

RECENT DEVELOPMENTS IN CONSTRUCTION LAW IN SINGAPORE

by

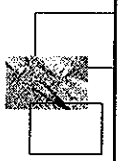
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REVIEW OF CONSTRUCTION RELATED CASES IN RECENT YEARS



- Cases
- *Fu Hai Construction Pte Ltd v Econ Corporation Ltd (Suit No. 1070 of 2001, unreported judgement dated 31.08.2002)*
- *Hiap Tian Soon Construction Pte Ltd and another v Hola Development Pte Ltd and another [2003] 1 SLR 667*
- *Steel Industries Pte Ltd v Deen Engineering Pte Ltd [2003] 3 SLR 377*
- *Hitachi Plant Engineering & Construction Co Ltd & Anor v Eltraco International Pte Ltd , Yi Wee Pools & Fountains Pte Ltd & Anor v Eltraco International Pte Ltd [2003] SGCA 38*

Fu Hai Construction Pte Ltd v Econ Corporation Ltd
(Suit No. 1070 of 2001, unreported judgement dated 31.08.2002)

- *"Tacit acceptance in another's self-deception does not itself amount to a misrepresentation, provided that it has not previously been caused by a positive misrepresentation. But there are exceptions to the general rule that there is no duty to disclose, namely where the contract is within the class of contracts uberrimae fidei, where there is fiduciary relationship between the parties, and where failure to disclose some fact distorts a positive representation."*

- Lai Siu Chiu J.

Con'td

- Whilst a construction contract is not within the class of contracts of the utmost good faith but where, as in this instance, the plaintiffs had actually inquired from the defendants whether there were any adverse factors the plaintiffs should know about and was assured there were none, the defendants' non-disclosure of the soil condition amounted to a misrepresentation.

- The Court found that there was misrepresentation in awarding the sub-contract to the Fu Hai where Econ will be taking away the major works and sub-contracting them to various other sub sub-contractors, without allowing Fu Hai to charge any attendance fee to co-ordinate the works of their appointees.

Hiap Tian Soon Construction Pte Ltd and another v Hola Development Pte Ltd and another [2003] 1 SLR 667

- The only cross-claims that may be deducted therefrom are those that are out of the same transaction or are so closely connected with the plaintiffs' demands that it would be manifestly unjust to allow the claim without taking into account the cross-claim

- Lai Siu Chiu, J in deciding that Hola's right of set-off remained intact held that *"in relation to a building contract one starts with the presumption that each party is to be entitled to all those remedies for breach as would arise by operation of law, including the right of set-off. However, it is open to parties to rebut that presumption by contrary provisions in the contract, provided that clear and unequivocal words are used."*

Con'td

- Further, the honourable judge held that it was not necessary for Hola to inform the Hiap Tian Soon that it intended to exercise the right of set-off, stating that *"a party purporting to exercise the right of set-off must quantify his loss by means of a reasonable assessment made in good faith".*

Steel Industries Pte Ltd v Deen Engineering Pte Ltd [2003] 3 SLR 377

- Architect could withdraw a Certificate if it was issued in error, and not due to his non-approval of the use of the Certificate by the beneficiary. In other words, where the Certificate was validly issued, the beneficiary was entitled to use it as the basis of his claim.

- Where strict compliance with the contract conditions have been waived, that waiver could not be taken as agreeing to pay under an interim certificate issued years after the prescribed time, in which case, the certificate of payment can be rendered invalid.

Con'td

- Clause 30(2) of the SIA Conditions of Contract and the circumstances in which it may be held to be invalid:

- Architect prior to issuing the Certificate of Payment must have applied his mind to ascertaining whether the reason for non-payment of the Interim Certificate fell within Clause 30(2)(a).

- The case confirmed that where the Architect failed to properly consider whether the sole reason for the Employer's deduction of monies due to the nominated sub-contractor was not due to the Main Contractor's default, then the Certificate was wrongly issue.

Con'td

- In order for an interim certificate to qualify as a revision certificate under Clause 31(4) it had to:

(a) identify the previous certificate which it sought to correct;

- state the reasons for the correction; and
- set out the details of what was being corrected.
- Court held that where there was a "pay when paid" contract where the risk of the employer's insolvency is shared; and where insolvency becomes the cause or on of the causes for non-payment by the employers, it would not be right to force the main contractor to pay the sub-contractor out of their own pockets.

Con'td

- Further, the Court had to consider the fact that there was an ongoing arbitration between the employers and the defendants wherein the plaintiffs' works formed part of the claim. The Court held in that case that where arbitration proceedings have been initiated, the Architect had no power to issue a certificate of payment.

Hitachi Plant Engineering & Construction Co Ltd & Anor v Eltraco International Pte Ltd , Yi Wee Pools & Fountains Pte Ltd & Anor v Eltraco International Pte Ltd [2003] SGCA 38

- The Court of Appeal confirmed that under Clause 31(10)(b) of the SIA Conditions of Contract as it is drafted, the nominated sub-contractors' entitlement to receive direct payment was merely contingent upon the Architects' exercise of their discretion to certify direct payment to the nominated sub-contractors.

- The Court of Appeal was of the view that the nominated sub-contractors had a right to direct payments if the Main Contract had stated that it is mandatory for the Architects to Certify direct payment upon a particular event.

Con'td

- where the Main Contractor falls into a scheme of arrangement, the nominated sub-contractor may bring to the attention of the Court sanctioning the scheme of arrangement, if there was a contingent entitlement to direct payments, the principles enunciated in *UDL Argos Engineering & Heaving Industries Co Ltd v Li Oi Lin [2001] HKCFA 53*, in deciding if it should direct a separate meeting for the nominated sub-contractors.

- The Court of Appeal held that the nominated sub-contractors' argument that their right to direct payments can only be affected by an express term in the scheme fails because they did not have a right to those payments when the scheme of arrangement was approved and sanctioned. The Court of Appeal further found that the direct payments would fall under the scheme of arrangement because they form part of the 'accounts receivable' by the Main Contractor, Eltraco.

Review of Construction Cases

- Contract Formation
- Contracting Parties
- Clauses stating that time is of the essence
- Termination due to delays in work
- Common or Unilateral Mistake
- Performance Bonds

CONTRACT FORMATION



SHIA KIAN ENG v NAKANO (2000)

- Development known as Woodsvale Executive Condominium.
- The Defendant engaged the Plaintiff as a sub-contractor for the block wall, plastering, steel lintel, floor screed and tiling works.
- The Plaintiff brought the case to claim $2.04 million while the Defendant counterclaimed for $2.7 million.
- Among the issues before the Court was the documents which evidenced the contract between the parties.

Con'td

- The works were placed by Purchase Orders ("PO") issued by the Defendant.
- The PO took a standard format and they refer to a number of other documents including "Conditions of Sub-Contract", "Bills of Quantity/Schedule of Rates" and "Drawings".
- However, the PO were issued only after the Plaintiff started work and given to him when he asked how payment was to be made.
- The court held that the sub-contracts were partly in writing and partly oral and the written portions of the sub-contracts comprised the quotations and the PO.



Con'td

- The Court found that:
- It was unclear that there was active negotiation by the parties on the form of terms and conditions, etc.
- No evidence that copies of the standard PO and conditions of sub-contract were given to the Plaintiff.
- The Defendant was familiar of having letters of intent but yet no such letter was issued.
- Not all documents were indeed annexed to the Plaintiff as mentioned in the PO.

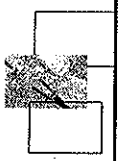
Con'td

- In short, *"it is difficult to incorporate them as part of the contract unless there is clear indication by that other party that he would accept documents subsequently"*.



CONTRACTING PARTIES

- A contractor may sometimes change its name when it undergoes incorporation.
- **This is discussed in the case of Lai Yew Seng Pte Ltd v Pilecon Engineering Bhd (2002)**



LAI YEW SENG PTE LTD v PILECON ENGINEERING BHD (2002)

- The Defendant was the main contactor to 3 school building projects for the government. The Plaintiff was its sub-contractor.
- There was an issue whether Lai Yew Seng Iron Works (the former company's name before it was incorporated under its present name) was the same as the Plaintiff and was entitled to sue the Defendant for work done under the sub-contract.
- The Defendant argued that the contracts were made between Lai Yew Seng Iron Works and not with the Plaintiff.

Con'td

- The High Court on appeal, held that the Defendants had all along accepted the Plaintiffs as its contractual partner and there was no dispute on the works done by them
- The Court was of the view that the parties were in a contractual relationship distinct from the original contract. Further, the Defendant had benefited from the Plaintiff's work and had paid them the initial progress payments.



MAKING TIME THE ESSENCE

NATIONAL SKIN CENTRE v EUTECH CYBERNETICS (2002)

- Sometime in 1998, the Plaintiff awarded the Defendant a contract to replace an existing computer system to Y2K compliant.
- The system was to be installed and commissioned by 31 August 1999.
- The Defendant failed to meet this target date and several EOT were given.



Con'td

- On 11 February 2000, the Plaintiff wrote to the Defendant that the project was in delay for more than 5 months and they expect delivery of the system within 3 months (i.e. by 11 May 2000).
- The defendant responded with 2 proposals suggesting it would not be able to meet the revised dates.
- As such, on 21 March 2000, the Plaintiff wrote to terminate the contract.
- The High Court ruled that when the Plaintiff elected not to terminate the contract when the Defendant failed to commission the system on 31 August 1999, but chose to continue with it, time was set at large and no longer of the essence.

Con'td

- However, the Plaintiff was entitled thereafter to make time of the essence again by giving reasonable notice to the Defendant which the Plaintiff did vide the letter 11 February 2000.



TERMINATION DUE TO DELAYS

TERMINATION DUE TO DELAYS

- When there is a delay, the employer is entitled to:
  - LD
  - replacing the main contractor
- When the contract is unclear, the employer may replace the contractor, the general law of repudiatory breach must be relied upon.



SHIA KIAN ENG v NAKANO (2000)

- One of the issues that the Court had to consider was whether the slow progress of the sub-contract works was sufficient to justify the termination of the sub-contract.
- The Court re-affirmed the principle that not every breach of contract justifies termination unless it can show that the contractor is either unable to proceed or had no intention of proceeding with them.

Con'td

- The learned Judith Prakash J highlighted 3 points:
- When the termination notice was served, the main contractors were not yet late.
- The Plaintiff's work were given a lower priority.
- The Defendant was haphazard in communicating its construction programme to its sub-contractors.



Con'td

- Thus, the Court held that whilst the Plaintiff did not work as fast as the Defendant desired, there were various reasons for the slow progress.
- Accordingly, the Court held that there was no justification for the termination of the Plaintiff's sub-contract.

COMMON OR UNILATERAL MISTAKE

HO SENG LEE v NIAN CHUAN (2001)

- Issue was whether the contracts should be rectified or rescinded on the ground of common or unilateral mistake.
- Dispute was about the number of metal-forms on site under a rental agreement.
- The Defendant entered into 3 agreements with the Plaintiff for which they rented metal-forms from the Plaintiff.

Con'td

- The Defendant disputed the quantity and asserted that the agreement were not binding or enforceable against them due to common mistake of the parties at the time the agreements were entered.
- The Court held that though the quantity was not the number stated in the rental agreements, the Defendant was unable to escape from its contractual liability to pay hire.



Con'td

- The learned Judith Prakash J. relied on the case of ***Associated Japanese Bank v Credit du Nord SA (1989)*** and highlighted 5 points:
- The law ought to uphold rather than to destroy apparent contracts.
- The common law rules as to a mistake regarding the quality of the subject matter.
- Such a mistake must substantially be shared by both parties, and must relate to facts as they existed at the time of the contract.

Con'td

- The mistake must render the subject matter of the contract essentially and radically different from the subject matter.
- The Court must ascertain whether there were reasonable grounds
- The Court ruled that the Defendant had not satisfied the essential element of unilateral mistake. As such, they were bound by the contracts signed.



PERFORMANCE BONDS

PERFORMANCE BONDS

- It is now settled law in Singapore that, apart from fraud, calls on performance bonds can be restrained on the ground that the call was unconscionable.
- The English Court of Appeal in ***Edward Owen v Barclays Bank (1978)*** laid down the position that the Courts will not restrain a call on payment unless fraud is involved.



- In Singapore, our Courts departed from the position in England. In ***Royal Design Studio v Chang Development (1991)***, it was suggested that "*if there is a failure of consideration*", the seller should be able to prevent a call upon the bond.
- The doctrine of unconscionability was first brought up in ***Bocotra Construction v Attorney General (1995)***.

SAMWOH ASPHALT v SUM CHEONG PILING (2002)

- The Defendant were the main contractors of a Mindef project and the Plaintiff was the sub-contractors for the paving works who had furnished the Defendant with a demand bond.
- The previous sub-contractors repudiated and dropped out of the contract and the Plaintiff then negotiated directly with the Defendant for a new contract.
- When the negotiations broke down, the Defendant called on the bond.



Con'td

- The Court of Appeal held that this was an abusive call on the bond. The learned LP Thean JA (as he was then) said:

  "*the call… was not based on any bona fide claim against Samwoh. The clear inference is that they invoked the performance guarantee as a bargaining chip to compel Samwoh to agree to their terms. It was an abusive call on the performance guarantee.*"

CHEW PIN PIN v AGF INSURANCE (2001)

- The Plaintiff employed TDS Construction to construct and build 3 houses at Robin Road who had procured a performance bond from the Defendant in the Plaintiff's favour.
- TDS went into liquidation and the Plaintiff subsequently called on the bond.
- The Defendant refused to pay, arguing that monies were due to TDS and hence the call was unconscionable, until the Plaintiff proved his entitlement to damages from TDS.



Con'td

- The learned Choo JC dismissed the appeal and held that the Defendant had no defence as the terms of the bond provided for payment upon demand without question.
- He stated in his judgement that the reference to the underlying contract was made between the Plaintiff and the Defendant where in consideration of the Plaintiff not seeking a security deposit from TDS, the Defendant warranted that it would pay the Plaintiff the bond amount upon demand without question.

A. *INTERIM CERTIFICATES & DELAY CERTIFICATES (with consideration of recent case law)*

- *LIABILITY OF EMPLOYER FOR ARCHITECT'S DEFAULT IN CERTIFICATION FUNCTIONS*
- *WARRANTIES/INDEMNITIES & PERFORMANCE BONDS*
- *LIABILITY FOR DEFECTS IN THE LIGHT OF SETRON V CHUANG U MING*



INTERIM CERTIFICATES & DELAY CERTIFICATES

A. *INTERIM CERTIFICATES & DELAY CERTIFICATES (with consideration of recent case law)*

- **High Court – China Construction v Leisure Park (2000)**
- Dispute – An interim certificate was challenged by the employer contending that it did not conform to the contract requirements by showing the valuation date and was issued long after the valuation date and regarded that even if it was a corrective certificate, it was not issued properly.

Con'td

- Warren Khoo J held that an interim certificate of the architect ought to be honoured and accorded temporary finality pending review unless it can show that the certificate had not been issued in the proper exercise of the architect's powers under the contract.
- The Court found that it will not insist in strict adherence which would enable the employer to take advantage of lapses in form and timing on the part of the certifier.



Con'td

- A comparison to be made with another case decided by the same judge in ***Lian Soon Construction v Guan Qian Realty (2000)***.
- The Plaintiff sued the Defendant for unpaid amounts due on interim certificates under the SIA form of contract and applied summary judgment.
- 3 days prior to the date for application of summary judgment, the architect issued 2 delay certificates and also granted 52 days EOT to the contractor.

Con'td

- These delay certificates were all issued more than a year after the latest Completion date.
- Warren Khoo J found the delay certificates to be invalid and that the EOT machinery was the foundation.
- The architect had not granted EOT in accordance with the contract mechanism.
- This suggests a dichotomy and this in principle, is defensible as a contractor is prima facie entitled to be paid once the work is done.



MAE ENGINEERING LTD v DRAGAGES SINGAPORE PTE LTD (fka Dragages et Travaux Publics (S) Pte Ltd) (2002)

- Dragages' appealed against the senior assistant registrar's decision to grant MAE's application for summary judgment and disallow the stay of proceedings.
- The learned Rajendran J had to consider whether or not there was any dispute at all between Dragages and MAE in connection with the amounts certified as due to MAE under interim certificates No. 27 and 28.
- The judge was of the view that Dragages' issuance of the revised interim certificates containing deductions were mere attempts to delay payment of the sums so certified and was accordingly satisfied that the rights of set-off claimed by Dragages had no basis whatsoever.

Con'td

- The judge was further of the view that Dragages was contractually bound to pay the moneys over to MAE once MAE had rendered its invoice under Clause 17(4) of the sub-contract and the employer had made the relevant payments in full to Dragages.
- The judge further stated that if Dragages had any rights of set-off, those rights ought to have been exercised before the interim certificate was issued.
- Where there was in fact a deduction, which was overlooked during the issuance of an interim certificate (and where there is no provision in the sub-contract for unilateral issuance of revised interim certificates), the Judge was of the view that the deduction should be made in subsequent interim certificate that may be issued or in the final accounts.



EMPLOYER'S LIABILITY FOR ARCHITECT'S DEFAULT IN CERTIFICATION



B. LIABILITY OF EMPLOYER FOR ARCHITECT'S DEFAULT

- Modern standard form contracts, the task of administering the contract – Architect or S.O.
- They act as an agent of the client in issuing directions or instructions under the contract to the Contractor.
- Required to perform their certification duties independently or impartially.

Con'td

- ***Hong Huat v Hiap Hong (2000)***
- This case concerns the old SIA form of contract.
- Contractor complained of under and later certification and sought to claim interest charges arising from that.
- Judgment delivered by CA – although the architect is employed by the client, he is supposed to be independent and impartial when certifying free from interference.

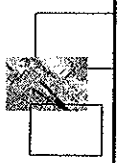


Con'td

- In public Sector form of contract, there is an express disclaimer of liability by the Employer for losses occasioned by late or under certification by the S.O.
- Woo Bih Li JC in the High Court held that the Architect could owe a duty of care to the contractor and be liable for breach of duty if he was negligent in carrying out his certification functions.

Con'td

- Under the current SIA form of contract, there is a discretionary power on the Arbitrator to order interest where there is an under certification by the Architect.
- This decision exposes the consultants to claims for breaches of their certification duties by contractors.



WARRANTIES/ INDEMNITIES & PERFORMANCE BONDS

C. *INDEMNITIES/WARRANTIES & PERFORMANCE BONDS*

INDEMNITIES

- An indemnity is a contract by one party to keep the other harmless against loss. This was the definition given by ***Holroyd Pearce L.J. in Yeoman Credit Ltd v. Latter (1961)***

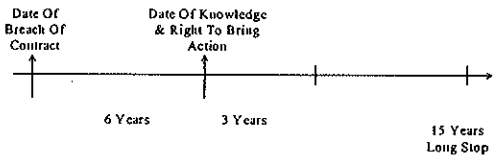
WARRANTIES

- A warranty refers to an undertaking that the title, quality or quantity of the subject matter of a contract is as it appears to be or as it has been represented.
- A breach of warranty entitles the Plaintiff to a claim for damages.

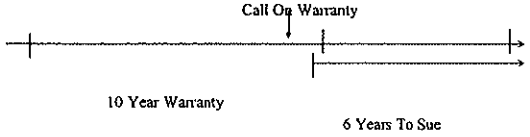


How Warranties Can Be Used To Overcome The Limitation Problem:

Current Limitation



How Warranties Can Be Used To Overcome The Limitation Problem:



GUARANTEES

- A guarantee is a contract to answer for the debt, default or miscarriage of another who is primarily liable to the promisee.
- The liability of a guarantor is secondary to that of a principal debtor and arises only when there is a default by the principal debtor under his contract with the creditor.
- The principal debtor remains primarily liable to the creditor.
- Thus, if the principal debt is for some reason unenforceable or is null and void in law, it follows that no default can arise on the principal debt.

DISTINCTION BETWEEN WARRANTIES & INDEMNITIES

- ***MCST Plan No. 1933 v Comtech Corp Anor (2000)***
- In this case, the High Court had to consider whether the deed in question was an indemnity or a warranty.
- This case involves a claim for defective works of a condominium



Con't

- The Plaintiffs are the Management Corporation for Dormer Park.
- The 1st Defendants were the Main Contractors while the 2nd Defendants were the Nominated Sub-Contractors (NSC) for the aluminum and glazing works.
- The Plaintiffs alleged that the works were defective and proceeded against the 2nd Defendants as the 1st Defendants had gone into liquidation.

Con't

- Central to the decision is the existence of a Deed of Indemnity jointly and severally executed by the 1st and 2nd Defendants for the works in favour of the developer and subsequently assigned to the Plaintiffs.
- Relevant parts of the deed:

  "Whereas:

  The Contractor and the Sub-Contractor have agreed to jointly and severally indemnity the Employer in the manner hereinafter appearing, against any defects in the design, workmanship, quality of materials, uneven fading, peeling, discolouration, watertightness or deterioration in the works to the Premises..."



Con't

- *"... The Contractors and the Sub-Contractors hereby jointly and severally agree with the Employer as follows:*

  ...

  2. In the event of any deterioration or defects (as shall be determined by the Employer) in the workmanship, quality of materials, installation, watertightness or deterioration appearing in the works, the Contractor shall forthwith upon notice given to either of them and within such time as the Employer may direct, effect remedial works..."

Con't

- *"... to the absolute satisfaction of the Employer all damages to surface finishes including but not limited to plaster, paneling, tiling and other similar works, mechanical, electrical or other installations or other property arising directly or indirectly out of the said defects.*
- *3. In the event that remedial works undertaken by the Contractor or the Sub-Contractor prove ineffective as determined by the Employer whose decision shall be final and conclusive, or are not to the satisfaction of the Employer, the Contractor and the Sub-Contractor shall effect such additional works in such a manner and within such time as the Employer may direct and shall carry out all test, as directed by the Employer until all the defects have been remedied to the absolute satisfaction of the Employer."*

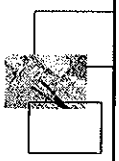


Con't

- *"4. Should the Contractor or Sub-Contractor fail to perform their obligations under Clause 2 and 3 above within a reasonable period, the Employer shall be entitled [sic] to remedy the said defects and the Contractor and the Sub-Contractor shall forthwith on demand reimburse the Employer all costs and expenses incurred by the Employer for making good the said defects including all legal costs on a Solicitor and Client basis incurred by the Employer in enforcing this Clause."*

Con'td

- The Plaintiffs tried to argue that the deed in question was actually a warranty and not an indemnity.
- This was because the Plaintiffs had not done any remedial works themselves and hence they could not claim any reimbursement under Clause 4 as no costs and expenses for remedial works were incurred yet.
- However, if the Plaintiffs could establish that the deed was a warranty, they would be able to sue for damages under Clauses 2 or 3.
- This is because a breach of a warranty gives rise to a claim for damages.



Con'td

- **Decision of the Judge:**
- Chan Seng Onn JC (as he was then) held that the substance of the deed was in the nature of an indemnity as opposed to a warranty.
- He said that when defects arise, the Plaintiffs could not simply sue for damages under the deed.
- The Plaintiffs must first give notice to either the Contractor / Sub-Contractor who would then have to remedy the defects as provided in Clause 2.
- The manner of rectification was left to the Contractor / Sub-Contractor as the case may be.

Con'td

- **Decision of the Judge:**
- If the rectification proved ineffective, then the Contractor and the Sub-Contractor would have to effect additional works in the manner as directed by the Plaintiffs under Clause 3.
- This ensured that they would still have the opportunity to carry out the remedial works although they now had to comply with the Plaintiffs' directions and instructions.
- Clause 4 stipulates what is to happen if the Contractor / Sub-Contractor fails to perform any of their obligations under Clauses 2 or 3.

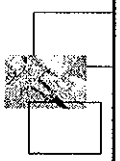


Con'td

- **Decision of the Judge:**
- Only then shall the Plaintiff be entitled to remedy the defects and subsequently claim reimbursement from them.
- Chan Seng Onn JC made it clear that the Contractor / Sub-Contractor had volunteered to subject themselves only to an *indemnity* provided that they were allowed the right to do the remedial works themselves first.
- The entire mechanism of indemnity is that only if the Contractor and the Sub-Contractor for some reason were unable to remedy the defects or they fail to do so, then the Plaintiffs have the right to claim an indemnity for the costs of rectification.

Con'td

- **Decision of the Judge:**
- The Judge differentiated a claim for damages (i.e. when a breach of *warranty* is involved) from an amount payable under an indemnity. He observed that a claim of damages can be at large while the amount payable under the indemnity is limited to the costs of making good the defect plus legal costs.
- The Plaintiffs were hence prevented from circumventing the deed of indemnity by suing for damages for breach of Clause 2 and 3 per se as if the deed were a warranty.



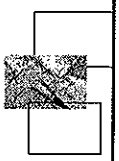
Con'td

- **Significance of the case:**
- The case has made it clear that whether the contract is construed as an indemnity or a warranty would affect the outcome of the proceedings.
- The Deed of Indemnity found in this case is very commonly found in building contracts in Singapore. It is hence important for solicitors to be aware of the Courts' manner of construction of such indemnity clauses.
- These clauses do not operate as a disjunctive warranty allowing claims for damages the moment any one clause is breached.

Con'td

- **Significance of the case:**

- If this is not desired, the draftsman should couch in very clear language that the deed is a deed of warranty and not one of indemnity.
- It is hence important to appreciate the legal differences between indemnities and warranties.



Con'td

- **Conclusion:**

- ***MCST 1933 v Comtech Corp. Pte Ltd*** is instructive that if a party were to sue on an indemnity similar to the one in the case, it must be borne in mind that the Plaintiff has to first allow for remedial works to be carried out by the contractors.
- Only in the event that the contractor fails to remedy the works despite having been given an opportunity to do so can the Plaintiff be entitled to remedy the defects and subsequently claim reimbursement.

Con'td

- **Conclusion:**

- More importantly, the case suggests that if the deed were construed as a warranty as opposed to an indemnity, the Plaintiff would be able to sue for damages despite not having given the contractor a chance to remedy the defects.

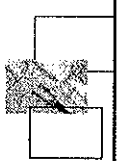


PERFORMANCE BONDS

- Introduction
- Restraint on Calls or Payment on Bonds
- Current Position
- Fraud Exception
- Unconscionability
- Standard of Proof
- Conclusion

- **Introduction:**

- Bank, insurance company or other financial institution ("bondsman").
- At the request of its customer ("account party").
- In favour of a third party ("beneficiary").
- Between 5 to 10 % of the Contract Sum



- **Introduction:**

- Unconditional / on-demand bonds or conditional / default bonds.
- Unconditional or on-demand bonds – bondsman is required to pay simply on demand by the beneficiary without proof of default on the account party.
- High Court decision – ***The Ngee Ann Kongsi v The Tai Ping Insurance Company Limited (1997).***
- Conditional bonds – require proof of breach of the terms of the contract by the account party as a precondition to the bondsman's liability under the bond.

RESTRAINT ON CALLS OR PAYMENT ON BONDS

- Autonomy Principle and the fraud exception to the Autonomy Principle.
- ***Edward Owen Engrg Ltd v Barclay Bank International Ltd and Anor (1978).***
- ***Potton Homes v Coleman Contractors (Overseas) (1984).***
- ***Royal Design Studio Pte Ltd v Chang Development Pte Ltd (1990).***



CURRENT POSITION

- ***Bocotra Construction Pte Ltd v Attorney General (No. 2) (1995)***:

- Court of Appeal – Karthigesu JA:

  "Fraud or unconscionability is the sole consideration in applications for injunctions restraining payment or calls on bonds to be granted. Once this is established, there is no necessity to expend energies in addressing the superfluous question of 'balance of convenience'. It does not lie in the mouth of the defendant to claim that damages would still somehow be an adequate remedy."

FRAUD EXCEPTION

- Where letters of credit are concerned, fraud is confined to the documents presented for payment to the bank by the beneficiary.
- Where performance bonds are concerned, there is limited scope for "documentary fraud".



UNCONSCIONABILITY

- ***GHL Pte Ltd v Unitrack Building Construction Pte Ltd (1999).***
- In April 1997, GHL engaged Unitrack to be the main contractors for their project.
- Contract sum for the project was $5,781,400 which include a sum of $3,820,000 for sub-contracts works.
- Contract sum revised downwards to $1,961,400 due to direct payment from GHL.
- GHL purported to call on the performance bond for the total sum of $578,140.

Con'td

- Court of Appeal – GHL only entitled to an amount equal to 10% of the revised contract sum - $196,140.
- In his judgment, LP Thean JA (as he was then) said:

  "….. It should not be forgotten that a performance bond can operate as an oppressive instrument, and in the event that a beneficiary calls on the bond in circumstances, there there is prima facie evidence of fraud or unconscionability,…. It should also not be forgotten that a performance bond is basically a security for the performance of the main contract, as such we see no reason, in principle, why it should be so sacrosanct and inviolate as not to be subject to the court's intervention except on the ground of fraud……."



Con'td

- In ***Raymond Construction Pte Ltd v Low Yang Tong and AGF Insurance (Singapore) Pte Ltd (1995)*** where Lai J explained unconscionability as follows:

  *"The concept of unconscionability to me involves unfairness, as distinct from dishonesty or fraud, or conduct of a kind so reprehensible or lacking in good faith that a court of conscience would either restraint the party or refuse to assist the party. Mere breaches of contract by the party in question would not by themselves be unconscionable...In my view, **Royal Design Studio** and **Kvaerner Singapore** are illustrations of the circumstances where payments would have been unconscionable."*

Con'td

- The contractors had undertaken to construct a double storey detached house.
- Disputes arose. Owner complained of defective works whilst contractors alleged wrongful refusal or delay by the owners in making payments of certified sums due.
- Injunction dismissed by Lai J who made the following observations:

"..... Plainly he could not allowed to get at the money and add insult of injury until trial. There was a strong evidence that he would postpone meeting his financial commitments by tactics of all sorts. The way he drew his cheques and the delays in his payments were legendary and habitual, if one took into account the fact that he has the unusual hallmark of being the subject of bankruptcy notices and suits for defaults in meeting his commitments."

Con'td

- ***Royal Design Studio Pte Ltd v Chang Development Pte Ltd (1990).***
- The Plaintiffs contracted to build 9 units of terrace houses, within 14 months and to obtain the temporary occupation licence within 17 months of the date of permit to commence construction works.
- The Plaintiffs alleged that the Defendants had delayed their interim payments which in turn severely affected their cash-flow. The Defendants complained that the Plaintiffs had been in delay.
- The Defendants terminated the contract and sought, inter alia, to call on the performance bond. The Plaintiffs obtained an ex parte injunction restraining the Defendants from calling on the bond.

Con'td

- In refusing to discharge the injunction on the bond, the learned Judge said:
- *"In innumerable cases, courts have, in appropriate circumstances, in exercise of their equitable jurisdiction granted interim injunctions restraining parties from enforcing their contractual provisions until the resolution of their disputes then pending...In this case, the defendant is only entitled to call on the bond in the event of breach of contract by the plaintiff. The defendant alleged that the plaintiff was in breach of contract but that allegation is hotly contested; the plaintiff said that I was not in breach and that it was the defendant who was in breach. Obviously, this issue can only be resolved at the trial or arbitration, depending on which forum the parties choose to conduct their litigation. Until that issue is decided in favour of the defendant, it cannot be said that at the moment the defendant is entitled under the agreement to call on the bond."*

Con'td

- ***Kvaerner Singapore Pte Ltd v UDL Shipbuilding (Singapore) Pte Ltd (1993)***
- The Plaintiffs sold to the Defendants some equipment for the sum of $1 m.
- Under the contract, the Defendants were to make part payment of 30% of the purchase price and to pay the balance by way of irrevocable letter of credit. Also, the Plaintiffs were to deliver to the Defendants a performance bond.
- The Defendants made the payment and the Plaintiffs procured the issuance of the performance bond.

Con'td

- Subsequently, the Defendants defaulted in opening the letter of credit for the payment of the balance despite repeated reminders from the Plaintiffs. Instead, the Defendants demanded payment under the performance bond.
- Selvam J, in granting the interim injunction said:

"The defendants invoked the principle in Edward Owen Engineering Ltd v Barclays Bank International Ltd that except in cases of established fraud known to the issuer of the performance guarantee he cannot be restrained from making payment on the ground that the party to the underlying contract disputes liability. Later cases show that it is not an immutable principle of universal application. And in my view it has no application where the injunction is sought against a party to the underlying contract who seeks to take advantage of the performance guarantee where by his own volition he fails to perform a condition precedent in the sense I have described...

Con'td

- *Furthermore, a demand under the performance guarantee can be made only when 'the seller has failed or refused to fulfil his obligations under the contract'. The seller's failure or refusal is a condition precedent to the buyer making a demand. An assertion to that effect is implied in a demand made by the buyer. In circumstances where it can be said that the buyer had no honest belief that the seller has failed or refused to perform his obligation, a demand by the Defendants/buyers in my view is a dishonest act which would justify a restraint order. On the facts of the case a demand made by the buyer was utterly lacking in bona fides."*

Con'td

- ***Anwar Siraj and another v Teo Hee Lai Building Construction Pte Ltd (2003).***
- 3 grounds relied on by the building contractor were as follows:
- The Owner/Employer already had sufficient security for their claims;
- The Owner/Employer's complaints over defects in the construction were the result of defective design by the architect; and
- The Owner/Employer had denied the building contractor access into the premises to carry out rectification work.

Con'td

- The Court of Appeal found that in respect of the first ground it was not the court's task to determine whose cost estimate was more realistic.
- In respect of second ground relied on by the building contractor, the Court of Appeal held that the court was in no position to conclude that there had been defective designing by the architect.
- Lastly, the Court of Appeal was unable to conclude from the voluminous correspondence between parties on this matter that the Owner/Employer was clearly at fault and guilty or unconscionable conduct.



Con'td

- The Court of Appeal finally concluded by finding that "*the court should guard against unnecessarily interfering with contractual arrangements freely entered into by the parties*".

Con'td

- ***Seng Hock Heng Contractor Pte Ltd v Hup Seng Bee Construction Pte Ltd & Anor (2002).***
- The learned Choo Han Teck JC held that the onus lay on the plaintiff to prove that by reason of fraud or unconscionable conduct an injunction ought to issue against the first defendant.
- It was unnecessary nor reasonably possible for the court to embark on an evaluation of the evidence to see whether the costs claimed by the first defendant were correctly and legitimately incurred.



STANDARD OF PROOF

- ***San International Pte Ltd v Keppel Engineering Pte Ltd (1996).***
- San sought an interim injunction to restrain Keppel from receiving a sum of $1,255,520.56 being the balance of a guaranteed sum under a performance bond.
- San sought to adduce evidence that some $3,114,000 was withheld by the Defendants which comprised certified and uncertified sums of work done and retention monies.
- Chelva Rajah JC held :

  "…. Whilst the Plaintiffs were entitled to require the Defendants to set-off certified sums due to them, the other amounts in their hands were at best uncertified claims which have yet to be substantiated and established…."

- ***Four Seas Construction Co Pte Ltd v The Tai Ping Insurance Company (1997).***
- The Plaintiffs had contracted with YHS to build a factory and office building.
- YHS advance monies to the Plaintiffs domestic subcontractor of $5,977,925.26 and direct payments to subcontractors $9.7m.
- YHS made a demand on the performance bond for the sum of $3.2m to cover the loans made to the Plaintiffs.
- Interim injunction was set aside by Tay Yong Kwang JC:

  "The affidavit evidence before him, there was at best a commercial dispute between the parties…"

- ***Sin Kian Contractor Pte Ltd v Lian Kok Hong & Anor (1999).***



- The Plaintiff had agreed to construct a two storey detached house.
- Prior to completion of the works, Employer wrote on 15 Mar 99 to the guarantor to demand payment under bond.
- The architect had issued various notices and directions to the Plaintiff to rectify the defects in the works. Despite these notices and directions, the Plaintiff did not comply thereby prompting the architect to issue the termination certificate on 17 Mar 99.

- ***Eltraco International Pte Ltd v CGH Development Pte Ltd (2000).***
- The project was completed in August 1998.
- Employer had $609,700 in retention monies.
- Main contractor submitted progress claim for $1,605,574.43 including $200,000 of VO agreed with the QS.
- The main contractor attended to some of the defects and thereafter embarked on discussions with the consultants and the employer to offer monetary compensation for some items of defective work.
- Whilst negotiations were still afoot, the employer through their lawyers made a full call on the bond for $2,438,800.

Con'td



- High Court granted an injunction restraining the employer from receiving more than $1.6m.
- Court of Appeal - the works were already completed and that the only reason for withholding certification was the unremedied defects, the Court found that there should be a further reduction of $1m from $1.6m.

LIABILTY FOR DEFECTS

(SETRON V CHUANG U MING)

D. LIABILITY FOR DEFECTS (ARCHITECT)

ARCHITECT'S DUTIES DURING CONSTRUCTION STAGE

- The Architect is expected as part of his engagement to supervise the construction works.
- In the absence of any express contractual provision, it would be implied in law.
- Under SIA Conditions of Appointment (1996 Ed.) Clause 1.1(7), the Architect is required to inspect the works at periodic intervals to ensure works are carried out according to contract.

Court of Appeal – Chuang Uming v Setron (2000)



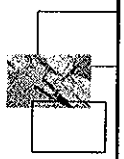
- *"... under these provisions, these was a duty to inspect and supervise the works carried out by the contractors... Where the construction works were important or critical, obviously closer and more frequent inspection and supervision was necessary..."*
- In the absence of any express provision defining the standard of supervision, the Architect would be under a general duty to give reasonable supervision which is defined as would enable the Architect to give an honest certificate according to work executed under the contract.

Con'td

- The Architect is not expected to examine every detail and his failure to discover defects will have regard to the following factors.
- Court of Appeal – ***Cotton v Wallis (1955)*** suggests that an Architect might be justified in accepting lower standards of work where the contract price was low.
- The frequency of supervision will depend on the criticality of the works in question – ***Dabous v Zuliani (1976)***.
- Standards of supervision set out in the contract.

Con'td

- Architect is to inform the QS of the contractor's defective work so that it can be excluded during the valuation process.
- ***Eastern Lagoon*** – the High Court noted that the Architect can discharge his responsibility of supervision if he instructs his COW to ensure that the works comply with the mock-up.
- If the Architect observes that the contractor is failing to take precautions to reduce risks, he should warn the contractor of the consequences.



Con'td

- In ***Sim & Associates v Tan Alfred (1994)***, the employer sued his Architect for breach of duties in certifying defective works for payment.
- The Court of Appeal held that in the absence of any provision in the contract requiring a higher degree of supervision, an Architect is merely required to give reasonable supervision.
- The test of reasonable supervision is to be measured against the standard expected of a reasonably qualified architect.

Delegation of Clerk-of-Works

- Under the SIA Conditions of Appointment (1996 Ed), Clause 1.1(8) contemplates that where frequent or constant supervision of the works is required, a COW should be employed.
- However, the designation to the COW will not absolve the Architect from his duty to ensure compliance with design nor exonerate himself from liability in relying on a COW known to be unreliable.
- In ***Chuang Uming v Setron (2000)***, one of the issues was the extent to which the Architect could deflect responsibility for supervision to the COW.

Con'td

- It was contended that the supervision was entrusted to the COW who was employed directly by the employer for whom was vicariously responsible.
- The Court of Appeal found that his appointment was approved or must have been approved by the Architect.
- Further, in performing his duties, the COW had remained under the control of the Architect in respect of the day-to-day on site supervision of the construction works.



Con'td

- It was also noted that the COW reported directly to the Architect instead of the employer and therefore, bound to inform the Architect of any defects in the works.

REVIEW OF CONSTRUCTION RELATED CASES IN RECENT YEARS

1. Current developments in 2003

Year 2003 has brought with it new developments as well as affirmation of certain legal rights of contractors in the face of a troubled economy where building and construction law is concerned. We will now examine the relevant construction related caselaw in 2003.

Non-disclosure amounting to misrepresentation; taking back of works

- *Chitty on Contracts* (28 ed vol 1 para 6-013 at p 343) which was also repeated in *Hudson's Building and Engineering Contracts* (11 ed vol 1 at para 1.145 p 73) states that :-

  "Non-disclosure. The general rule is that mere non-disclosure does not constitute misrepresentation, for there is, in general, no duty on the parties to a contract to disclose material facts to each other, however dishonest such non-disclosure may be in particular circumstances."

  Further down in the same passage from *Chitty's*, the following extract also appears and which is relied upon by Lai Siu Chiu J. in the case of ***Fu Hai Construction Pte Ltd v Econ Corporation Ltd*** *(Suit No. 1070 of 2001, unreported judgement dated 31.08.2002)*:-

  "Tacit acceptance in another's self-deception does not itself amount to a misrepresentation, provided that it has not previously been caused by a positive misrepresentation. But there are exceptions to the general rule that there is no duty to disclose, namely where the contract is within the class of contracts uberrimae fidei, where there is fiduciary relationship between the parties, and where failure to disclose some fact distorts a positive representation."

- The Court in ***Fu Hai*** accepted that whilst a construction contract is not within the class of contracts of the utmost good faith but where, as in this instance, the plaintiffs had actually inquired from the defendants whether there were any adverse factors the plaintiffs should know about and was assured there were none, the defendants' non-disclosure of the soil condition amounted to a misrepresentation.

- Further, the case of ***Fu Hai*** dealt with the main contractor's whittling down of the subcontract scope of works to exclude major works. The Court found that there was misrepresentation in awarding the sub-contract to the Fu Hai where Econ will be taking away the major works and sub-contracting them to various other sub sub-contractors, without allowing Fu Hai to charge any attendance fee to co-ordinate the works of their appointees. Econ also told Fu Hai that they would appoint the sub sub-contractors. To make matters worse, copies of Econ's various contracts with numerous subcontractors (signed before as well as after the subcontract) were never extended to the Fu Hai at the material time.

Defence of Equitable set-off

- Where a defendant has a cross-claim against the claimant he may be able to set this up in diminution of the claimants' claim, i.e. plead a set-off, or he may counterclaim or he may both set-off and counterclaim. There are essentially three types of set-offs recognised in law: legal set-off, abatement and equitable set-off.

- The recent case of ***Hiap Tian Soon Construction Pte Ltd and another v Hola Development Pte Ltd and another*** *[2003] 1 SLR 667* succinctly laid down the principles where equitable set-off may or may not apply in a building and construction scenario. An equitable set-off can be used where a defendant's counterclaim is closely related to the claim so as to justify it being used as a defence. The case sets out what is a clear rule in applying this doctrine of set-off, i.e. the only cross-claims that may be deducted therefrom are those that are out of the same transaction or are so closely connected with the plaintiffs' demands that it would be manifestly unjust to allow the claim without taking into account the cross-claim.

- It is trite law that parties may, by contract, exclude the remedy of equitable set-off. Lai Siu Chiu, J in deciding that Hola's right of set-off remained intact in ***Hiap Tian Soon Construction Pte Ltd*** held that *"in relation to a building contract one starts with the presumption that each party is to be entitled to all those remedies for breach as would arise by operation of law, including the right of set-off. However, it is open to parties to rebut that presumption by contrary provisions in the contract, provided that clear and unequivocal words are used."* Further, the honourable judge held that it was not necessary for Hola to inform the Hiap Tian Soon that it intended to exercise the right of set-off. She further stated that *"a party purporting to exercise the right of set-off must quantify his loss by means of a reasonable assessment made in good faith"*.

- To put it simply, the following must be considered when considering whether or not equitable set-off can be applied:

1. The defendant must have a valid cross-claim that may be deducted from the same transaction or are so closely connected with the plaintiffs' demands that it would be manifestly unjust to allow the claim without taking into account the cross-claim.

2. The defendant must consider if the remedy of equitable set-off is excluded by the contract. If it is, the defendant cannot set-off his claim against the plaintiff's claim.

3. If the right is not excluded by contract, the defendant must quantify his loss by means of a reasonable assessment made in good faith. The defendant need not inform the plaintiff of his intention to exercise the right of set-off.

- Additionally, the case of ***Hiap Tian Soon Construction Pte Ltd*** stood for the proposition that where the original contract sum was revised downwards, it was unconscionable of Hola to call on the performance bond based on a percentage of the original contract sum. The judge found that Hola was only entitled to call on and demand payment on the performance bond based on 10% of the revised contract sum. It is therefore pertinent to ensure that when considering calling on a performance bond, one can only consider the revised contract sum (when adjusted downwards), and not the original sum.

Certificates - Whether the Architect has the power to issue and withdraw certificate of payment and if so, on what basis

- The Court in the case of ***Steel Industries Pte Ltd v Deen Engineering Pte Ltd [2003] 3 SLR 377*** held that the Architect could withdraw a Certificate if it was issued in error, and not due to his non-approval of the use of the Certificate by the beneficiary. In other words, where the Certificate was validly issued, the beneficiary was entitled to use it as the basis of his claim. The Court further held that even where strict compliance with the contract conditions have been waived, that waiver could not be taken as agreeing to pay under an interim certificate issued years after the prescribed time, in which case, the certificate of payment can be rendered invalid.

- The case further discusses the Certificate of Payment of Main Contractor under Clause 30(2) of the SIA Conditions of Contract and the circumstances in which it may be held to be invalid. The Court held that the Architect prior to issuing the Certificate of Payment must have applied his mind to ascertaining whether the reason for non-payment of the Interim Certificate fell within Clause 30(2)(a). The case confirmed that where the Architect failed to properly consider whether the sole

reason for the Employer's deduction of monies due to the nominated sub-contractor was not due to the Main Contractor's default, then the Certificate was wrongly issue.

- The Court further considered the effect of a corrective certificate issued pursuant to Clause 31(4) of the SIA Conditions of Contract and held adopting the defendant's submissions that in order for an interim certificate to qualify as a revision certificate under Clause 31(4) it had to:

  (a) identify the previous certificate which it sought to correct;

  (b) state the reasons for the correction; and

  (c) set out the details of what was being corrected.

- In finding that the Certificate of Payment was not valid, that Court held that where there was a "pay when paid" contract where the risk of the employer's insolvency is shared; and where insolvency becomes the cause or on of the causes for non-payment by the employers, it would not be right to force the main contractor to pay the sub-contractor out of their own pockets. Further, the Court had to consider the fact that there was an ongoing arbitration between the employers and the defendants wherein the plaintiffs' works formed part of the claim. The Court held in that case that where arbitration proceedings have been initiated, the Architect had no power to issue a certificate of payment. (10)

Whether sub-contractors have a right to receive direct payments under Clause 31(10)(b) prior to the Architect's exercise of its discretion and Whether direct payments to sub-contractors fell within the scope of a scheme of arrangement between the Main Contractor and its creditors

- The Court of Appeal in ***Hitachi Plant Engineering & Construction Co Ltd & Anor v Eltraco International Pte Ltd , Yi Wee Pools & Fountains Pte Ltd & Anor v Eltraco International Pte Ltd [2003] SGCA 38*** confirmed that under Clause 31(10)(b) as it is drafted, the nominated sub-contractors' entitlement to receive direct payment was merely contingent upon the Architects' exercise of their discretion to certify direct payment to the nominated sub-contractors. In so deciding, the Court of Appeal considered the cases of ***B Mullan & Sons (Contractor) Ltd v Ross & Anor (1996) 54 Con LR*** and ***Glow Heating Ltd v Eastern Health Board (1992) 8 Const L J 56.*** The Court further indicated their inclination to adopt the position in the ***Glow*** case and hold that the nominated sub-contractors had a right to direct payments if the Main Contract had stated that it is mandatory for the Architects to certify direct payment upon a particular event. (11)

- Further, in the current financial climate it is pertinent to note that where the Main Contractor falls into a scheme of arrangement, the nominated sub-contractor may bring to the attention of the Court sanctioning the scheme of arrangement, if there was a contingent entitlement to direct payments, the principles enunciated in ***UDL Argos Engineering & Heaving Industries Co Ltd v Li Oi Lin*** *[2001] HKCFA 53*, in deciding if it should direct a separate meeting for the nominated sub-contractors. The Court of Appeal held that the nominated sub-contractors' argument that their right to direct payments can only be affected by an express term in the scheme fails because they did not have a right to those payments when the scheme of arrangement was approved and sanctioned. The Court of Appeal further found that the direct payments would fall under the scheme of arrangement because they form part of the 'accounts receivable' by the Main Contractor, Eltraco.

- For completeness, the principles enunciated in accordance with which creditors should be divided into classes in the case of ***UDL Argos Engineering*** are as follows:

  (1) It is the responsibility of the company putting forward the Scheme to decide whether to summon a single meeting or more than one meeting. If the meeting or meetings are improperly constituted, objection should be taken on the application for sanction and the company bears the risk that the application will be dismissed.

  (2) Persons whose rights are so dissimilar that they cannot sensibly consult together with a view to their common interest must be given separate meetings. Persons whose rights are sufficiently similar that they can consult together with a view to their common interest should be summoned to a single meeting.

  (3) The test is based on similarity or dissimilarity of legal rights against the company, not on similarity or dissimilarity of interests not derived from such legal rights. The fact that individuals may hold divergent views based on their private interests not derived from their legal rights against the company is not a ground for calling separate meetings.

  (4) The question is whether the rights which are to be released or varied under the Scheme or the new rights which the Scheme gives in their place are so different that the Scheme must be treated as a compromise or arrangement with more than one class.

(5) The Court has no jurisdiction to sanction a Scheme which does not have the approval of the requisite majority of creditors voting at meetings properly constituted in accordance with these principles. Even if it has jurisdiction to sanction a Scheme, however, the Court is not bound to do so.

(6) The Court will decline to sanction a scheme unless it is satisfied, not only that the meetings were properly constituted and that the proposals were approved by the requisite majorities, but that the result of each meeting fairly reflected the views of the creditors concerned. To this end it may discount or disregard altogether the votes of those who, though entitled to vote at a meeting as a member of the class concerned, have such personal or special interests in supporting the proposals that their views cannot be regarded as fairly representative of the class in question.

The cases which will be discussed shortly sets out clearly the position taken by the Courts in Singapore in relation to building and construction law. The cases featured in this seminar are not meant to be exhaustive but are useful indications of the local legal position of the main players in the construction field.

2. Contract Formation

- In a typical construction project, a large number of parties are involved and a lot of documents are exchanged. Often, contracts may be poorly drafted and sometimes, there may be an absence of full documentation with many of the agreements being entered orally.

- Contractors may work with particular sub-contractors on more than 1 project and often assumes that things will be done as before without specific documentation or clear incorporation of a past course of dealing.

- The recent unreported case of ***Shia Kian Eng (trading as Forest Contractors) v Nakano Singapore (Pte) Ltd*** *(Suit 600245/2000. HC, unreported judgment dated 3.4.2001)* illustrates how the court decides on which documents form part of the contract.

- This case arose out of the construction of the development known as Woodsvale Executive Condominium. The developer appointed Nakano as their main contractor under a design and build contract. Nakano in turn appointed a number of sub-contractors to carry out different aspects of the works, one of which was Shia Kian Eng who carries on construction work under the name of Forest Contractors.

- There were a number of disputes between the parties. Forest had sued for non-payment, under payment and damages while Nakano counter-sued for damages claiming that it was repudiation on the part of Forest that caused it to terminate Forest's works before they were completed and as a consequence, incur additional expenses to procure the completion of the works. In addition, Nakano also claimed that part of Forest's works were defective.

- One of the issues before the court was what documents evidenced the contracts evidenced the contracts between the parties. Forest and Nakano agreed that there was no single sub-contract which covered the works to be carried out by Forest in relation to the project. They differed, however, as to the form in which the various sub-contracts took.

- Forest's position was that there were made partly orally, partly in writing and partly by conduct. Further, during the course of the various sub-contract works, Forest had pursuant to reference to the Purchase Orders which Nakano, carried out additional and variation works.

- Nakano's position was that the sub-contracts were wholly in writing and that they comprised the Purchase Orders issued by Nakano and the various other documents mentioned in those Purchase Orders. The Purchase Orders took a standard format and all referred to the relevant quotation submitted by Forest. In additional, almost all referred to a document entitled "Conditions of Sub-contract" and many referred to an "Undertaking on Hiring of Foreign Workers." The Purchase Order which caused the most dispute related to the contract for block wall and external wall plastering and that referred, in addition to the documents just mentioned, to a document entitled "Conditions of Purchase", to one entitled "Bills of Quantity/Schedule of Rates" and to "Drawings".

- It is not in dispute that none of the Purchase Orders were issued before Forest started work on any of the sub-contracts. They were only given to Forest subsequently when he asked how payment was to be made.

- The Court held that the sub-contracts were partly in writing and partly oral and the written portions of the sub-contracts comprised the quotations and the purchase orders. However, documents which were simply mentioned in the purchase orders did not form part of the contract. The Court found that:

  (i) it was not clear that there was active negotiation by the parties on the form of terms and conditions or that they had started work on the assumption that these would eventually be agreed and made applicable to the parties; relationship.

  (ii) No evidence that copies of the standard purchase orders and conditions of sub-contract were given to the sub-contractor

  (iii) Nakano was familiar with the practice in the construction industry of having letters of intent with a provision indicating that a formal contract would follow. Yet no such letter of intent was issued.

  (iv) As for some other documents, whilst the purchase orders mentioned that these documents were annexed to them, not all the documents were indeed so annexed.

- In short, if documents are not furnished by one party to another prior to or at the time of signing of the contract, it is difficult to incorporate them as part of the contract unless there is clear indication by that other party that he would accept documents subsequently.

3. **Contracting Parties**

- A contractor may sometimes change its name, especially when it undergoes incorporation.

- In ***Lai Yew Seng Pte Ltd v Pilecon Engineering Bhd*** *[2002] 3 SLR 425*, the Court had to decide whether a plaintiff was entitled to sue on a contract between its former entity and the defendant.

- The defendant, Pilecon, was the main contractor to 3 school building projects for the government. The plaintiff was its sub-contractor. There was an issue whether Lai Yew Seng Iron Works (the company's previous name before it was incorporated under its present name) was the same as the plaintiff and was entitled to sue Pilecon for work done under the sub-contracts.

- Pilecon argued that the contracts of employment were all made between Pilecon and the firm known as Lai Yew Seng Iron Works and not with the plaintiff, Lai Yew Seng Pte Ltd.

- The High Court, on appeal, held that Pilecon had all along accepted Lai Yew Seng Pte Ltd as its contractual partner and known that it had changed to its present name and taken on limited liability corporate identity. Furthermore, there was no dispute that the work had been done by Lai Yew Seng Pte Ltd.

- Even though there was an issue as to whether there was an assignment of the contracts to Lai Yew Seng Pte Ltd from Lai Yew Seng Iron Works, the court was of the view that the parties were in a contractual relationship distinct from the original contract. Pilecon had benefited from the plaintiff's work and had paid the plaintiff the initial progress payments for the work. Hence, the court held that even if there was no assignment of contract, there was an apparent contractual relationship between the parties which was extraneous and independent to the ones signed between Pilecon and Lai Yew Seng Iron Works.

4. **Clauses stating that time is of the essence**

- It is not usual for the contract to contain a clause stating that time is of the essence. Where such a clause exist, failure to complete the works by the stipulated date entitle the innocent party to terminate the contract.

- In the case of ***National Skin Centre (Singapore) Pte Ltd and v Eutech Cybernetics Pte Ltd [2002] 1 SLR 241***, the Plaintiff, the National Skin Centre ("NSC") brought an action against Eutech Cybernetics for breach of contract to commission a computer system with customized software within the stipulated time under the contract.

- Sometime in 1998, in compliance with the government policy of reviewing computer systems to ensure that they will be able to operate after 31 December 1999, NSC decided to replace its existing system, which was not Y2K compliant, with a new system that would. A closed tender was called and after reviewing the proposals of the tenderers, NSC awarded the contract to Eutech. The commission of the system was supposed to be carried out by 31 August 1999.

- Eutech failed to meet the target date. Several extensions of time were given by NSC. However, Eutech failed to commission the system even within the extended time. Finally, on 11 February 2000, NSC issued a letter to Eutech stating that the project was already in delay for more than 5 months and that NSC expected the full system to be delivered within 3 months (ie by 11 May 2000).

- Eutech subsequently responded with 2 more proposals, each suggesting that it would not be able to meet the revised dates.

- NSC took this to be a clear expression by Eutech that it could not deliver the system by deadline of 11 May 2000 and accordingly terminated the contract by a letter dated 21 March 2000.

- Eutech alleged that the termination by NSC on 21 March 2000 was wrongful for the following reasons:

  (a) after expiry of the various stipulated dates under the contract, NSC had not elected to terminate the contract but instead had, by is conduct, elected to continue with the contract;

  (b) NSC had agreed to the revised schedules, or alternatively, had induced Eutech to work in accordance with the revised schedule; and

  (c) NSC had issued a letter to Eutech on 11 February 2000 giving Eutech a period of 3 months to deliver the system. Despite this, the letter of termination of 21 March 2000 was issued only one and a half months after the 11 February letter.

- It was held by the High Court that when NSC elected not to terminate the contract after Eutech was in breach by its failure to commission the system on 31 August 1999, but chose to continue with it, time was set at large and was no longer a condition. However, NSC was entitled thereafter to make time of the essence again by giving reasonable notice to Eutech. NSC's letter dated 11 February 2000 constituted such notice.

5. **Termination due to delays in work**

- Delays are commonplace in construction contracts.

- When there is a delay, the employer is often entitled to impose liquidated damages. But the delay may sometimes reach a point where liquidated damages no longer sufficiently compensates the employer and the employer may need to consider replacing the main contractor.

- When the contract is unclear as to when the employer may replace the contractor concerned, the general law of repudiatory breach must be replied upon.

- One of the issues that arose in ***Shia Kian Eng (trading as Forest Contractors) v Nakano Singapore (Pte) Ltd (Suit 600245/2000. HC, unreported judgment dated 3.4.2001)*** was whether the slow progress of the sub-contract works was sufficient to justify the termination of the sub-contract.

- Judith Prakash held that although there had been delay that did not of itself amount to repudiation. The learned judge re-affirmed the principle that not every breach of contract justifies termination and that delay to

construction works per se does not amount to repudiation unless it is of such magnitude and character as to show that the contractor is either unable to proceed with the works or had no intention of proceeding with them.

- Prakash J noted that when the termination notice was served, the main contractors (ie Nakano) were not yet late and there was no evidence that following the termination of the sub-contractors (ie Shia Kian Eng), the works were completed any faster than they would have been had the sub-contractors continued.

- Further, the slow progress of the works was not entirely due to default on the part Shia Kian Eng. Shia Kian Eng' works, namely the plastering works, were given a lower priority than the concreting works. For eg, resources that Nakano was already short of was first allocated to other sub-contractors rather than Shia Kian Eng.

- Lastly, it was also significant that Nakano was rather haphazard in the communication of its construction programme to its sub-contractors, including Shia Kian Eng.

- Having considered the evidence as a whole, the court held that whilst Shia Kian Eng did not work as fast as Nakano desired or as fast as it could have, there were various reasons for its slow progress and among these were the deficiencies of Nakano's part as well. The court further held that it was not at all clear at the time of termination that delays on the part of Shia Kian Eng would have a devastating impact on Nakano's work. Instead of resorting to termination, Nakano could have continued to chivvy Shia Kian Eng to hurry up and also make a claim against it for damages if in fact the completion of the project was delayed due to Shia Kian Eng's slow speed.

- Accordingly, the court held that there was no justification for the termination for the Shia Kian Eng's sub-contract by Nakano.

6. <u>Common or Unilateral Mistake</u>

- It is not uncommon in construction contracts for disputes to arise over quantities of building materials or equipment left on site.

- Usually, such a dispute arises as a result of a measurement or valuation issue. However, in ***Ho Seng Lee Construction Pte Ltd v Nian Chuan Construction Pte Ltd [2001] 4 SLR 407***, the issue that surfaced was whether the contracts in question should be rectified or rescinded on the round of common or unilateral mistake.

- The case involved a dispute over how many metal-forms were on site under a rental agreement.

- Ho Seng Lee leased metal-forms to builders for use in constructing buildings. Nian Chuan entered into 3 agreements with Ho Seng Lee under which they rented metal-forms from Ho Seng Lee. Ho Seng Lee claimed that there was outstanding rental due to them from Nian Chuan arising under the 3 agreements. Nian Chuan then disputed the number of metal-forms on each site at the time the rental agreements were entered into and asserted that the agreement were not binding on or enforceable against them due to common mistake of the parties at the time the agreements were entered into, or alternatively, unilateral mistake on their part as to the number of metal forms leased.

- Although the Court held that the number of metal-forms on each site was not the number stated in the rental agreements, Nian Chuan was unable to escape from its contractual liability to pay hire in respect of the contractually stated numbers. Whether Nian Chuan can do so depends on whether their contracts with Ho Seng Lee had been vitiated by mistake.

- Judith Prakash, J relied on the case of ***Associated Japanese Bank (International) v Credit du Nord SA [1988] 3 All ER 902*** in which the principles of common mistake was set out.

- Firstly, the law ought to uphold rather than to destroy apparent contracts.

  - The court regarded this point as more of a timely reminder to the judge considering such an issue that to grant a party relief from a contractual obligation on the basis of a mistake is something that is not lightly or commonly done.

- Secondly, the common law rules as to a mistake regarding the quality of the subject matter, like the common law rules on regarding commercial frustration, are designed to cope with the impact of unexpected and wholly exceptional circumstances.

  - The court accepted Ho Seng Lee's submission that any discrepancy in the quantities of metal-forms arose purely from the Defendants' failure to check them before signing the acknowledgement forms despite being given ample opportunity to do so. The circumstances are neither unexpected nor exceptional.

- Thirdly, such a mistake in order to attract legal consequences must substantially be shared by both parties, and must relate to facts as they existed at the time of the contact.

  - The court accepted that both parties were mistaken in that the quantities on site were probably not the quantities reflected in the rental agreements. However the court considered the real question to be whether the subject matter of the 3 agreements was essentially different from what it was reasonably believed to be. The court accepted Ho Seng Lee's submission that there was absolutely no mistake by either party, at the time each contract was entered into, as to the quantity of the metal forms intended to be leased. The dispute as to quantity arose solely as a result of the Nian Chuan's failure to check on the quantities on site. If Nian Chuan had carried out checks, there would still have been rental agreements between the parties – the only difference would have been that the number of forms reflected in each agreement would have been different.

- Fourthly, the mistake must render the subject matter of the contract essentially and radically different from the subject matter which the parties exist.

  - The court found that the mistake related only to the quantity. The essence of the contract, namely the lease of metal-forms was not diminished. Since Nian Chuan in fact received more than sufficient metal forms though not as many as stated on the agreements, the subject matter of the contracts was not radically or essentially different from the subject matter which the parties believed to exist.

- Fifthly, the court must ascertain whether there were reasonable grounds for the Defendants' belief.

  - The court did not need to consider this point as the subject matter of the contracts was not radically or essentially different from the subject matter which the parties believed to exist.

- The court was not satisfied that Nian Chuan had satisfied the essential element of unilateral mistake in that they could not show that Ho Seng Lee knew that Nian Chuan were mistaken about the quantities of the metal-forms on each site.

- As Nian Chuan was unable to establish the defence of mistake, they were bound by the contracts that they signed.

7. Performance Bonds

NB: This is only a brief overview of the current legal position concerning performance bonds in Singapore. We will be studying this topic with more in-depth later.

- Settled law in Singapore that calls on performance bonds can be restrained on the ground that the call was fraudulent or unconscionable.

- Strict position under English Law. On-demand bonds are as good as "cash in hand". The English Courts will not restrain a call on payment unless fraud is involved: ***Edward Owen Engineering v Barclays Bank International*** *(1978) QB 159*

- In Singapore, our courts have departed from the strict position in England. In ***Royal Design Studio Ltd v Chang Development Ltd*** *[1991] 2 MLJ 229*, it was suggested that the seller should be able to prevent a call upon the bond "*if there is a failure of consideration.*"

- The doctrine of unconscionability was first brought up in ***Bocotra Construction and Attorney General*** *[1995] 2 SLR 733*. Kathegesu, J stated in his judgement that the sole consideration in applications for injunctions restraining payments or calls on bonds to be granted is whether there is fraud or unconscionability.

- The concept of unconscionability was thereafter defined in subsequent cases:

  - ***Raymond Construction v Low Yang Tong*** *[1995](Suit 1715 of 1995)*

  - ***GHL Pte Ltd v Unitrack Building Construction Pte Ltd*** *[1999] 4 SLR 604*

  - ***Eltraco v CGH Developments*** *[2000]4 SLR 290*

- A recent case where the Singapore Courts made use of the doctrine of unconscionability to restrain a performance bond: ***Samwoh Asphalt Premix Pte Ltd v Sum Cheong Piling Pte Ltd & Anor*** *[2002] 1 SLR 1*

  Sum Cheong were the Main Contractors of a construction Project with the Ministry of Defence. Samwoh was the sub-subcontractors for the paving works and had earlier furnished Sum Cheong with a demand bond. When the sub-contractors for the pavement and drainage works

repudiated the contract and dropped out, Samwoh then negotiated directly with Sum Cheong for a new contract. However negotiations broke down over the issue of price and Sum Cheong called on the bond.

- The Court of Appeal reiterated that unconscionability on the part of the beneficiary in calling for payment under a performance guarantee is a separate and distinct ground from fraud for seeking injunctive relief. The Court then held that the call for payment by Sum Cheong under the performance bond was not based on any bona fide claim they had against the Samwoh. The clear inference was that they invoked the performance bond as a bargaining chip to compel Sum Cheong to agree to their terms. It was an abusive call on the performance bond and in all the circumstances, Samwoh had acted unconscionably in calling for payment and should have been restrained.

- Recently, there is an interesting twist in the field of performance bonds. The past year saw a unusual case whereby the bondsman (as opposed to the contractor who had procured the bond) sought to restrain an employer's call on a performance bond issued by it: ***Chew Pin Pin v AGF Insurance (Singapore) Pte Ltd [2001] 2 SLR 152.***

  Chew Pin Pin employed TDS Construction Pte Ltd to construct and build 3 houses at Robin Road. Pursuant to the contract between them, TDS procured a performance bond issued by AGF Insurance in Chew Pin Pin's favour. TSD went into liquidation and Chew Pin Pin subsequently called on the bond. AGF Insurance refused to pay. Action was commenced against AGF Insurance and summary judgement was obtained against AGF Insurance by Chew Pin Pin. AGF Insurance appealed to the District Judge and the appeal was dismissed. AGF Insurance then appealed to the High Court.

- AGF Insurance sought to rely on the underlying contract between Chew Pin Pin and TDS, arguing that in fact monies were due to TDS and hence the call was unconscionable, at least until such time as Chew Pin Pin proved his entitlement to damages from TDS.

- Choo Han Teck JC dismissed the appeal and held that AGF Insurance had no defence as the terms of the bond provided for payment upon demand without question. Choo JC stated in his judgment that the reference to the underlying contract was that made between Chew Pin Pin and AGF Insurance where in consideration of Chew Pin Pin not seeking a security deposit from TDS, AGF Insurance warranted that it would pay Chew Pin Pin the bond amount upon demand without question.

- The basis of intervention to restrain calls upon performance bonds is unconscionability between the employer and the contractor. When a performance bond is called, the bondsman will have immediate recourse to the contractor. As between employer and bondsman, the only question is the allocation of the risk of the contractor's insolvency. The purpose of the performance bond is precisely to protect the employer from that risk and to shift the risk to the bondsman. The bondsman would have the opportunity to price that risk in its initial negotiation with the contractor.

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WongPartnership
(Updated as of 16 December 2003)

A. INTERIM CERTIFICATES & DELAY CERTIFICATES
(with consideration of recent case law)

Payment certificates and temporary finality in the SIA form of contract

1. The role of interim certificates in regulating the financial position of parties in the SIA form of contract has been considered in numerous cases e.g. ***Tropicon Contractors v Lojan Properties.***

2. In ***China Construction (South Pacific) Development Co Pte Ltd v Leisure Park (Singapore) Pte Ltd [2000] 1 SLR 622***, an interim certificate was challenged by the employer. The employer contended that the interim certificate did not conform to the contract requirements by showing the valuation date and was issued long after the valuation date and even if it was regarded as a corrective certificate, the certificate was not in the form or content a corrective certificate issued properly under clause 31(4). The current case of ***Steel Industries Pte Ltd v Deen Engineering Pte Ltd*** further dealt with the requirements required for the issuance of corrective certificate.

3. The Employer's arguments in ***China Construction*** did not find favour with the High Court. Warren Khoo J found that in keeping with the philosophy behind interim certificates, an interim certificate of the architect ought to be honoured and accorded temporary finality pending review unless it can be shown in a summary way that the certificate had not been issued in the proper exercise of the architect's powers under the contract. The Court found that although strict compliance with the certification requirements should be the norm, the Courts will not insist in strict adherence which would enable the employer to take advantage of lapses in form and timing on the part of the certifier.

4. It would be useful to contrast the decision in ***China Construction*** with another case decided by the same judge in ***Lian Soon Construction Pte Ltd v Guan Qian Realty Pte Ltd [2000] 1 SLR 495. Lian Soon*** concerned a case where the contractor sued the developer for unpaid amounts due on interim certificates under the SIA form of contract and applied for summary judgment. Just three days prior to the date for application of summary judgment, the architect then issued two delay certificates, one for the main building and the other for a sub station. The architect also granted the contractor 52 days extension of time. These delay certificates were all issued more than a year after the latest extended completion date.

5. Warren Khoo J found the delay certificates to be invalid. The learned judge found that extension of time machinery was the foundation of the delay certificate and that the architect had not granted extensions of time in accordance with the contract mechanism. More interestingly, the Court opined that where a certificate purports to detract from the contractor's right to be paid, the court will

scrutinise the exercise of that power more closely than it would in the case of payment certificates. This suggests a dichotomy in treatment of certificates issued by the Architect. In principle, this dichotomy is defensible as a contractor is prima facie entitled to be paid once the work is done. The money has been earned and the burden is on the paying party to show good reasons why the contractor should not be paid.

6. In the case of ***MAE Engineering Ltd v Dragages Singapore Pte Ltd (fka Dragages et Travaux Publics (S) Pte Ltd) [2002] 3 SLR 45***, the learned Rajendran J dismissed Dragages' appeal against the senior assistant registrar's decision to dismiss Dragages' application for stay of proceedings and grant of MAE's application for summary judgment. In so doing, the learned Judge had to consider whether or not there was any dispute at all between Dragages and MAE in connection with the amounts certified as due to MAE under interim certificates No. 27 and 28. The judge was of the view that Dragages' issuance of the revised interim certificates containing deductions were mere attempts to delay payment of the sums so certified and was accordingly satisfied that the rights of set-off claimed by Dragages had no basis whatsoever.

7. The judge was further of the view that Dragages was contractually bound to pay the moneys over to MAE once MAE had rendered its invoice under Clause 17(4) of the sub-contract and the employer had made the relevant payments in full to Dragages. The judge further stated that if Dragages had any rights of set-off, those rights ought to have been exercised before the interim certificate was issued. Not having done so and the contractual obligation to pay having crystallized, it was no longer open to Dragages to unilaterally vary those contractual obligations by issuing revised interim certificates to replace the interim certificate already issued. Further, the Court noted that there was in fact no provision in the sub-contract for the unilateral issue of such revised interim certificates.

8. Where there was in fact a deduction, which was overlooked during the issuance of an interim certificate (and where there is no provision in the sub-contract for unilateral issuance of revised interim certificates), the Judge was of the view that the deduction should be made in subsequent interim certificate that may be issued or in the final accounts.

B. LIABILITY OF EMPLOYER FOR ARCHITECT'S DEFAULT IN CERTIFICATION FUNCTIONS & THE COURT OF APPEAL DECISION IN HONG HUAT DEVELOPMENT CO PTE LTD V. HIAP HONG & CO PTE LTD

9. Under modern standard form contracts, the task of administering the contract falls on either the Architect or the Superintending Officer. It is trite law that an Architect or SO acts as the agent of the client in issuing directions or instructions under the contract to the Contractor. However, where the Architect or SO performs certification duties under the contract, he is required to carry out those duties independently or impartially.

10. Until the Court of Appeal decision in ***Hong Huat Development Co Pte Ltd v Hiap Hong & Co Pte*** **Ltd** [2000] 2 SLR 609, it was unclear as to whether the Employer would be liable for the Architect 's default in performing his certification duties. If the Architect acts as agent of the Client in certifying, then the Client would be liable under ordinary principles of agency.

11. This case concerns the old SIA form of contract. The contractor had complained of under and late certification and sought to claim interest charges arising from late and undercertification. In a sterling judgment delivered by the CA, the CA found that although the architect is employed by the client, he is supposed to be independent and impartial when certifying free from interference. A lay employer should not be placed in a position where he warrants the performance of the architect without knowing that the architect had failed to discharge his duties.

12. Whilst the decision appears to be rightly decided on the facts and pleadings, it carries wider implications. If the Architect is not liable, then what recourse does the contractor have? In the case of the Public Sector form of contract, this issue is a very real one as there is an express disclaimer of liability by the Employer for losses occasioned by late or under certification by the SO. One strong possibility which was canvassed by Woo Bih LI JC in the High Court decision is that the Architect could owe a duty of care to the contractor and be liable for breach of duty if he was negligent in carrying out his certification functions.

13. It is submitted that under the current SIA form of contract, there is already a discretionary power on the part of the Arbitrator to order interest where there is undercertification by the Architect. Thus, in the case of an arbitration governed by the 1980 and post-1980 SIA forms, the arbitrator would have a discretion to order interest.

14. The decision holds important implications for consultants as it exposes them to claims for breaches of their certification duties by contractors.

C. WARRANTIES/INDEMNITIES & PERFORMANCE BONDS

1. Warranties/Indemnities/Guarantees

Indemnities

15. An indemnity is a contract by one party to keep the other harmless against loss. This was the definition given by ***Holroyd Pearce L.J. in Yeoman Credit Ltd v. Latter [1961] 2 All ER 294.***

16. In a contract of indemnity, the liability of a person giving an indemnity is primary and is not dependent on the default or failure of a prior party to perform his contract. The promisor undertakes an original and independent obligation to indemnify, as distinct from a collateral contract.

Warranties

17. A warranty refers to an undertaking that the title, quality or quantity of the subject matter of a contract is as it appears to be or as it has been represented. A breach of warranty entitles the Plaintiff to a claim for damages.

18. Unlike an indemnity or guarantee, a warranty does not necessarily relate to the obligations of a third party. It should be noted that the terms warranty and guarantee are often used interchangeably although this should not be so in strict legal terms. There is some historical basis for this usage for it appears that the two words were once the same, the letter "g" of the Norman-French being convertible with the "w" of the German and English.

Guarantees

19. A guarantee is a contract to answer for the debt, default or miscarriage of another who is primarily liable to the promisee. The liability of a guarantor is secondary to that of a principal debtor and arises only when there is a default by the principal debtor under his contract with the creditor. The principal debtor remains primarily liable to the creditor. Thus, if the principal debt is for some reason unenforceable or is null and void in law, it follows that no default can arise on the principal debt.

Distinguishing Features Between Guarantees And Indemnities

20. Most of the leading textbooks on guarantees contain a section on the differences between guarantees and indemnities. There have also been a number of cases discussing the differences between guarantees and indemnities.

- The case of ***Birkmyr v. Darnell (1704) 1 Salk. 27*** gave a very good example of the distinguishing feature between contract of guarantee and a contract of indemnity. The judge in that case said:
  "If two come to a shop, and one buys, and the other, to gain him credit, promises the seller, if he does not pay you, I will; this is a collateral undertaking, and void without writing, by the Statute of Frauds: but if he says, Let him have the goods, I will be your paymaster, or I will see you paid, this is an undertaking as for himself, and he shall be intended to be the very buyer, and the other to act but as his servant."

- In the first scenario, the person is the guarantor while in the latter scenario, he is giving an indemnity.

21. The most significant difference between guarantees and indemnities is that a guarantor's obligation to pay arises only on default of payment by the principal debtor. Whereas for an indemnity, a third party undertakes payment to the creditor irrespective of whether the principal debtor has been in default.

Distinction between Warranties and Indemnities

22. The distinction between warranties and indemnities was considered in ***MCST Plan No. 1933 v Comtech Corp Pte Ltd & Anor***[1]. The case concerned an action brought by the management corporation against the contractor and sub-contractor, who constructed the windows in the condominium based in a deed of indemnity given by them jointly, the benefit of the indemnity having been assigned by the developer to the management corporation. As there were defects in the windows, the management corporation gave notice to the indemnitors in accordance to clause 2 of the indemnity. Clause 3 of the deed of indemnity provided that in the event that the remedial works undertaken by the indemnitors proved ineffective, the indemnitors shall effect such additional works as the management corporation may direct until all the defects have been rectified.

23. Clause 4 provided that should the indemnitors fail to perform their obligations under clauses 2 and 3 of the deed within a reasonable period, the management corporation shall be entitled to remedy the said defects and the indemnitors shall reimburse the management corporation all costs and expenses incurred by them in making good the said defects including legal costs on an indemnity basis. The High Court held that the deed of indemnity contemplated that only if the defendants were unable to remedy the defects or fail to do so would the plaintiffs have the right to claim an indemnity for the cost of rectification. Since the plaintiffs had not expended any moneys to remedy the defects, they could not claim any reimbursement under the deed as yet.

[1] *Suit 119/2000, unreported.*

24. The plaintiffs sought to get round this problem by arguing that the deed of indemnity was actually a warranty and, consequently, could sue for damages for breach of clauses 2 and 3. This contention was rejected by the High Court, which found that the deed was in substance an indemnity and not a warranty. The learned judicial commissioner drew a distinction between a claim on a warranty and a claim based on an indemnity. In the case of a breach of warranty, a right to damages arises whilst the claim under the indemnity is explicitly limited to the costs of making good the defects plus legal costs on an indemnity basis. As the plaintiffs had not yet incurred the costs of rectification, their claim was premature and hence their action failed. The plaintiffs appealed against this decision.

25. On appeal, the Court of Appeal allowed the appeal by a majority[2]. The Court of Appeal considered that in equity, a contract of indemnity could be specifically enforced by the indemnitee against the indemnitor as soon as liability covered by the indemnity has arisen. The indemnitee did not have to pay first before seeking relief[3]. In the case of an express indemnity such as that found in the instant case, the question of when a cause of action accrues depends on the terms of the indemnity and the construction of those terms[4]. In construing clauses 2 and 3 of the deed, the Court of Appeal found that a breach of either of these clauses gave rise to an action for damages at law. The court went on to observe that clause 4 of the deed did not expressly or by implication remove the right of the plaintiffs to sue for damages of common law. There was no requirement that the plaintiffs had to first remedy the defects and incur the costs of doing so before their cause of action on the indemnity accrued.

Significance Of The Case

26. ***The Management Corporation Strata Title Plan No. 1933 v. Comtech Corporation Pte Ltd and Liang Huat Aluminium Limited*** has made it very clear that whether a contract is construed as an indemnity or a warranty would affect the outcome of the case.

27. The Deed of Indemnity as found in that case is one which is very common in building contracts. It is hence important for solicitors to be aware of the manner which the courts would construe the operation of such clauses in the deed and that the clauses do not each operate as a disjunctive warranty allowing one to make a claim for damages the moment one of the clauses is breached.

[2] *CA 125/2000, unreported.*
[3] *See Johnston v Salvage Association (1887) 19 QBD 458.*
[4] *See Telfair Shipping Corp v Intersea Carriers SA [1985] 1 WLR 553, which was cited with approval by the Court of Appeal.*

28. If this is not desired, the draftsman should perhaps couch in very clear language that the deed is a deed of warranty and not one of indemnity and that in the event of a breach of any of the clauses, the right to damages arises immediately. It is therefore necessary to appreciate the differences between indemnities and warranties and to be aware of the different legal implications when each of them is used.

29. The case of ***The Management Corporation Strata Title Plan No. 1933 v. Comtech Corporation Pte Ltd and Liang Huat Aluminium Limited*** is enlightening in that if someone were to sue on an indemnity similar to the one in the case, it should be borne in mind in the light of the case that in order for a claim to be made, the Plaintiff has to first allow for remedial works to be carried out by the contractors. Only in the event that contractor fails to remedy the works despite having been given an opportunity to do so can the Plaintiff be entitled to remedy the defects and subsequently claim reimbursement.

30. More importantly, the case suggests that if the deed were construed as a warranty as opposed to an indemnity, the plaintiff would be able to sue for damages for a breach of warranty despite not having given the contractor a chance to remedy the defects.

2. Performance Bonds

31. A performance bond is essentially an undertaking by one party usually a bank, insurance company or other financial institution ("bondsman") given at the request of its customer ("account party") in favour of a third party ("beneficiary") whereby the bondsman undertakes to indemnify or pay the beneficiary up to a specified amount in the event of the account party's breach of his obligations to the beneficiary. Performance bonds have become a well entrenched feature in our construction industry. They serve as security for the performance of the contract by the contractor. Most building contracts would contain a provision requiring the contractor to furnish a performance bond in favour of the Employer. In Singapore, it is common to find employers requiring bonds to be provided for between 5 to 10% of the Contract Sum. In some instances, the provision of a performance bond by the contractor is couched as a condition precedent to the contractor's entitlement to be paid under the contract.

32. Performance bonds are either unconditional / on-demand bonds or conditional / default bonds.

33. Unconditional or on-demand bonds are bonds where the bondsman is required to pay simply on demand by the beneficiary without proof of default on the part of the account party or regard to the existence of any disputes in the underlying contract between the beneficiary and the account party. Whether a bond is unconditional or conditional is a matter of construction .A good illustration of an

unconditional bond can be found in a recent High Court decision in ***The Ngee Ann Kongsi v The Tai Ping Insurance Company Limited.***[5] In that case, the main contractor procured a performance bond from the Defendant in favour of the Employer. There were substantial delays in the works and the Architect proceeded to certify the delays in completion by the contractor. On 16 October 1997, the Employer made a demand on the bond. The Defendant refused to pay contending that proof of default was required. The Court found that as a matter of construction, the Bond in question was an on-demand bond. Clause 2 of the Bond expressly stated that" the guaranteed sum shall be payable to the Employer immediately upon demand for payment in writing notwithstanding the existence of any dispute between the Employer and the Contractor in relation to the contract or any amount payable thereunder." Being an on-demand bond, the Defendants' liability to pay was triggered by the Plaintiffs' call.

34. Conditional bonds on the other hand require proof of breach of the terms of the contract by the account party as a precondition to the bondsman's liability under the bond. For this reason, conditional bonds are not favoured by employers in the construction industry as they are put to the expense and uncertainty of having to establish default before a call can be made.

35. On-demand bonds have been a fertile source of litigation in Singapore and the question of when the courts would intervene to restrain abusive calls on on-demand bonds has attracted considerable judicial attention in recent years.

Restraint on Calls or Payment on Bonds

36. Judicial approach on this subject has been shaped by a tension between competing principles and countervailing policy considerations. On the one hand, courts profess a need to give effect to the commercial purpose of such bonds. This has found expression in what is known as the "autonomy principle". Conceptually, a bond constitutes a separate and autonomous contract from the underlying contract between the beneficiary and account party. In this sense, they are likened to letters of credit which are widely used in international business transactions. Where the bond is an on-demand bond, there is a separate and autonomous undertaking on the part of the bondsman to honour its payment obligation regardless of disputes in the underlying contract .On the other hand, the courts are equally cognisant of the need to guard against abusive calls. The fraud exception to the autonomy principle was born out of this concern. In ***Edward Owen Engineering Ltd v Barclay Bank International Ltd and Anor,***[6] Lord Denning MR said:

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[5] Suit No. 2033 of 1997
[6] (1978) 1 QB 159

"The performance guarantee stands on a similar footing to a letter of credit. A bank which gives a performance guarantee must honour that guarantee according to its terms. It is not concerned in the least with the relations between the supplier and the customer nor with the question of whether the supplier has performed his contracted obligation or not; nor with the question whether the supplier is in default or not. The bank must pay according to its guarantee, on demand, if so stipulated, without proof or conditions. The only exception is when there is a clear fraud of which the bank has notice."

37. The fraud principle as defined by the English Courts is a narrow one and challenges to calls on demand bonds have been rigorously contained within the strict limits of the fraud exception even in cases where there is no evidence of "a colourable breach of contract by the guaranteed party or of a bona fide claim by the beneficiary." [7] Not surprisingly, attempts were made by some to try and circumvent the autonomy principle and the narrow fraud exception by seeking injunctive relief not against the bondsman but against the beneficiary. The argument advanced here is that where an injunction is sought against the beneficiary as opposed to the bondsman, the court would not be interfering with the sacrosanct nature of the bondsman's obligations under the bond but would be at liberty to examine the underlying contract between the parties. In ***Potton Homes v Coleman Contractors (Overseas),***[8] Eveleigh LJ gave the following illustration:

"For a large construction project the employer may agree to provide finance(perhaps by way of advance payments) to enable the contractor to undertake the works. The contractor will almost certainly be asked to provide a performance bond. If the contractor were unable to perform because the employer failed to provide the finance, it would seem wrong to me if the court was not entitled to have regard to the terms of the underlying contract and could be prevented from considering the question whether or not to restrain the employer by the mere assertion that a performance bond is like a letter of credit..... The facts of each case must be considered. If the contract is avoided or if there is total failure of consideration between the buyer and the seller for which the seller undertook to procure the issue of the performance bond, I do not see why as between the seller and the buyer , the seller should not be unable to prevent a call upon the bond by the mere assertion that the bond is to be treated as cash."

38. These sentiments were echoed in ***Royal Design Studio Pte Ltd v Chang Development Pte Ltd***[9] by Thean J (as he then was) when he said:

[7] see para 17.070Hudson's"Building and Engineering Contracts" (11th Edition)
[8] (1984) 28 BLR 19
[9] (1990) SLR 1116

"We are not concerned with the irrevocable nature of the obligation assumed by the relevant bank; we are concerned with the relationship between the parties under the main or underlying contract they made and the dispute arising from such relationship. In the present case, the plaintiff is not restraining the insurance company from paying on the bond and therefore the question of the insurance company not being able to honour its obligations does not arise. The dispute is only between the plaintiffs and the defendant and relates solely to the main or underlying contract made between them. In such case, I do not see why the court should be inhibited from exercising its equitable jurisdiction and restraining the defendant from calling on the bond, if the facts warrant it, merely because the bond is like a letter of credit."

Current position

39. The law on the enforcement of bonds in Singapore has now been settled by the Court of Appeal in the landmark case of ***Bocotra Construction Pte Ltd v Attorney General (No 2).***[10] In that case, the appellants were appointed as contractors by the Director-General of the Public Works for the construction of Phase II of the Central Expressway. The appellants were required to furnish a bank guarantee as security for their due performance of the works. Disputes subsequently arose between the parties over delays in the works and defects and arbitration proceedings were commenced. The Respondents made a call on the performance bond.

40. After undertaking a comprehensive review of the relevant case law in this area, the Court of Appeal, following its earlier decision in ***Brody, White & Co Inc v Chemet Handel Trading (S) Pte Ltd***[11] dispelled any misconception that different principles should apply when dealing with restraints on banks and those dealing with restraint of callers from calling for payment. The following passage taken from the judgment delivered by Lai J in Brody was quoted with approval:

"It was irrelevant that the injunction in the present case was one which prevented the appellants from encashing the letter of credit rather than one which restrained the bank from honouring the credit. The consequence would have been the same; the documentary credit contract between the bank and the appellants, which should be independent of the underlying contract between the appellants and the respondents, was in effect being frozen by the injunction obtained by the appellants."

[10] (1995) 2 SLR 733
[11] (1993) 1 SLR 65

41. The Court of Appeal went on to clarify the circumstances under which calls on demand bonds would be restrained. Karthigesu JA delivering the judgment of the Court said:

> *"In our opinion, whether there is fraud or unconscionability is the sole consideration in applications for injunctions restraining payment or calls on bonds to be granted. Once this is established, there is no necessity to expend energies in addressing the superfluous question of 'balance of convenience'. It does not lie in the mouth of the defendant to claim that damages would still somehow be an adequate remedy."*

Fraud Exception

42. What does "fraud" in the context of performance bonds mean? The learned author in Hudson's "Building and Engineering Contracts"[12] had this to say:

> *"The English Courts have repeatedly stated, however, that as a general exception to this will be where there is fraud. Apparently, fraud for this purpose will be on the part of the beneficiary who knows that there is no right to payment but expressly or impliedly represents his claim to be valid, provided that this is known to the issuing bank at the time of paying or passing on the demand although later knowledge, if the bond has not yet been paid, will probably also suffice. The so-called "fraud exception" will also apparently apply where the beneficiary claims payment in good faith but the bank is aware of an invalidity."*

43. Much of the case-law on the subject of fraud was developed in the context of letters of credit. Where letters of credit are concerned, fraud is confined to the documents presented for payment to the bank by the beneficiary. In ***Brody, White & Co Inc v Chemet Hendel Trading(s) Pte Ltd,***[13] an injunction was sought to restrain the beneficiary of a letter of credit from receiving payment. In refusing the injunction, the Court of Appeal said:

> *"It appeared to us that the kind of fraud sufficient to constitute an exception to the autonomy of an irrevocable credit is fraud in the presentation of the required documents to the bank ie where the beneficiary, for the purpose of drawing on the credit, fraudulently presents to the bank documents that contain material representations of fact that to his knowledge are untrue: United City Merchants(Investments) Ltd v Royal Bank of Canada. It would seem that fraud as perpetrated by the seller on the buyer in respect of the underlying contract of sale between them would not affect the contract of documentary credit between the seller and the issuing/confirming bank.....*

[12] para 17.067 (11th Edition)
[13] (1993) 1 SLR 65

> *What fraud existed(if any) would have been a matter as between the appellants and the respondents, concerning the agreement between them. In the absence of evidence that there existed in the documents presented by the appellants fraudulent misrepresentations which the bank was aware of, we concluded that the respondents should not be allowed an injunction to freeze the credit contract between the Bank of America and the appellants."*

44. It would not be appropriate to import the same conception of fraud developed in letters of credit to performance bonds. Where performance bonds are concerned, there is limited scope for "documentary fraud". The bondsman is rarely concerned with representations in documents presented by the beneficiary. He acts on the demand which is made by the beneficiary and is merely concerned to ensure that the call has been made in compliance with the bond. In Hudson's "Building and Engineering Contracts"[14], the learned author has sought to expose the fallacy in analogy between letters of credit and performance bonds used in construction projects as follows:

> *"Moreover, while the English cases contain many judicial references to the importance of safeguarding the status of letters of credit and of the reputation of issuing or confirming banks in honouring such documents, it is difficult to see any real analogy between letters of credit and unconditional contractors' performance bonds in construction projects, nor how the reputation of a bank can suffer if prevented by an order of the Court from making a payment in a case where the bond obligation itself is, however nominally or cosmetically, expressed to secure due performance and to arise on contractor default....The position remains that there are few if any reported cases in England or the Commonwealth where enforcement of an unconditional performance bond in a construction contract has been prevented on the ground of "the fraud exception" despite the frequently expressed acknowledgment of the principle of such an exception by the courts."*

Unconscionability

45. The Singapore Courts have made a conscious departure from the English position and have refused to allow their equitable jurisdiction to be fettered by the fraud exception. However, even after ***Bocotra,*** there was still some uncertainty as to whether the Court of Appeal in that case had intended unconscionability as a separate limb or whether it was used interchangeably with fraud. There were conflicting High Court decisions on this point. In ***Sin Kian Contractor Pte Ltd v Lian Kok Hong & Anor,***[15] Lim Teong Qwee JC took the view that the two concepts were separate and that the Court of Appeal in ***Bocotra*** did not use the term "fraud" and "unconscionability" interchangeably. However, in an earlier

[14] para 17.071 (11th Edition)
[15] (1999)3SLR 732

High Court decision ***New Civil build Pte Ltd v Guobena Sdn Bhd & Anor***,[16] the Court had taken a different view. In the ***New Civilbuild*** case, the learned judge , in discharging the injunction, considered that fraud was the only ground for injunctive relief, that unconscionability alone would not suffice and that the term "unconscionability" was used interchangeably with the concept of fraud by the Court of Appeal in ***Bocotra***. Fortunately, the debate as to whether unconscionability constitutes a separate ground for relief has now been laid to rest in a recent pronouncement of the ***Court of Appeal in GHL Pte Ltd v Unitrack Building Construction Pte Ltd***.[17]

46. In the ***GHL*** case, GHL Pte Ltd ("GHL") were the owners and developers of a property at Lorong 17 Geylang, Singapore In April 1997, they engaged Unitrack Building Construction Pte Ltd ('Unitrack'), to be the main contractors for their project. The contract sum for the project was $5,781,4000, which included a sum of $3,820,000 for sub-contracts works. It was contemplated that in respect of the latter, sub-contracts would be entered into between Unitrack and sub-contractors nominated by GHL. Under the contract, Unitrack were obliged to furnish a performance bond for an amount equal to 10% of the contract sum. Pursuant to the contract, on or about 26 June 1997, AGF Insurance (Singapore) Pte Ltd ('AGF')' at Unitrack's request issued a performance bond in the amount of $578,140 in favour of GHL. This was kept by Unitrack at all material times and was not handed to GHL. On 30 April 1998, Unitrack and GHL executed a written variation of the main contract. They agreed that the sub-contractors of the project would receive payment directly from GHL, and that the contract sum would be revised downwards to $1,961,400. At that point in time no sub-contracts had as yet been made between Unitrack and the sub-contractors which had been nominated by GHL. Thereafter, GHL dealt direct with sub-contractors for the project. A dispute subsequently arose and GHL on 6 October 1998 purported to call on the performance bond for the total sum of $578,140. On 23 October 1998, Unitrack commenced an action against AGF and GHL claiming, inter alia, an injunction restraining GHL from seeking or claiming payment from AGF on the performance bond on the basis that in light of the revision of the contract sum, such action would be unconscionable on the part of GHL. On 13 January 1999, Unitrack applied for an interim injunction to the same effect. The interim injunction was granted by Lim Teong Qwee JC and subsequently confirmed by Rubin J at a special hearing . The appellants appealed. In dismissing the appeal, the Court of Appeal held that unconscionability was a separate ground apart from fraud for restraining a beneficiary of a performance bond from enforcing it. The Court of Appeal also found on the facts of the case that GHL's call on the performance bond was unconscionable. In particular, they considered the fact that there was a drastic revision of the contract sum downwards by about 65% and that after revision the sub-contracts works were

[16] (1999) 1 SLR 374
[17] (1999) 4 SLR 604

taken out of the contract and GHL entered into direct contracts with the sub-contractors. In consequence, there were no sub-contracts entered into between Unitrack and the sub-contractors, and Unitrack did not have the benefit of similar performance bonds from them to back up their performance bond to the extent as originally contemplated. As a result of the revision in the contract sum, Unitrack's commitment was considerably reduced. Under the main contract, GHL was only entitled to a performance bond of an amount equal to 10% of the contract sum, and 10% of the contract sum as revised was only $196,140. By calling on the performance bond for the full amount of $578,140 GHL was effectively seeking to obtain a sum which represented about 30% of the revised contract sum.

47. In his judgment, L P Thean JA had this to say:

"We agree that performance bonds are used frequently in the construction industry; that they are provided by and to parties who deal at arm's length; that the use of performance bonds has resulted in substantial benefits to the parties and also in savings; that the courts should give effect to the intention of the parties; and that the law in relation to performance bonds should be placed on 'a clear and unambiguous footing' so that they could be accepted by parties whether in Singapore or abroad. But, with respect, these are not the points involved with which we are concerned. We are concerned with abusive calls on the performance bonds. It should not be forgotten that a performance bond can operate as an oppressive instrument, and in the event that a beneficiary calls on the bond in circumstances, where there is prima facie evidence of fraud or unconscionability, the court should step in to intervene at the interlocutory stage until the whole of the circumstances of the case has been investigated. It should also not be forgotten that a performance bond is basically a security for the performance of the main contract, and as such we see no reason, in principle, why it should be so sacrosanct and inviolate as not to be subject to the court's intervention except on the ground of fraud. We agree that a beneficiary under a performance bond should be protected as to the integrity of the security he has in case of non-performance by the party on whose account the performance bond was issued, but a temporary restraining order does not prejudice or adversely affect the security; it merely postpones the realisation of the security until the party concerned is given an opportunity to prove his case (per Chan Sek Keong J in Chartered Electronic at p 31 of the transcript)."

48. By widening the door to embrace the concept of unconscionability, the Courts are now free to consider all the circumstances of the case including the underlying contract between the parties in deciding whether to exercise its equitable jurisdiction. What then constitutes unconscionability? In explaining this concept, the Court of Appeal in ***GHL*** referred to an earlier unreported decision of

Raymond Construction Pte Ltd v Low Yang Tong and AGF Insurance (Singapore) Pte Ltd[18] where Lai J explained unconscionability as follows:

"The concept of unconscionability to me involves unfairness, as distinct from dishonesty or fraud, or conduct of a kind so reprehensible or lacking in good faith that a court of conscience would either restraint the party or refuse to assist the party. Mere breaches of contract by the party in question would not by themselves be unconscionable... In my view, ***Royal Design Studio*** *and* ***Kvaerner Singapore*** *are illustrations of the circumstances where payments would have been unconscionable."*

49. In ***Raymond Construction***, the contractors had undertaken to construct a double storey detached house for the owner. Pursuant to the main contract, the contractors provided a performance guarantee by an insurance company. Subsequently, disputes between the parties arose. The owner complained of defective work whilst the contractors alleged that there had been wrongful refusal or delay by the owners in making payments of certified sums due. The owner called on the bond and the contractors obtained an interim injunction restraint against the insurance company from making payment and the owner from receiving payment. The owner sought to discharge the injunction. The owner's application for discharge of the injunction was dismissed by Lai J.

50. On the facts before him, the learned Judge found that it was unconscionable for the owner to have called on the bond and made the following observations:

"Having considered all the evidence, I was driven to the conclusion that evidence was strongly suggestive that the conduct of the first defendant from first to last was most unfair and it was against the court's conscience to have allowed him to insist on his pound of flesh. Plainly he could not be allowed to get at the money and add insult to injury until trial. There was strong evidence that he would postpone meeting his financial commitments by tactics of all sorts.The way he drew his cheques and the delays in his payments were legendary and habitual, if one took into account the fact that he has the unusual hallmark of being the subject of bankruptcy notices and suits for defaults in meeting his commitments."

51. The learned Judge referred to two earlier decisions of the Singapore High Court in ***Royal Design Studio Pte Ltd v Chang Development Pte Ltd*** [19]and ***Kvaerner Singapore Pte Ltd v UDL Shipbuilding(Singapore) Pte Ltd.***[20] as illustrations of unconscionability. At this juncture, it would be useful to consider the facts in these two cases.

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[18] Suit No. 1715 of 1995
[19] (1990) SLR 1116
[20] (1993)3 SLR 350

Royal Design case

52. The Plaintiffs in this case had contracted to build nine units of terrace houses. Under the contract, the Plaintiffs were required to complete construction of the houses within 14 months and to obtain the temporary occupation licence within 17 months of the date of permit to commence construction works. The Plaintiffs furnished a performance bond to the Defendants. During the course of the project, disputes arose between the parties. The Plaintiffs alleged that the Defendants had delayed their interim payments which in turn severely affected their cash-flow. On the other hand, the Defendants complained that the Plaintiffs had been in delay. The Defendants terminated the contract and sought, inter alia, to call on the performance bond. The Plaintiffs obtained an ex parte injunction restraining the Defendants from calling on the bond.

53. The matter came before Thean J (as he then was). In refusing to discharge the injunction on the bond, the learned Judge said:

"In innumerable cases, courts have, in appropriate circumstances, in exercise of their equitable jurisdiction granted interim injunctions restraining parties from enforcing their contractual provisions until the resolution of their disputes then pending...In this case, the defendant is only entitled to call on the bond in the event of breach of contract by the plaintiff. The defendant alleged that the plaintiff was in breach of contract but that allegation is hotly contested; the plaintiff said that I was not in breach and that it was the defendant who was in breach. Obviously, this issue can only be resolved at the trial or arbitration, depending on which forum the parties choose to conduct their litigation. Until that issue is decided in favour of the defendant, it cannot be said that at the moment the defendant is entitled under the agreement to call on the bond."

54. The learned judge considered that the Defendants had large sums and other security in their hands and assuming that damage was suffered by them, they had adequate funds to cover these losses. Consequently, it was inequitable for the Defendants to call on the bond.

Kvaerner Singapore

55. The Plaintiffs sold to the Defendants some equipment for the sum of $1 m. Under the contract, the Defendants were to make part payment of 30% of the purchase price and to pay the balance by way of irrevocable letter of credit. Also, the Plaintiffs were to deliver to the Defendants a performance bond. The Defendants made the payment and the Plaintiffs procured the issuance of the performance bond. Subsequently, the Defendants defaulted in opening the letter of credit for the payment of the balance despite repeated reminders from the Plaintiffs. Instead, the Defendants demanded payment under the performance bond. Selvam J, in granting an interim injunction to restrain a call on the bond, had this to say:

"The defendants invoked the principle in Edward Owen Engineering Ltd v Barclays Bank International Ltd that except in cases of established fraud known to the issuer of the performance guarantee he cannot be restrained from making payment on the ground that the party to the underlying contract disputes liability. Later cases show that it is not an immutable principle of universal application. And in my view it has no application where the injunction is sought against a party to the underlying contract who seeks to take advantage of the performance guarantee where by his own volition he fails to perform a condition precedent in the sense I have described.

Furthermore, a demand under the performance guarantee can be made only when 'the seller has failed or refused to fulfill his obligations under the contract'. The seller's failure or refusal is a condition precedent to the buyer making a demand. An assertion to that effect is implied in a demand made by the buyer. In circumstances where it can be said that the buyer had no honest belief that the seller has failed or refused to perform his obligation, a demand by the Defendants/buyers in my view is a dishonest act which would justify a restraint order. On the facts of the case a demand made by the buyer was utterly lacking in bona fides."

56. The recent local cases sweeping the legal position in respect performance bonds are as follows:

- ***Anwar Siraj and another v Teo Hee Lai Building Construction Pte Ltd*** *[2003] 1 SLR 394*
- ***Seng Hock Heng Contractor Pte Ltd v Hup Seng Bee Construction Pte Ltd & Anor*** *[2002] 4 SLR 612*

57. In the case of ***Anwar Siraj***, the Court of Appeal held that the Owner/Employer was entitled to call on the performance bond, thus setting aside the decision below.

58. The Court of Appeal held that the grounds relied on by the building contractor were insufficient to make out a case of unconscionability and/or that the arguments raised did not establish that the Owner/Employer acted unconscionably by calling on the performance bond.

59. The 3 grounds relied on by the building contractor were as follows:

- The Owner/Employer already had sufficient security for their claims;
- The Owner/Employer's complaints over defects in the construction were the result of defective design by the architect; and

- The Owner/Employer had denied the building contractor access into the premises to carry out rectification work.

60. The Court of Appeal found that in respect of the first ground it was not the court's task to determine whose cost estimate was more realistic. In respect of second ground relied on by the building contractor, the Court of Appeal held that the court was in no position to conclude that there had been defective designing by the architect. Lastly, the Court of Appeal was unable to conclude from the voluminous correspondence between parties on this matter that the Owner/Employer was clearly at fault and guilty or unconscionable conduct. The Court of Appeal finally concluded by finding that *"the court should guard against unnecessarily interfering with contractual arrangements freely entered into by the parties"*.

61. In ***Seng Hock Heng***, the learned Choo Han Teck JC held that the onus lay on the plaintiff to prove that by reason of fraud or unconscionable conduct an injunction ought to issue against the first defendant. It was unnecessary nor reasonably possible for the court to embark on an evaluation of the evidence to see whether the costs claimed by the first defendant were correctly and legitimately incurred.

Standard of proof required

62. In ***Bocotra***, the Court of Appeal made it clear that to warrant injunctive relief, fraud or unconscionability must be clearly established. A warning was issued on the following terms:

"To allay these concerns, we need only note that dispensing with consideration of the balance of convenience test does not make an injunction any easier to obtain. Indeed, a higher degree of strictness applies, as the applicant will be required to establish a clear case of fraud or unconscionability in interlocutory proceedings. It is clear that mere allegations are insufficient."

63. Since ***Bocotra***, there have been numerous attempts by parties to restrain perceived abusive calls on bonds. We will now examine some of these attempts.

64. In ***San International Pte Ltd v Keppel Engineering Pte Ltd***,[21] San International sought an interim injunction to restrain Keppel Engineering from receiving a sum of $1,255,520.56 being the balance of a guaranteed sum under a performance bond.

65. Briefly, the facts in this case were these. The Defendants, Keppel Engineering Pte Ltd were the Main Contractor for a warehouse project. The Plaintiffs was one

[21] Suit No. 411 of 1996

of the sub-contractors. Under the terms of the sub-contract, the Plaintiffs had to procure a performance bond for 10% of the contract sum. Disputes during the Project subsequently surfaced between the parties and the Plaintiffs' sub-contract was terminated. The Defendants then made a call on the performance bond. One of the grounds on which the Defendants sought to restrain the call was that the Defendants had acted unconscionably.

66. The Plaintiffs argued that in determining whether the call was unconscionable, the Court was entitled to look at the state of accounts between the parties as at the date of call and to consider whether the monies retained by the beneficiary were adequate to cover its potential losses without the need for the monies realised from the bond. The Plaintiffs sought to adduce evidence that the Defendants held some $3,114,000 belonging to the Plaintiffs comprising certified and uncertified sums of work done as well as retention monies which the Defendants must give credit for before demanding payment under the Bonds.

67. At first instance, the interim injunction was refused by the Honourable Judicial Commissioner Chelva Rajah. Applying the ***Bocotra*** test, Chelva Rajah JC held that clear evidence was required. On the basis of the material before him, whilst the Plaintiffs were entitled to require the Defendants to set-off certified sums due to them, the other amounts in their hands were at best uncertified claims which have yet to be substantiated and established. It was also not possible on the untested affidavit evidence before him to find that the Defendants' claim for $1,255,520.56 was lacking in bona fides. The Plaintiffs' appeal against the decision of Chelva Rajah was dismissed by the Court of Appeal.

68. Another instructive case is ***Four Seas Construction Co Pte Ltd v The Tai Ping Insurance Company.***[22] The Plaintiffs there had contracted with YHS to build a factory and office building. Due to their financial problems, YHS agreed to advance monies to the Plaintiffs to pay their domestic subcontractor. The total amount of loans made by YHS amounted to $5,977,925.26 whilst direct payments made by YHS to the subcontractors totalled $9.7 million. On 9 December 1997, YHS made a demand on the performance bond issued by Tai Ping Insurance company for the sum of $3.2 million to cover the loans made by YHS to the Plaintiff. The Plaintiffs applied for and obtained an interim injunction restraining payment out on the bond. The plaintiffs alleged that the demand made on the bond was dishonest as YHS knew that it was not made in respect of a matter concerning the underlying contract but was made with regards to the loan agreement. The Plaintiffs also complained that their works were grossly undercertified. The interim injunction was set aside by Tay Yong Kwang JC. His Honour found that the on the affidavit evidence before him, there was at best a commercial dispute between the parties. The allegations concerning under-valuation and under-certification were nothing extraordinary. Unless Plaintiffs

[22] Suit No. 2118 of 1997

could demonstrate that YHS' assessment was so absurd or their documents in support were concocted or so irrationally done that no reasonable person could honestly believe them, the Plaintiffs were not even at the starting gates of establishing a prima facie case of fraud or unconscionability. The Plaintiffs were chastised for unjustifiably elevating their differences with YHS to the level of fraud or unconscionability.

69. Yet another failed attempt at halting a call on a demand bond occurred in ***Sin Kian Contractor Pte Ltd v Lian Kok Hong & Anor.***[23]The Plaintiff had agreed to construct a two storey detached house for the owner . Pursuant to the building contract, the Plaintiff duly furnished a performance bond in favour of the Employer. Prior to completion of the works, the Employer wrote on 15 Mar 99 to the guarantor to demand payment under the bond. The architect also issued and duly served on the Plaintiff a termination certificate on 17 Mar 1999. The Employer then terminated the Plaintiff's employment on 19 March 1999. The Plaintiff applied for an injunction to restrain payment on the bond on the grounds that the Employer had acted unconscionably in demanding payment. In refusing the Plaintiff's application, the court found that the contractor had fallen short of establishing unconscionability. During the course of the project, the architect had issued various notices and directions to the Plaintiff to rectify the defects in the works. Despite these notices and directions, the Plaintiff did not comply thereby prompting the architect to issue the termination certificate. Further, on 15 March 1999, just prior to termination of the contractor's employment, the architect had issued a certificate for progress claim 17 certifying a sum of $143,256.72 payable to the employer. Even after allowing for the retention sum of $138,500, there would still be a shortfall. As the works were not completed , the employer may well have a claim for damages.

Eltraco International Pte Ltd v CGH Development Pte Ltd[24]

70. The ***Eltraco*** case is the most recent pronouncement by the Court of Appeal on this subject of unconscionability. Eltraco was engaged as the main contractor for a development project .The main contract incorporated the SIA Form of Contract. The project was completed in August 1998. As at completion, the employer had retained $609,700 in retention monies. The main contractor had also submitted a progress claim no 32 for $1,605,574.43 for work done up to completion. This sum included an amount of $200,000 being variations works, which had been assessed and agreed with the quantity surveyor. The main contractor's progress claim was not certified by the architect ostensibly because of a number of unrectified defects. Towards the maintenance period, the Architect had delivered a schedule of defects to the main contractor. The main contractor attended to some of the defects and thereafter embarked on

[23] (1999) 3 SLR 732
[24] [2000] 4SLR 290

discussions with the consultants and the employer to offer monetary compensation for some items of defective work. Whilst negotiations were still afoot, the employer through their lawyers made a call on the performance bond provided by the main contractor. The bond was for $2,438,800 and the employers made a full call on the bond. The main contractor applied for an injunction to restrain payment out on the bond. At first instance, the High Court granted an injunction restraining the employer from receiving more than $1,600,000. The High Court in granting an injunction for a smaller sum took into account the fact that the employer had retention monies of $609,700 and the agreed variations amounting to $200,000 which had not been certified or paid to the main contractor. The main contractor appealed to the Court of Appeal. On appeal, the Court of Appeal held that the High Court should also have taken into account the main contractor's uncertified progress claim in considering the issue of unconscionability. Bearing in mind that the works were already completed and that the only reason for withholding certification was the unremedied defects, the Court found that there should be a further reduction of $1m from the sum which the court below had directed that the employers should be allowed to call.In the Court's view, this should give the employers ample security without being that inordinate as to be unconscionable.

71. The ***Eltraco*** case is significant in several respects. Firstly, the Court took the opportunity to clarify the meaning of unconscionability as expounded by Lai J in the ***Raymond Construction*** case. Whilst unconscionability necessarily entails unfairness, it does not follow that in every instance where there is unfairness, there would be unconscionability. Unfairness is only one factor in the consideration. Secondly, the Court recognised that in the exercise of its equitable jurisdiction when granting an injunction, it can limit the restraint to only that part which was clearly excessive and allow the other part which would not be unconscionable to remain .It is submitted however that such partial restraints are feasible only where the bond permits calls from time to time and for such sums as may be appropriate subject to a maximum.

Judicial Vigilance or Statutory Reform?

72. In ***Tins Industrial Co Ltd v Kono Insurance Ltd,***[25] Hunter JA said that a bond "can be an oppressive document". These remarks are particularly apposite in the construction industry which is notorious for its adversarial attitudes. When disputes arise between the contractor and employer or between the main contractor and sub-contractors, there is always a risk that the beneficiary may resort to specious and unjustified claims for payment under the bond. Indeed, calls or threatened calls on the bond are often used by employers or main contractors to great effect as a tactical weapon to advance their bargaining position in disputes. The consequences for the contractor or sub-contractor as the

[25] (1998) 2 HKLR 36

case may be in such circumstances can be disastrous. Once the bank or insurance company pays out on the bond, it would invariably exercise its rights under a counter-indemnity against the contractor and/or its directors. To a contractor who is already beset by cash-flow problems, a call on the bond may well prove to be the final nail on the coffin.

73. The concern with abusive calls has led some quarters to demand for an outright ban on the use of on-demand bonds in the construction industry. In his Report "Constructing the team", Sir Michael Latham recommended that bonds should not be on-demand or unconditional but should have clearly defined circumstances set out in them for being called. In "Construction Contracts: Law and management," its authors, John Murdoch and Will Hughes noted that" the use of these bonds in construction contracts is on the whole undesirable since, while the employer may not intend to call on such bonds irresponsibly, the contractor cannot rely on this; the contractor must therefore increase the tender price to cover the cost of something which is not really necessary."[26]

74. These calls for the abolition of on-demand bonds are perhaps more applicable in the UK context where the English Courts have shown a marked reluctance to venture beyond the fraud exception. Thankfully, our judiciary has taken a more robust approach in the enforcement of bonds and judicial vigilance can be counted on to check abuse by the unscrupulous. By insisting on strict standards of proof whilst preserving the latitude to intervene where there is fraud or unconscionability, our courts are to be commended for preserving the commercial efficacy of such instruments without detracting from their fundamental duty to do justice in deserving cases.[27]

D. LIABILITY FOR DEFECTS IN THE LIGHT OF SETRON V CHUANG U MING

Duties During Construction Stage

75. The architect is expected as part of his engagement to supervise the construction works to ensure that they are being carried out in accordance with the contract requirements. In the absence of any express contractual provision, such a duty would be implied in law[28]. The level of supervision required depends on the terms of the engagement between the employer and the architect.

[26] see also para 17.076 Hudson's "Building and Engineering Contracts"(11th Edition)
[27] This paper is a modified version of an earlier paper entitled "Performance bonds: use and abuse in the construction industry" presented by the author in the 1st Butterworths Annual Construction Law Review
[28] *See Brodie v Cardiff Corp (1919) AC 337.*

76. Where the SIA Conditions of Appointment (1996 Ed) are adopted, clauses 1.1(7) and 1.1(8) set out the architect's duties of supervision and inspection. Clause 1.1(7) requires the architect to inspect the works at such periodic intervals as the architect deems necessary to ensure that the works are being carried out in accordance with the building contract and to enable the architect to certify in accordance with statutory requirements. The clause makes it clear that constant or daily inspection will not form part of the basic services of the architect.

77. These clauses received judicial consideration in ***Chuang Uming Pte Ltd v Setron***[29]. In that case, the Court of Appeal made the following observation:-

> "*... under these provisions, there was a duty to inspect and supervise the works carried out by the contractors not constantly or daily but certainly periodically from time to time. How frequent or regular should such inspections and supervision be must of course be left to good sense of architects and must depend on the nature of the work for the time being carried out by the contractors. Where the construction works were important or critical, obviously closer and more frequent inspection and supervision was necessary and in other areas of work which were not that important or critical less frequent inspect and supervision was called for.*"

78. The approach taken by the Court of Appeal in the ***Setron*** case accords with the approach taken in an earlier English case ***Alexander Corfield v David Grant***[30] where the court noted that adequacy of supervision is not tested by the number of physical hours spent on site but whether the attention given is sufficient or adequate having regards to the nature of the job being supervised.

79. In the absence of any express provision defining the standard of supervision required, the architect would be under a general duty to give the building works reasonable supervision. Reasonable supervision has been defined as such supervision as would enable the architect to give an honest certificate that the work had been executed according to the contract[31]. What constitutes reasonable supervision will depend on the requirements and nature of each project.

80. The architect is not expected to examine every detail on site and his failure to discover a defect which is not detectable by reasonable examination is not necessarily negligent[32]. The court will have regard to the following factors in determining that constitutes reasonable supervision in each case:

[29] *[2000] 1 SLR 166.*
[30] *(1992) 59 BLR 102.*
[31] *Jameson v Simon (1899) 1 F (Ct of Sess) 1211.*
[32] *East Ham Corp v Bernard Sunley & Sons Ltd (1966) AC 406.*

(1) In ***Cotton v Wallis***[33], the Court of Appeal seemed to suggest that an architect might be justified in accepting lower standards of work where the contract price was low. However, the architect should not infer or presume lower standards of specifications from the price unless such standards are expressly stated. It is also borne in mind that regardless of the architect's own remuneration or the size of the contract value, the law would expect a minimum level of supervision from the architect.

(2) The frequency of supervision will depend on the criticality of the works in question. In ***Dabous v Zuliani***[34], the court made the following observation in the context of a critical part of the works:-

> "*The proper installation of this type of chimney was critical to the safety of the dwelling ... the failure of the defendant architects to ensure that the chimney leading from the fire place was properly installed, even if this required the removal of some of the concealing gyprock, was a failure to meet the reasonable standard of care which they owed to the plaintiff.*"

(3) The terms of the engagement can prescribe standards of supervision. The architect will have to meet the standards set in the contract.

(4) The architect is under a duty to inform the quantity surveyor of the contractor's defective work so as to enable the quantity surveyor to exclude it during valuation[35].

(5) The architect is not expected to be at the site all the time. In the ***Eastern Lagoon*** case, the High Court noted that the architect can discharge his responsibility of supervision if he supervises the construction of a sample and then instructs his Clerk-of-Works to ensure that the rest of the works comply with the mock-up or sample.

(6) The architect is generally under no duty to direct or instruct the contractor on the manner of performance of his work. However, if he observes that the contractor is failing to take special precautions which would be necessary to reduce risks of injury or damage to property, the architect should warn the contractor of the consequences[36].

81. In ***Sim & Associates v Tan Alfred***[37], the employer sued his architect for breach of duties in certifying defective works for payment and neglecting to require the

[33] *(1955) 1 WLR 1168.*
[34] *(1976) 68 DLR 3 414.*
[35] *Sutcliffe v Chippendale and Edmondson (1971) 18 BLR 149.*
[36] *Clayton v Woodman and Son (Builders) Ltd (1962) 1 WLR 585.*
[37] *[1994] 3 SLR 169.*

main contractor rectify the defects. The Court of Appeal held that in the absence of any provision in the contract requiring a higher degree of supervision, an architect is merely required to give reasonable supervision.

82. The test of reasonable supervision is to be measured against the standard expected of a reasonably qualified architect. The employer's claim against the architect for negligent supervision failed on the grounds that the evidence of negligent supervision against the architect was inadequate. The court noted that the architect's liability in this respect is not absolute in the sense that he is liable whenever loss results. It must be demonstrated that he has been negligent in that he has failed to exercise the requisite standard of care required for ordinarily skilled architects in the profession.

Delegation to Clerk-of-Works

83. The architect is not expected to be on site full-time and it is acceptable for matters of detailed supervision to be delegated to the Clerk-of-Works[38]. Where the SIA Conditions of Appointment (1996 Ed) are adopted, clause 1.1(8) contemplates that where frequent or constant supervision of the Works is required, a Clerk-of-Works should be employed either directly by the employer or the architect. Where the Clerk-of-Works is to be employed directly by the employer, he shall be nominated or approved by the architect and be under the architect's direction or control. Where the architect appoints the Clerk-of-Works, the employer would nevertheless remain responsible for the remuneration of the Clerk-of-Works.

84. It should be pointed out the delegation to the Clerk-of-Works will not absolve the architect from his duty to ensure compliance with design as opposed to matters of detail nor will the architect be able to exonerate himself from liability in relying on a Clerk-of-Works know to be unreliable[39].

85. In ***Chuang Uming Pte Ltd v Setron Ltd And Anor***[40], one of the issues which arose was the extent to which the architect could deflect responsibility for supervision to the Clerk-of-Works. It was contended on behalf of the architect in that case that the on-site supervision was entrusted to the Clerk-of-Works who was employed directly by the employer and for whom the employer was vicariously responsible.

[38] *Eastern Lagoon case (supra); Old School v Gleeson (Construction) Ltd (1976) 4 BLR 103.*
[39] *See Saunders & Collard v Broadstairs Local Board (1890) 2 Hudson's BC (4th Edition 1914) 419.*
[40] *[2000] 1 SLR 166.*

86. In rejecting the contention that the architect's duty of supervision to the employer was negatived by the presence of the Clerk-of-Works, the Court of Appeal found that notwithstanding the fact that the Clerk-of-Works was employed by the employer, his appointment was approved or must have been approved by the architect.

87. In the performance of his duties, the Clerk-of-Works had remained under the control and direction of the architect and was his 'ears and eyes' in respect of the day-to-day on site supervision of the construction works. The Court of Appeal also noted that the Clerk-of-Works reported directly to the architect as opposed to the employer and was duty bound to inform the architect of any defects or shortcomings in the works.

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