under an essential error as to the ranking of the standard security by LLH to the pursuers. The error was induced by the pursuers' misrepresentation that the pursuers would obtain a first ranking security over Hazelburn. The pursuers did not obtain a first ranking security over Hazelburn. The standard security ranks third behind the floating charge in favour of the Royal Bank of Scotland and Bass Brewers Limited. The defender has been materially prejudiced by the pursuers' failure to obtain a first ranking security. The defender, if he were to pay the sums due under the guarantee, would be entitled to an assignation of the pursuers' security over Hazelburn."

It was decided at a debate at an earlier stage in this case that that aspect of the case will have to go to proof.

1.4 This appeal is concerned with the relevancy of the next part of the case for the appellant, which has been added by amendment subsequent to the earlier debate. That part is predicated on the assumption that the Bank is entitled to enforce the guarantee and that there was no essential error induced by the Bank. On that basis the appellant claims that the Bank failed to obtain a first ranking security over Hazelburn because of a failure on their part to perfect the security. The appellant's case continues:

> "The pursuers were lending money to LLH for the purpose of LLH purchasing a new asset, Hazelburn. The Royal Bank of Scotland and Bass Brewers Limited had no reason to refuse to enter into a ranking agreement to enable the pursuers' security to rank first. The Royal Bank of Scotland's security would not have been prejudiced by such a ranking agreement. Bass Brewers Limited's security would not have been prejudiced by such a ranking agreement. It would have been normal commercial practice for the Royal Bank of Scotland and Bass Brewers Limited to enter into such a ranking agreement. The Royal Bank of Scotland and Bass Brewers Limited would have entered into a ranking agreement to enable the pursuers' security to rank first had the pursuers requested them to do so at or about December 1996. The pursuers failed to do so. The pursuers' failure was caused by their fault or that of their solicitors. As a result of the pursuers' failure the defender has been prejudiced."

1.5 After averments as to the value of the asset at different dates and an averment to the effect that Hazelburn was sold in April 1999 for £150,000 the appellant goes on to aver that:

> "On or about 19th May 1998 the defender wrote to the pursuers offering to pay the sums due under the guarantee by refinancing Hazelburn on his own name. The defender would have been in a position to pay the sums due under the guarantee had the pursuers been able to assign a first ranking standard security to him. The pursuers' security over Hazelburn has no value because it ranks third behind the securities in

favour of the Royal Bank of Scotland and Bass Brewers Limited. The defender has accordingly been prejudiced by the pursuers' failure to effect their security."

2. The terms of the guarantee

2.1 The terms of the guarantee are *inter alia* as follows:

"D. This guarantee shall be in addition 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 liabilities hereby guaranteed.

K. The Bank shall be at liberty without any further consent from the Guarantors and without in any way affecting its right against the Guarantors, at any time to renew, determine, enlarge or vary any credit to the Customer, to renew, vary, exchange, release or abstain from perfecting or enforcing any other securities held or to be held by the Bank for or on account of the monies intended to be hereby secured or any part thereof, to renew bills and promissory notes in any manner and to compound with, give time for payment to, accept compositions from and make any other arrangements with the Customer or any other party in respect of the liabilities hereby secured and the Bank may release or discharge any of the Guarantors from the obligations of this guarantee or make any composition or arrangement with any one or more of them without affecting its rights against the other or others of them.

R. This guarantee shall not be discharged nor shall the Guarantors' liability be affected by reason of any failure or irregularity defect or informality in any security given by or on behalf of the Customer in respect of the monies or liabilities hereby secured nor any legal limitation, disability, incapacity or want of any borrowing powers of or by the Customer or want of authority of any director, manager, official or other person appearing to be acting for the Customer in any matter in respect of the monies or liabilities hereby secured or any other circumstance which rendered the liability of the Customer void or unenforceable and such monies or liabilities will be recoverable by the Bank from the Guarantors as sole, original and independent obligors upon first written demand by way of a full indemnity together with all losses, claims, costs, charges and expenses to which the Bank may be subject or which it may incur in connection with the Customer's liabilities or this guarantee."

The "Customer" in terms of the guarantee is LLH.

3. The Sheriff's decision

3.1 Following a debate the learned Sheriff refused to allow the case to go to proof in relation to the third plea in law for the appellant which is to the effect that the Bank, having failed to perfect their security over Hazelburn as a result of their fault, the appellant is entitled to be released from his obligation under the guarantee to the extent of the value of the security which the Bank had lost. Briefly, he did so because he took the view that clause D of the guarantee indicated that the appellant had accepted that the guarantee was in addition to any other security which the Bank might have obtained. In these circumstances he considered that no duty was owed by the Bank to the appellant to ensure that a particular ranking was obtained for the standard security and that the appellant had not demonstrated that there was an obligation on the Bank to secure a ranking for the standard security prior to the two floating charges. He also considered that the appellant had failed to specify the value which such a first ranking security would have had at the time when the appellant would have been entitled to insist on its assignation to him, i.e. at the date when the guarantee was called up and the appellant would have made payment of the sum due in terms of the guarantee. I will return to that point later in this opinion.

4. Submissions for the appellant

4.1 Mr Olson for the appellant submitted that the learned Sheriff had been wrong to refuse to allow the case to proceed to proof. The appellant offered to prove that the Bank could have obtained a first ranking security, that they had negligently failed to do so and that, as a result of that failure, the Bank had prejudiced the appellant. The effect of that conduct was to release the appellant from his liability in terms of the guarantee to the extent to which he had been prejudiced, i.e. *pro tanto*. He offered to prove that it was in accordance with normal commercial practice, where a new asset was being

acquired, to enter into a ranking agreement with prior floating charge holders. Such an agreement would have resulted in the Bank having a ranking which would have had priority over both the floating charges. The failure to enter into such an agreement had been the result of negligence on the part of the solicitors acting for the Bank. The effect of that failure had been to render the standard security valueless.

4.2 As a matter of law, if the circumstances were that the contract of guarantee contained an express stipulation that the creditor would obtain or retain a security against the debtor, the guarantor is fully released from liability in the event that the security has been given up or has not been perfected or has been caused to depreciate as a result of failure or omission on the part of the creditor. In circumstances in which there is no such stipulation the guarantor is released to the extent to which he has been prejudiced i.e. to the extent that the value of the lost security has diminished. See Stair Memorial Encyclopaedia, Volume 3 p 516. So where a security was lost or the value of the security had depreciated through the failure or omission on the part of the creditor to make it effectual the guarantor is released from liability to the extent to which he has been prejudiced. That was because the guarantor, on paying the whole debt due, is entitled to an assignation of the security so that he may pursue the debtor in terms of the security. It was open to parties to a contract of guarantee to contract out of the common law position just described. One of the issues in this case was whether the Bank had done so. Counsel submitted that the appellant had relevantly averred that he was entitled to relief to the extent to which he had been prejudiced.

4.3 The principle underlying this position was long established: see Erskine Institute III.3.66, Gloag & Irvine: *Law of Rights in Security*, 870, 916, 918 and 921, Gloag and Henderson: *The Law of Scotland*, Tenth Edition 642, Halsbury's, *Laws of England* Vol 20 at pp 193 and 214, Butterworths, *Encyclopaedia of Banking Law* E(2140) at p 695-696. In relation to this matter the laws of both Scotland and England are to the same effect: see *Smith v Bank of Scotland* 1977 SC (HL) 111 *per* Lord Clyde at 118D-E. Counsel drew attention to the cases of *China & South Sea Bank Ltd v Tan* [1990] 1AC 536 *per* Lord Templeman at pp 543-545, and *Bank of Baroda v Patel* [1996] 1Ll LR 391 at p 396. These were recent examples of the operation of equitable relief of guarantors. There were two Scottish cases which were to the same effect: see *Fleming v Thomson* (1826) 2 W & S 277 at pp 292-293 and *Storie v Carnie* (1830) 8 S 853. Reference was also made to *Sligo v Menzies* (1840) 2D 1478 at p 1485. On a proper reading of these cases it was apparent that *Fleming* was a case in which there was an express stipulation which had the effect of discharging the guarantor completely, whereas *Storie* was an example of a case in which the guarantor would be entitled to be released to the extent that he had been prejudiced. In the latter case he was in fact released entirely from the guarantee.

4.4 With reference to the terms of the guarantee counsel for the appellant submitted that there had been no agreement which had the effect of overriding the common law position outlined above. The contract of guarantee was on a printed form which had been drafted by the Bank. It should be construed *contra proferentem* i.e. where there was ambiguity, it should be construed in favour of the appellant. In this case there were allegations of negligence on the part of the Bank or their advisers. The contract of guarantee could not be relied upon by the party putting forward the terms of the contract to exclude or excuse the consequences of that party's own negligence. If negligence were to be excluded, it had to be excluded expressly. See Butterworths, *Encyclopaedia of Banking Law* E (2054) and E(2072) and *Smith v UMB Chrysler (Scotland) Limited* 1978 SC (HL) 1 *per* Lord Fraser of Tullybelton at p 11. *Smith* made it clear that negligence must be expressly mentioned if liability for the consequences of negligence is to be excluded. The terms of the contract of guarantee in the present case did not exclude the consequences of negligence. In these circumstances, if the appellant succeeded in proving that the bank or their advisers had been negligent, the appellant would be entitled to succeed. The learned Sheriff had taken too narrow a view of the meaning of the clauses in question. But for clause K the common law situation would have applied and the guarantor would have been released in the circumstances of this case. The issue was whether that clause afforded the Bank protection from such consequences. Although that clause provided that the Bank could, without consent from the guarantors and without in any way effecting its right against the guarantors, vary,

release or abstain from perfecting or enforcing any securities held by the Bank, it did not say that the Bank could negligently fail to obtain an effective security. What that clause entitled the Bank to do was to take a conscious decision not to perfect a security. It was the equivalent of saying that the Bank could refrain from doing so. The Bank had not successfully exempted itself from the consequences of the negligence of its own servants. The words used were not wide enough to achieve that purpose. If there was any doubt about the matter the terms of the clause must be construed against the Bank. The clause covered other specific grounds than negligence. It therefore could not be construed in such a way as to protect them from the common law consequences of a negligent failure to make a security effective. The result therefore must be that the guarantor was released to the extent to which he was prejudiced.

4.5 Clause R dealt with the situation when things went wrong with a security which had been given by or on behalf of the customer, such as improper execution of the security or lack of authority to grant the security. This clause looked at problems from the point of view of the grantor of the security but did not deal with the mistakes which the creditor might make. It made provision for a situation where the debtor could escape liability for one of the reasons mentioned and provided that, in that situation, the guarantor was still liable. In the present situation there was nothing wrong with the security itself.

4.6 Counsel for the appellant submitted that the appellant had relevantly averred all that he required to aver to make a relevant case. The third plea in law for the defenders was an apt plea in the circumstances. In a matter of this kind the creditor had an obligation to protect the guarantor. In the cases of *Fleming* and *Sligo* there had been a failure to record dispositions in security. These cases were concerned with steps which were necessary to make the security effective. That was not simply a matter of recording it. In a case such as this recording it was not sufficient. The creditor had to obtain a first ranking security. That was a matter for proof, as were the averments to the effect that there would have been no difficulty obtaining a ranking agreement and that the pursuers has been negligent. If these averments were proved it would be clear that the creditor had acted so as to weaken the guarantor's right of relief. The Bank had failed to make the security effectual in the manner which had been anticipated. If it was shown that the Bank had failed to act in accordance with normal commercial practice in these circumstances the appellant would have succeeded in establishing that he had been prejudiced. His averments showed that the subjects had been worth more than the sums due in terms of the guarantee, and that that was so at a time when he wrote offering to pay the sums due by him as guarantor. He would not be entitled to an assignation of the standard security until all sums due in terms of the guarantee had been paid. It was not suggested that there were any other sums due by him in terms of the guarantee. He had averred that in May 1998 he would have repaid all sums due in terms of the guarantee but the Bank would not have been able to offer him an assignation of a first ranked standard security. There was an issue as to the date at which the loss should be assessed. If the date when he offered to repay was the appropriate date then, as at that date, the property was worth £280,000, which exceeded the sum sued for. In these circumstances the loss would have been totally discharged. If there had been a first ranked security and the appropriate date was the date of the sale of the property, the extent of his liability would be reduced by the sale price of the property, namely £150,000. If it was appropriate to have regard to the date when the pursuers failed to obtain a first rank standard security, i.e. December 1996, the property was worth substantially more than the sum guaranteed - in excess of £450,000. Depending upon the view which the court took of the value of Hazelburn at the material time (and that was a matter for proof) the discharge could be to the full extent. In all these circumstances the whole case should be remitted to a proof before answer and the appellant should be found entitled to the expenses of the appeal.

5. Submissions for the respondent

5.1 On behalf of the respondents Mr Lindsay invited the court to refuse the appeal and affirm the interlocutor of the Sheriff. He made two principal submissions. Firstly, the appellant had failed to

aver that the Bank was under a duty to obtain a first ranked standard security. Secondly, the appellant had failed to aver what the value of the standard security had been which the Bank had lost. Both of these were failures in pleading and each of them was fatal to the appellant's position.

5.2 So far as the first of these submissions is concerned the appellant's case was based on a failure to obtain a first ranked standard security. Nowhere did the appellant aver that the Bank was under a duty to obtain such a security. The Bank was under no duty to the appellant to secure the ranking of the standard security which they had obtained. The position of the appellant had been that in cautionary obligations in Scotland, including contracts of guarantee, there was an implied contractual term to that effect. The appellant had no averments as what the implied term was nor had he given notice of why it was necessary to imply such a term. Since this implied term would appear to contradict the express terms of the contract such notice was necessary. Similarly counsel for the appellant had made repeated reference to negligence on the part of the pursuers or their solicitors. If there was a claim in negligence that was a claim, not in contract, but in delict. If it was maintained that there was a duty not to be negligent in this respect and the duty was owed to the appellant, the nature and extent of that duty was nowhere stated. It was not clear whether the appellant was relying on breach of an implied term of contract or on breach of a duty of care based on delict. The Bank was entitled to know what case or cases it had to meet. The appellant required to clarify what the nature and extent of any alleged duty was. It was not clear whether it was maintained that there was an obligation on the Bank to use reasonable endeavours to obtain the agreement specified or that there was an absolute duty to do so. It was not sufficient to leave the matter in the vague form in which it was. There were no averments of duty at all nor as to the standard of care which was owed in the circumstances averred. For these reasons the basis of the claim by the appellant was not relevant.

5.3 It was accepted that common law imposed certain obligations on a creditor who benefited from a guarantee. Amongst those obligations would be an obligation to make a security effectual by perfecting it. That meant that the creditor had to register it without unreasonable relay in the appropriate register. It was also accepted that there was an obligation on a creditor not to squander a security which had been obtained. In this case the position of the appellant was that not only should the security be registered, as it was in this instance, but that a preference should be obtained over two other parties who already had securities in relation to the company involved. To do that required the co-operation of two other parties over whom the Bank had no control whatever. There was no duty at common law on the Bank to do that. On the face of it such co-operation was unlikely to have been forthcoming. Where a company acquires new property it would fall within the scope of a floating charge. The Royal Bank of Scotland might have considered entering into a ranking agreement if, but only if, they were satisfied that they had sufficient cover for any loans which they had made to the company. There was however no obvious reason why they should give up an advantage for no return in these circumstances. If the Royal Bank of Scotland had obtained a personal guarantee of their own in connection with the security provided by the floating charge it is very unlikely that they would have felt able to give up their then ranking. There was no authority in law for the existence of a common law duty being imposed on the Bank requiring them to secure the agreement of third parties to confer a preference on the Bank. The appellant could have made it an express term of the guarantee that the Bank should do so but he had not done that.

5.4 So far as the value of the lost security was concerned it was clear from the third plea in law for the appellant that he sought to be released to the extent of the value of the security. He had not sought to be absolved from liability entirely. Two possible dates had been advanced in the appellant's pleadings as the dates at which the value of the property should be assessed. One of these was the date of the alleged negligence, namely December 1996. The other was 19 May 1998. No valuation of the property was averred for the later date. The nearest valuation was as at 12 March 1998 when it is claimed that the property was worth £280,000. Since it had been valued at £480,000 a year before it was clear that the value of the property was dropping rapidly. The value of the property as at 19 May 1998 was therefore unknown. On that ground also the appellant's case was not relevant. The appeal should be refused.

6. Decision

1. For the purpose of this decision it is necessary to assume that it will be possible for the appellant to prove that the Royal Bank of Scotland and Bass Brewers would have entered into a ranking agreement, if asked by the Bank, in terms of which the standard security secured over the Hazelburn property would have been accorded a ranking prior to the existing floating charges in relation to that property. It must also be assumed that the appellant can prove that this would have been normal commercial practice and that the failure to achieve such a ranking agreement was the fault either of the Bank or of their solicitors. If these facts were to be proved it would probably follow that the conclusion could be drawn that the failure to achieve such a ranking resulted in prejudice to the appellant.

2. The issue which is presented in this appeal is whether the appellant has pleaded a sufficiently relevant and specific case to justify the allowance of a proof before answer. The fact that the Bank failed to obtain a first ranking agreement does not in itself provide a basis for a claim on the part of the appellant for compensation for any prejudice which he may have suffered. He would be entitled to compensation for loss occasioned by that failure if the Bank was under an obligation not to cause him the loss which he claims to have suffered. The Bank could be under such an obligation in consequence of an express or, as in *Storie v Carnie sup. cit.*, an implied term of a contract to that effect. Alternatively the Bank could be under an obligation not to cause loss through its own negligence, or the negligence of others whom it was responsible, i.e. that circumstances were such that the Bank owed a duty of care to the appellant not to cause him such prejudice. In my opinion, if it is necessary to plead a case on one of these bases the appellant's pleadings are open to the criticism that they do not focus the basis of the appellant's case in that way.

3. In order to discover whether the appellant is proceeding by way of an express or an implied term of contract or by way of a case based on negligence or on some other basis it is necessary to have regard to what has been averred. In answer 2 the appellant avers that:

   "The pursuers failed to obtain a first ranking security over Hazelburn because of a failure on their part to perfect their security."

The appellant goes on to aver that the pursuers failed to enter into a ranking agreement, which they could have done. That failure is said to have prejudiced the defender. Although the Bank has incorporated the terms of the guarantee into the pleadings the appellant's response is to refer to the guarantee for its terms but to make no further admission in relation to it. The situation therefore is that the appellant does not appear to rely on the express terms of a contract which would oblige the Bank to obtain a first ranking security. Nor does the appellant aver that it was an implied term of the contract of guarantee or of some other related contract between himself and the Bank, that the Bank would obtain such a security of which he would obtain the benefit in the event that he had to meet, and did meet, his liability in terms of the guarantee. So far as negligence is concerned, although the appellant avers that there was a failure on the part of the Bank or their solicitors to enter into a ranking agreement with the Royal Bank of Scotland and Bass Brewers Limited, there is no specification as to the basis upon which the Bank owed the appellant a duty to take reasonable care in this regard. If the matter is to be tested simply by reference to the appellant's pleadings on one or other of these bases the pleadings, it must be said, are very sparse. But, it seems to me, that that approach is arguably flawed. In my opinion the proper approach is to look at what has been averred by the appellant having regard to the law relating to cautionary obligations (of which a contract of guarantee is an example) and determine whether sufficient notice has been given of a case which

could result in him succeeding in obtaining judgement in his favour. If so, it is necessary to consider whether the terms of the contract of guarantee, properly construed, must have the effect that he would not succeed at proof. If that would be the consequence of such a construction a proof would be pointless.

6.4 Leaving aside for the moment the terms of the contract of guarantee, the question is whether, assuming that the appellant can prove that, as a result of the acts or omission of the Bank or the Bank's solicitors he suffered prejudice, he is entitled to be released from his liability in terms of the guarantee to the extent that he was prejudiced. The common law position was stated thus:

> "From the right of the cautioner to total relief against the principal debtor, and to the benefit of all securities for the debt in the hand of the creditor, there arises a corresponding duty on the part of the creditor to have regard to the interests of the cautioner. To this extent the creditor is in the position of a trustee for the cautioner, and, as such, he must preserve intact all the remedies against the principal debtor, whether in his own name or in name of the cautioner; must not, by any voluntary act, do away with, release, lose, or depreciate any securities for the principal debt; and must abstain from any dealing with the principal debtor, or with third parties, which would prejudicially affect the position of the cautioner, as by extending the time of payment of the debt, varying the mode of accounting, or the like. "If" in the words of Erskine, "The creditor shall do any act, which shall have a tendency to weaken the cautioner's right of relief, the cautionary obligation ceaseth." "

See Gloag and Irvine: *Law of Rights in Security* at pages 809-810. Put thus it is clear that the duty imposed on the creditor arises not so much from a term of the contract of guarantee, whether express or implied, but by operation of law. Gloag and Irvine treat the matter as akin to breach of trust. In *Bonar v Macdonald* (1847) 9D 1537 at pp 1548-9 Lord President Boyle referred to:

> "the great cardinal principle applicable to all cautionary obligations - that the liability of the surety - the risk he incurs - cannot be increased either directly or indirectly by the conduct of the obligees who hold a bond of caution - without a full communication to the cautioner; and, in the event of no such communication having been made, the cautioner shall be entitled to freedom from his bond. That is the fixed principle of law illustrated by many decisions. If anything is done to increase the risk, that is not an act of omission, but of commission. It is not a mere oversight."

On that basis if the creditor fails to have regard to the interests of the cautioner, with the result that the cautioner is prejudicially affected, the cautioner would not necessarily have to prove negligence to secure the diminution of his liability.

> "A cautioner may be liberated not only by a voluntary act of the creditor, but also where, through mere neglect or omission on the part of the creditor, securities, to the benefit of which the cautioner is entitled, are lost or rendered ineffectual through not being properly perfected." (Gloag and Irvine at p 918).

Where there has been release of a security in contravention of an express stipulation that the creditor would obtain and retain such a security, the basis upon which the cautioner would be discharged, and discharged wholly, would be that the creditor was in breach of contract. The basis upon which, in other cases, a cautioner would be discharged either wholly or *pro tanto* could be by reason of breach of an implied term or by reason of a breach of trust. At this stage I am not convinced that it is essential for the cautioner to peril his case on one or other of these bases. It may not be possible to categorise the basis until he facts are established by evidence. The question is whether, in circumstances in which the defender has not clearly stated the category into which this case falls, his case is irrelevant.

6.5 Though it may not be necessary in a particular case to prove fault, fault is not wholly irrelevant. There must be some voluntary act or omission on the part of the creditor (to which the cautioner did not consent) which led to the loss of or decline in the value of the security. A decline in the market value of the security does not affect the position of a cautioner. In some cases there has been a tendency to consider the conduct of the creditor more by reference to the law of negligence; in others more in terms of breach of contract (see *Lord Advocate v Maritime Fruit Carriers Ltd* 1983 SLT 357 at p 360, *China & South Sea Bank, sup. cit.*). It is a question of fact whether there has been prejudice

to a cautioner as a result of the voluntary act or omission of the creditor. If it is proved that there has been prejudice caused by such voluntary act or omission the cautioner is entitled to a remedy. In such circumstances it is not easy to see why the cautioner should be deprived of the opportunity to prove that he is entitled to that remedy simply because he has not attached a particular label to the creditor's act or omission; whether the act or omission is deliberate or negligent, a breach of an implied term of contract or a breach of trust makes no difference to the parties' respective rights and liabilities in practice.

6.7 In the end of the day the question is whether the appellant has given sufficient notice of a case that he is entitled to a *pro tanto* reduction in his liability by reason of prejudice arising from the failure of the Bank or its solicitors for the reasons averred on record. His third and fourth pleas in law are in the following terms:

> "3. *Esto* the Pursuers are entitled to enforce the contract of guarantee and the Defender's consent to the guarantee was not vitiated by essential error induced by the Pursuers (which is denied), the Pursuers having failed to perfect their security over Hazelburn as a result of their fault the Defender is entitled to be released from his obligations under the guarantee to the extent of the value of the security which the Pursuers have lost.
>
> 4. The sum sued for not being due and resting owing to the Pursuers, Decree of Absolvitor should be pronounced with expenses."

6.8 In my opinion the Bank has been given sufficient notice of the case which is made against them by the appellant to justify the allowance of a proof before answer.

6.9 If there is to be a proof before answer it is a matter for the court at the conclusion of the proof to decide what has been proved in relation to the value of Hazelburn. Since matters of relevancy and specification may be raised at that stage it would be inappropriate to express a concluded view. It is for the court, following proof, to consider at which date the value of Hazelburn should be assessed. The appellant offers to prove that Hazelburn was valued at £280,000 as at 12 March 1998, i.e. about two months prior to the date on which he claimed to have been in a position to pay the sums due in terms of the guarantee. He avers that the property was sold for £150,000 in April 1999. If May 1998 is held to be the appropriate date, in my opinion, it cannot be said that there is insufficient notice of the appropriate value of the property then.

6.10 So far as the question whether the terms of the guarantee were such as to exclude the Bank's liability for failure to perfect the security is concerned in my opinion the contract of guarantee should be construed having regard to the evidence led at a proof. The guarantee was part of a package of arrangements made to secure the loan by the Bank to LLH. In the construction of commercial contracts courts now tend to pay somewhat less attention to linguistic considerations and more to the factual background which led to the contract being entered into than once they did. Where there is ambiguity in relation to a contract such as this the contract will be constructed *contra proferenteum*.

6.11 At proof it is likely to be argued by the appellant that it was a material part of the agreement between the Bank and the appellant that the Bank would obtain a first ranking standard security over Hazelburn. It may be argued by the Bank that, on a proper construction of the contract, in the light of the events which occurred, clauses K and R have the effect of preserving the appellant's liability to the Bank. That would be disputed by the appellant, who is likely to contend that the Bank or its solicitors were negligent and that these clauses do not have that effect in those circumstances. These are matters which can best be resolved once the facts have been established. I have allowed a proof before answer. See *Smith v U.M.B. Chrysler (Scotland) Ltd sup. cit.* at pp 11-12.

6.12 It was agreed that expenses should follow success and that the appeal was a matter which justified the employment of counsel.