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THE TIME BARRING OF CLAIMS UNDER COLLATERAL WARRANTIES IN SCOTLAND AND A COMPARISON WITH THE POSITION UNDER ENGLISH LAW

- Two recent cases have highlighted the differences between the English of limitation and the Scots law of prescription.
- What prescriptive period applies to a claim under a collateral warranty under Scots law?
- What impact does a "no greater liability" clause in the collateral warranty have on that period?

What's it about?

The Scottish case of *British Overseas Bank Nominees & Henderson v Stewart Milne Group Limited (2018)* considered whether a collateral warranty, granted by the contractor in favour of a beneficiary, created a fresh period of prescription in relation to a known defect, unfettered by the fact the defect was already apparent prior to the date the warranty was granted and whether that period was shortened by the presence of a "no greater liability" clause in the collateral warranty.

Stewart Milne designed and constructed a car-park in Inverurie under an SBCC Design & Build (2007 revision) contract. Practical completion was reached in 2009. Henderson purchased the site in June 2013 and Stewart Milne granted Henderson a new collateral warranty in August 2013. Henderson brought proceedings against Stewart Milne in June 2018, for the cost of rectifying defects in the works based on a breach of the collateral warranty (resulting from breach of the building contract). The claim was raised before the new five-year prescriptive period under the collateral warranty, which commenced on the issue of the warranty in August 2013, had expired.

In response, Stewart Milne argued several points. If there had been a breach of the building contract (which was denied), the prescriptive period under Scots law in respect of the defect was five years, but this commenced on the date of practical completion (in 2009). Accordingly, by June 2018, the prescriptive period had expired, and thus Henderson's claim had prescribed. The warranty contained "equivalent rights of defence" and "no greater liability" wording in relatively standard terms which will be familiar to many in the industry. If Stewart Milne had "no greater liability" to Henderson than they had to the original 'Employer' under the building contract, Henderson's claim must fail. Equally, if Stewart Milne could plead "equivalent rights of defence" in response to Henderson's claim, Stewart Milne's defence of prescription against the claim as if it had been brought by the original 'Employer' (the prescriptive period beginning in 2009) must win the day.

The court held with the pursuer, and allowed Henderson's claim to proceed. The key point was that the Scottish law of prescription created a new five-year prescriptive period between the parties, commencing on the date the collateral warranty was granted. The parties were not bound by the prescriptive period between the employer and contractor, but by the new prescriptive period between beneficiary and contractor. The wording of the "no greater liability" and "equivalent rights of defence" provisions referred back to the building contract and was not sufficient to cut short the new prescriptive period. Accordingly, the "clock" had started running in August 2013, and not at the date of practical completion (as Stewart Milne had argued).

So what?

The finding of the court that the "equivalent rights of defence" and "no greater liability" provisions contained in the warranty were not sufficient to cut short the new five-year prescriptive period which was created when the new collateral warranty was granted is an important decision relating to collateral warranties in Scotland and is likely to have an impact on the drafting of collateral warranties and the negotiating stance of both warrantors and beneficiaries.

Now what?

Contractors and consultants under Scots law construction contracts may be much more wary of granting fresh collateral warranties any length of time following practical completion, either at all, or without a provision expressly and clearly limiting the prescriptive period under the collateral warranty by reference to the building contract. Providing rights to a new beneficiary by means of an assignation of contractual rights as opposed to a fresh warranty may become the preferred starting position of contractors and consultants.

Purchasers or funders of construction projects in Scotland may, in turn, become more insistent that fresh collateral warranties are granted. Use of cash retentions to "incentivise" delivery of collateral warranties may become a possibility where a "first purchaser", "first funder" or "first tenant warranty has not been called for by the date of PC.

Parties (and their lawyers) operating in the two jurisdictions should be mindful of the differences between the laws of limitation and prescription and the effect of "no greater liability" clauses in each – see below for more detail as to the contrast between the two legal systems.

A contrast with English Law

The position under Henderson v Stewart Milne (Stewart Milne) can be contrasted with the position which applies under English law (which does not have the concept of a 5 year prescriptive period) as illustrated by the case of *Swansea Stadium Management Co Ltd v City* and *County of Swansea (1) and Interserve Construction Ltd (2) (Swansea)*. In Swansea, the recipient of a warranty granted by the contractor after practical completion of the works sought to bring a claim under the warranty for defects in the works. As explained in more detail in our article on this case – click here – the court held that, based on the words used in the warranty and the factual matrix, the warranty was intended to have a retrospective effect. Accordingly the limitation period for claims under the warranty commenced on practical completion of the Works under the building contract (at the same time as the limitation period under the building contract) and ended 12 years thereafter (as the warranty was executed as a deed).

The collateral warranty in the Swansea case contained a proviso that the contractor should have no greater liability under it than if the beneficiary under the warranty had been named as joint employer. In the context of this case the court read this as a clear indication that the parties had intended the beneficiary to "…stand in the shoes of the employer" and be in the same position as the employer vis a vis the contractor, supporting the conclusion that the warranty was intended to have retrospective effect.

Accordingly, the beneficiary's claim was refused, as it was made after the end of the applicable limitation period.

So, whilst in England the "no greater liability provision" supported the retrospective effect of the warranty (which led to the claim being time barred) in Scotland the 'equivalent rights' cannot include the question of prescription. The collateral warranty, when granted, creates a fresh contractual relationship between the counterparties, with a fresh five-year prescriptive period. Equivalent defences, such as caps on liability, may be raised in respect of that new relationship, but the primacy of the new contractual relationship (and the five year prescriptive period that it creates) makes any notion of retrospectivity otiose under Scots law.

The court in Stewart Milne was clear – any reference to English cases was unhelpful in evaluating the application of the Scots law of prescription. While the same wording might be present in warranties granted in both jurisdictions, the underlying law was different, and different considerations applied.

The result in practical terms: in Swansea, the limitation period was the same as that under the building contract and as such the claimant's case was time barred. In Stewart Milne, the claimant succeeded as a new prescriptive period applied to the claim under the collateral warranty, even though more than five years had passed since the defect first became apparent and the claim could accordingly not have been brought under the building contract.

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