Construction Law Focus
CHAN TAN & PARTNERS ISSUE 1 OF 1997 NO.1 COLOMBO COURT #09-26/27 SINGAPORE 179742

Performance bond - injunction to restrain payment pursuant to call made on the bond

There have been a series of decisions recently in the Singapore courts relating to injunctions taken out to restrain calls made on bonds. The latest is the case of *San International Pte Ltd v Keppel Engineering Pte Ltd* (Suit no. 411 of 1996). where the Singapore Court of Appeal in June 1996 dismissed an appeal by Plaintiffs, San International Pte Ltd against the decision of the High Court in refusing to grant an interim injunction applied ex-parte by them to restrain the Defendants, Keppel Engineering Pte Ltd, from claiming or receiving any part of a sum of $1,255,520.56 being balance of a guaranteed sum under a performance bond. No written judgment was given by the appellate court but some guidance on this subject can be obtained from the unpublished Grounds of Judgment of the Learned Judicial Commissioner, Mr C. R. Rajah, who heard the matter at the court of first instance.

The facts of this case were fairly typical of construction cases. The Defendants were the Main Contractor in a construction project and the Plaintiffs were one of their Sub-Contractors. Under the terms of the sub-contract, the Defendants had to provide the Plaintiffs with a performance bond ("the Bond") of $1,342,926.54 amounting to 10% of the contract sum. This the Plaintiffs did through a insurance company ("the Guarantor").

The Bond in clause 1 stated that it was supplemental to the contract and clause 2 of the Bond provided that

> "In the event of the Sub-Contractor failing to fulfil any of the terms and Conditions of the Contract, the Guarantor shall indemnify the Main Contractor against all losses, damages, costs expenses or otherwise sustained by the Main Contractor thereby up to .. ($1,342,926.54)(hereinafter called "the Guaranteed Sum"). The Guaranteed Sum shall be paid to the Main Contractor in full immediately upon demand for payment in writing and notwithstanding the existence of any dispute between the Main Contractor and the Sub-Contractor in relation to the Contract or any amount payable thereunder."

The Plaintiffs relied on the fact that there was language in the Bond that it was "supplemental" to the sub-contract and that the Guarantor's duty to indemnify only arose upon the Plaintiffs failing to fulfil any terms of the sub-contract. The case of *Trafalgar House Construction (Regions) Ltd v General Surety and Guarantee Co Ltd* 73 BLR and *Tins Industrial Co Ltd v Kono Insurance Ltd* 42 BLR 110 were cited in support.

There were disputes between the parties and the Defendants terminated the sub-contract by a letter dated 29 November 1995. The Plaintiffs claimed that the termination was wrongful and amounted to a repudiatory breach by the Defendants which the Plaintiffs accepted by a letter dated 1 December 1995. On 1 December 1995, the Defendants commenced an action against the Plaintiffs and on the same day obtained an ex-parte injunction ordering the Plaintiffs to vacate the site and restraining the Plaintiffs from, inter alia, removing plant, equipment and materials from and interfering with the Defendants' personnel at the site. This interim injunction was discharged upon the Plaintiffs' giving certain undertakings.

On the same day after the aforesaid injunction was discharged, the Defendants by a letter dated 1 March 1996 demanded from the Guarantor payment under the Bond of the sum of $1,255,20.56. The Defendants had earlier obtained default judgment against the Guarantor under the Bond for $87,405.98. The Plaintiffs thereafter commenced the present case on 5 December 1996 and applied exparte for an interim injunction to restrain the Defendants from claiming or receiving any part of the sum under the Bond.

The grounds for the Plaintiffs' application were as follows:

1. The bond was not an "on-demand" bond but a guarantee ie the Court must be satisifed that there was default on the part of the Plaintiffs before a call can be made; and
2. That the Defendants' conduct in calling on the bond was unconscionable.

The learned Judicial Commissioner ruled that the Bond was an on-demand bond. He said that the bond in the 2 cited cases were worded differently and have no clause even similar to the clause 2 in the instant case. The Judicial Commissioner placed weight on the fact that clause 1 had stated that the Bond was provided in

consideration of the Defendants not insisting that the Plaintiffs pay them the Guaranteed Sum as a security deposit. This read with clause 2 would indicate that the Bond was meant to operate akin to a cash deposit.

As regards the submission of unconscionability, the Plaintiffs submit that the total damages claimed as of 29 November 1995 was only $87,405.98 which had escalated to a figure greater than $1,255,520.56 by March 1996 which was not possible over such a short time. The Plaintiffs also submitted that the Defendants held some $3,114,000 belonging to the Plaintiffs comprising of certified and uncertified sums of work done as well as retention money which the Defendants must set-off before they can demand payment under the Bond.

In rejecting this submission, the Judicial Commissioner accepted the principle laid down by the Court of Appeal in *Bocotra Construction Pte Ltd & Ors v Attorney General (2)* [1995] 2 SLR 733 that fraud or unconscionability was the sole consideration in applications for injunctions restraining payment or calls on bonds or guarantees. The party seeking the injunction are required to establish clear case of fraud or unconscionability. Mere allegations were insufficient. The Defendants' letter of demand of 1 March 1996 showed on its face that their claim was for more than $1,255,520.56. While the Plaintiffs were entitled to require the Defendants to set-off first from the certified sum, the other sums were merely claims and not confirmed as due and payable. There was also nothing to show that the Defendants did not credit the Plaintiffs with the set-off and still have a claim for more than $1,255,520.56 outstanding. No clear grounds were given as to why the Defendants' claim for damages on 1 March 1996 could not come up to the aggregate amount. After stating his view that "It could not therefore be said that the Defendants had no honest belief that they were entitled to payment of the $1,255,520.6 under the Bond", the application was dismissed.

EDITORIAL COMMENT

In recent years, it is common in Singapore for employers to require what is known as "demand" performance bonds from contractors. This means that the surety (usually a bank or an insurance company) must, in the absence of fraud, make payment on demand by the employer. It is, of course, quite rare for the contractor to be able to demonstrate a clear case of fraud. Hence the more common arguments advanced to challenge calls are as follows:

(a) The call was improperly made as it was not made according to the requirements of the terms and conditions of the bond;

(b) There was no breach or default by the contractor of the terms and conditions of the underlying construction contract; and

(c) The employer was not entitled to call on the bond since he was himself in breach of the terms and conditions of the underlying construction contract.

Previously, these kind of arguments used to carry very little weight in Singapore (see the decision of Chan Sek Keong J in *The Brightside Mechanical and Electrical Services Group Ltd & Anor v Standard Chartered Bank & Anor* [1989] 3 MLJ 13) . However, in Singapore there was a trend of judicial decisions in recent years starting from the case of *Royal Design Studio Pte Ltd* v *Chang Development Pte Ltd* [1991] 2 MLJ 229. which appears to suggest that the contractor may not have to demonstrate fraud in order to get an injunction to stop the calling of the bond.

The Singapore Court of Appeal eventually had an opportunity in *Bocotra Construction Pte Ltd & Ors v the Attorney-General, Singapore (2)* [1995] 2 SLR 733 to review the law relating to demand bond The Court of Appeal held, inter-alia that the mere fact that the validity of the guarantee was substantially challenged in other proceedings does not automatically provide a basis for an injunction to be obtained restraining an intended call for payment. It will still be in the 'wholly exceptional case' of fraud that an injunction can be granted. The present decision being one decided after *Bocotra* is instructive for the light it throws on the viability of an injunction to restrain the surety from making payment pursuant to a call.

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