

THE REPUBLIC OF UGANDA
IN THE HIGH COURT OF UGANDA SITTING AT KAMPALA
(COMMERCIAL DIVISION)
MISCELLANEOUS CAUSE No. 0083 OF 2021

5 **ROKO CONSTRUCTION LIMITED** **APPLICANT**

VERSUS

1. PEARL JUBILEE ESTATES LIMITED }
2. JUBILEE INSURANCE CO. OF UGANDA LIMITED }..... **RESPONDENTS**

10 **Before: Hon Justice Stephen Mubiru.**

RULING

a. Background.

On or about 1st April, 2019 the applicant signed a contract with the 1st respondent by which the
15 applicant undertook to execute the design and construction of “Bella Vista Villas” comprising
240 apartments for a sum of US \$ 8,498,797 with a scheduled completion date of 30th September
2021. Subsequently, on 1st August 2021, the contract was varied, increasing the applicant’s scope
of work with an additional 120 Units for US \$ 3,828,645.49 with the completion date revised to
18th December 2021. The total contract price for the works (360 Units) inclusive of the revised
20 scope stood at US \$ 12,327,342.48 inclusive of VAT. The applicant was obliged to and duly
obtained both an advance payment guarantee No. P/210/7001/2019/000009 in the sun of US \$
569,595.04 and a performance guarantee No. P/210/7001/2019/000012 in the sun of US \$
1,232,732.48.

25 The 1st respondent then made an advance payment of US \$ 849,869.70 equivalent of 10% of the
original contract price. The said advance payment was recoverable on a *pro rata* basis from the
interim payment certificates raised by the applicant. The 1st respondent subsequently was
dissatisfied with the applicant’s execution of the works and thus terminated the contract on 20th
April 2021 with the works carried out at that time valued at 23% of the total works. The
30 termination letter spelt out the grounds of termination. By the date of termination of the contract,
the 1st respondent had paid US \$ 1,824,533 to the applicant. On its part the applicant attributed

the case of the delayed execution to the fact that the 1st respondent had not paid the certificates on time as and when they fell dues, and had not paid the last two at all.

Both parties subsequently entered into a Mutual Release and Settlement Agreement dated 5th May, 2021 where they agreed, *inter alia*, to jointly conduct an audit of the works carried out by the applicant as well as the goods and materials on site to determine the amount owed to the applicant. The final accounts showed that instead it was the applicant who owed the 1st respondent a sum of US \$ 929,084. The parties then agreed upon the following mode of recovery of that amount; - i) the amount was to be paid in twelve (12) equal monthly instalments from 30th June 2021 until payment in full; in the event that the payments were not made for three (3) consecutive months, the 1st respondent would be entitled to recover the amounts owing from any money payable to the applicant from M/s Cascadia Development (their sister Company in Kenya); in the event of failure of all the above, Pearl Marina would be entitled to recall the Advance Payment Guarantee and the Performance Security

It had been agreed between the parties that any disputes between the parties arising in performance of the contract were to be referred to arbitration. When these differences arose between them, they duly appointed an arbitrator, referred the dispute to him and arbitration proceedings are already afoot. In the meantime, the 1st respondent made a call on the two guarantees.

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b. The application.

This application is made under the provisions of section 6 of *The Arbitration and Conciliation Act*, section 98 of *The Civil Procedure Act* and Order 52 rules 1 and 2 of *The Civil Procedure Rules*. The applicant seeks an order of an interim measure of protection pending arbitration, by way of an injunction restraining the respondents, their agents, servants, employees, assignees or anyone else claiming or deriving authority from them, from cashing the two guarantees until conclusion of the ongoing arbitration. It is the applicant's case that the terms for encashment of the two guaranties were varied by the Mutual Release and Settlement agreement which conditioned a call thereon on a joint audit by the parties. The call made by the applicants is in violation of that condition since no joint audit has been undertaken. In any event, the advance

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payment guarantee was discharged upon the applicant's partial performance of the contract. The order is necessary in order to maintain the status quo until conclusion of the ongoing arbitration.

c. The affidavit in reply;

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In the 1st respondent's affidavit in reply, it is averred that the rights of the 1st respondent to call on the guarantees were unaffected and reserved by the Mutual Release and Settlement agreement, and were to be made without notice to the applicant. This was a compromise to terminate the contract and was entered into without prejudice to the rights of both parties under
10 the building contract. It was an express term of the agreement that the performance guarantee and advance guarantee were to remain in place and in full force until expiration thereof. The advance payment guarantee expired on 9th December, 2021 after Court had issued an Interim Injunction Order while the performance guarantee is due to expire on 1st April, 2023. The final account arose out of a joint audit that the two parties conducted. The payment schedules were
15 agreed upon arising out of the joint audit but were ignored by the applicant.

d. Submissions of counsel for the applicant.

M/s Newmark Advocates on behalf of the applicant submitted that the terms for encashment of
20 the two guaranties were varied by the Mutual Release and Settlement agreement which conditioned a call thereon on a joint audit by the parties. The call made by the applicants is in violation of that condition since no joint audit has been undertaken. In any event, the advance payment guarantee was discharged upon the applicant's partial performance of the contract. Encashment of the guarantees before conclusion of the arbitration will prejudice the applicant
25 since it will have been denied its right to be heard by pre-empting the issue at the arbitration. The applicant will suffer irreparable injury since the encashment will affect it financially and its business reputation will be dented as well. The 1st respondent seeks to cash the guarantees by concealing the fact that a call thereon is subject to a prior joint audit that is yet to be undertaken, which constitutes fraud. Under the contract, the 1st respondent is only entitled to general
30 damages.

e. Submissions of counsel for the 1st respondent.

M/S Kasirye, Byaruhanga & Co. Advocates and Solicitors on behalf of the 1st respondent submitted that demand guarantees are a special type of contract which cannot be the subject of
5 injunctions the kind sought by the applicant. They are autonomous from the underlying contract and constitute a separate undertaking from the underlying contract. Such a guarantee must be honoured according to its terms unless the guarantor had notice of clear fraud and the applicant and the guarantor (2nd respondent) may not avail itself of contractual defences that the applicant may raise under the Contract. In the circumstances, the 1st respondent is entitled to be paid
10 irrespective of any dispute about the underlying transaction except where the above fraud exception applies.

The status quo sought to be preserved in respect of the performance guarantee has longed changed as the 1st respondent made a demand for payment thereunder on the 4th November, 2021
15 before the applicant obtained the interim order of injunction on 12th November, 2021. The purpose of the said interim order was to allow the court hear the instant main application *inter parties*. The applicant has not challenged the termination of the contract which is the basis of this instant application. It only challenges the encashment of the guarantees which is clearly a delaying tactic by the applicant to restrain the 1st respondent from accessing funds to assist in the
20 completion of the construction project. The applicant has not presented a case with a likelihood of success.

It is well established that the payment of money under a performance guarantee, cannot lead to irreparable damage. This is the general position because the cashing out of a performance
25 security is the whole essence of a performance guarantee and is foreseeable by both parties to the said construction project. An injunction would have the negative effect of reinstating a contract which is already terminated. The 1st respondent stands to suffer loss when the guarantee expires without a call, yet the applicant has defaulted on the contract. On the other hand, even upon expiry of the guarantee, the applicant could claim relief under the arbitration. The balance of
30 convenience is in favour of the 1st respondent.

f. The decision.

According to section 6 of *The Arbitration and Conciliation Act*, a party to an arbitration agreement may apply to the court, before or during arbitral proceedings, for an interim measure of protection, and the court may grant that measure. The jurisdiction exercised by the Court under section 6 of *The Arbitration and Conciliation Act* is ancillary to the process of arbitration. While the subject matter jurisdiction rests with the chosen arbitrator, that of this court is invoked only in aid of, or supplementary to, the process of arbitration for the purpose of: (i) procuring or preserving evidence; (ii) facilitating the proceedings as the justice of the case might require; (iii) restraining the assertion of doubtful rights; (iii) providing for the safety of property either pending arbitration or when it is in the hands of accounting parties or limited owners; (iv) where the efficacy or integrity of the arbitral proceedings is in jeopardy; (v) enforcing awards obtained, and so on. The Court is empowered to grant whatever interim protective measures it deems necessary, including injunctive relief and measures for the protection and conservation of property.

When court is called upon to grant injunctive relief as an interim measure of protection pending arbitral proceedings, the court will generally have regard to the following: (a) the nature and strength of the applicant's case, i.e., whether there is a serious question to be arbitrated, in respect of which the applicant demonstrates a sufficient likelihood of success; (b) whether there is an imminent risk of irreparable loss, by considering whether damages are an adequate remedy to the perceived risk of harm; and (c) the course of action favoured on a balance of convenience, i.e. the course of action that results in the lower risk of injustice if the decision to grant the injunction is incorrect. The purpose of granting an interim protective measure is for preservation of the parties, legal rights pending hearing of the application for the protective measures. The court doesn't determine the legal rights that will be the subject of the arbitration but merely preserves it in its current condition until their respective rights can be established or declared by the arbitrator. If failure to grant the injunction might compromise the applicants' ability to assert their claimed rights, there is a very high likelihood of occasioning a loss that cannot be compensated for with money.

It has been established by the law and the decided cases that, the main purpose for issuance of a temporary injunction order is the preservation of property the subject of arbitration and the maintenance of the *status quo* between the parties pending the disposal of the main proceeding. The conditions for the grant of an interlocutory injunction are now, well settled. First, an applicant must show a *prima facie* case with a probability of success. Secondly, an interlocutory injunction will not normally be granted unless the applicant might otherwise suffer irreparable injury, which would not adequately be compensated by an award of damages. Thirdly, if the court is in doubt, it will decide an application on the balance of convenience (see *E.A. Industries v. Trufoods*, [1972] E.A. 420 *American Cyanamid Co v. Ethicon Limited* [1975] AC 396; *Geilla v. Cassman Brown Co. Ltd* [1973] E.A. 358 and *GAPCO Uganda Limited v. Kaweesa and another H.C. Misc Application No. 259 of 2013*). The conditions that have to be fulfilled before court exercises its discretion to grant an interlocutory injunction have been well laid out as the following: -

1. The applicant has shown a *prima facie* case or a serious question to be arbitrated, with a probability of success.
2. The likelihood of the applicant suffering irreparable damage which would not be adequately compensated by an award of damages.
3. Where in doubt in respect of the above two considerations, then the application will be decided on a balance of convenience

The applicant seeks to restrain payment under a demand performance guarantee. The independence of the demand guarantee from the underlying contract has the effect that, in principle, the guarantor must pay a demand presented in compliance with the terms of the guarantee, irrespective of whether or not the principal has, in fact, committed a breach of the underlying contract with the Beneficiary. Therefore, Courts will very rarely order a guarantor not to pay a beneficiary who has made an apparently complying demand. However, in order to preserve the autonomy between the guarantor' obligations, on the one hand, and the rights and obligations of the parties to the underlying contract on the other, the law applies a separate, more stringent, test in the case of injections sought against the payment of demand guarantees.

The exceptions are; (i) fraud affecting the documents presented by the beneficiary (for example if they have been forged). Fraud is not limited to dishonesty or fraudulent intent, but extends to an absence of objective good faith, as where no reasonable person would have considered the demand to be justified e.g. if the beneficiary had no honest belief in the validity of its demand;

5 (ii) illegality in the demand guarantee contract or underlying contract; (iii) the infringement of international obligations and express contractual derogation from the principle of autonomy; and (iv) the total failure of the basis of the contract, i.e. the reason for its existence.

In order to obtain a temporary injunction, the applicant will be required to establish that: (i) there is a serious question to be arbitrated as to whether the 1st respondent has a right to call on the

10 guarantee; (ii) that if the application is not granted, the applicant stands to suffer irreparable damage; and (iii) the balance of convenience favours leaving the guarantee intact until the dispute is resolved. This will often be the case where the applicant can demonstrate that the payment of damages in lieu of an injunction would be an inadequate remedy.

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While it might appear that these requirements could be readily satisfied where there is a bona fide dispute, particularly where the applicant stands to suffer significant reputational damage if a call were to be made, in the context of demand performance guarantees, courts will typically refuse an injunction unless there are special circumstances that suggest they should do otherwise.

20 The rationale behind this is that, by agreeing that the applicant will provide the demand performance guarantee on the terms set out in the contract, the parties have also agreed to allocate the financial risk of any dispute to the applicant until it is finally resolved.

There are however at least three instances where courts will deviate from this position: (i) where

25 there is compelling evidence of fraud on the part of the beneficiary; (ii) where there is compelling evidence of unconscionable conduct on the part of the beneficiary; or (iii) to ensure the beneficiary adheres to any contractual promise not to call on the performance guarantee (i.e., a negative stipulation). Unless the above circumstances are present, a court is likely to refuse an injunction for the reasons set out above.

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- i. Whether the applicant has a *prima facie* case or a serious question to be arbitrated, with a probability of success against the 1st respondent.

First, a preliminary assessment must be made of the merits of the matter taken to arbitration, to ensure that there is a “serious question to be arbitrated.” One of the criteria to be applied when considering whether or not to grant a temporary injunction is disclosure by the applicant’s pleadings, of a “serious arbitrable issue,” with a possibility of success, not necessarily one that has a probability of success (see *American Cyanamid v. Ethicon* [1975] AC 396; [1975] ALL ER 504; *Godfrey Sekitoleko and four others v. Seezi Peter Mutabazi and two others*, [2001 –2005] HCB 80 and *Nsubuga and another v. Mutawe* [1974] E.A 487). There is no need to be satisfied that a permanent injunction is probable at arbitration; the court only needs be satisfied that the claim is not frivolous or vexatious; in other words, that there is a serious question to be arbitrated. A serious question is thus any question that is not frivolous or vexatious. As long as the claim is not frivolous or vexatious, the requirement of a *prima facie* case is met. The Court must be satisfied that there is a serious question to be arbitrated as to whether the respondent has a right to call on the guarantee (see *G&S Engineering Services v. MACH Energy Australia Pty Ltd* [2019] NSWSC 407).

The court no doubt must be satisfied that the claim is not frivolous or vexatious; in other words, that there is a serious question to be arbitrated, and that there is at least a reasonable chance that the applicant will succeed at the arbitration. The applicant needs to show only a reasonable likelihood of success on the merits; a better than negligible chance of success otherwise, parties with weak cases will be encouraged to seek interim injunctive relief in cases where permanent relief may not be possible. The applicant’s burden on this part of the test is relatively low, and in most cases an applicant will be able to show that there is a serious question to be arbitrated. The court must not decide issues that the parties have left to arbitrators. The applicant is required to provide reasonably available evidence to satisfy the court with a sufficient degree of certainty that the applicant is the rights-holder and that his or her rights are being infringed, or that such infringement is imminent. The applicant must show a strong probability that the feared conduct and resulting damage will occur.

On basis of the facts pleaded by the parties, the controversy between them seems to rotate around the question whether the respondent has a right to call on the guarantee. While the applicant contends that the terms for encashment of the two guaranties were varied by the Mutual Release and Settlement agreement which conditioned a call thereon on a joint audit by the parties, the 1st respondent argues that it was an express term of the agreement that the two guarantees were to remain in place and in full force until expiration thereof. These are sufficiently serious questions going to the merits to make them a fair ground for arbitration. To obtain an interlocutory injunction an applicant must show only that its claim is not frivolous or vexatious, that is to say, it has a serious issue to be arbitrated. The applicant has satisfied this requirement.

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- ii. Whether the applicant will have an adequate remedy at law or will be irreparably harmed if the injunction does not issue.

Second, the applicant must show that it will suffer irreparable harm if the court refused to grant the injunction and the respondents were allowed to continue in their course of conduct. “Irreparable” in this context refers not to the size of the harm that would be suffered, but its nature. If the harm could not be quantified by payment of money, or if the harm is not readily calculated or estimated, this part of the test will usually be satisfied. In some cases, the availability of damages often precludes such a finding.

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Irreparable damage has been defined by *Black’s Law Dictionary*, 9th Edition page 447 to mean; “damages that cannot be easily ascertained because there is no fixed pecuniary standard of measurement.” It has also been defined as “loss that cannot be compensated for with money” (see *City Council of Kampala v. Donozio Musisi Sekyaya C.A. Civil Application No. 3 of 2000*).

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The purpose of granting a temporary injunction is for preservation of the parties, legal rights pending litigation. The court doesn’t determine the legal rights to the property but merely preserves it in its current condition until the legal title or ownership can be established or declared. If failure to grant the injunction might compromise the applicants’ ability to assert their claimed rights, for example when intervening adverse claims by third parties are created, there is a very high likelihood of occasioning a loss that cannot be compensated for with money.

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The Court may grant a temporary injunction if it is apparent that the respondent is about to embark on a course of action that would infringe an applicant's rights. The court will particularly be inclined to grant the injunction where there appears to be a *prima facie* breach of property rights, or where the potential harm that could flow should a court order not be granted is difficult or impossible to calculate and quantify at a later stage in the arbitration, or where the damages when awarded may be irrecoverable (*see Itek Corp. v. First Nat. Bank of Boston, 566 F. Supp. 1210 (D. Mass. 1983)*). The fact that damages may be reasonably calculable will provide an applicant with little consolation in the event those damages ultimately prove uncollectable.

As an injunction is an equitable and discretionary remedy, it is a general rule that an injunction will not be granted where damages are an adequate remedy. Before an injunction is ordered, it must be established that an award of damages is not an adequate remedy. That type of claim can be made in exceptional cases involving breach of contract, akin to a breach of fiduciary duty, where the normal remedies are inadequate and where deterrence of others is an important factor. Courts often will step in to preserve the status quo where the withholding of injunctive relief would render the process of arbitration meaningless or a hollow formality because an arbitral award, at the time it was rendered, could not return the parties substantially to the status quo ante i.e., conditions would be so changed that no arbitral award could substantially remedy the grievances. An injunction ought not to be granted where the respondent would be restored to the financial position it would have been in had the injunction not been granted.

In order to establish that damages are not adequate, the innocent party will generally have to evidence either that a) the subject matter of the contract is rare or unique or b) damages would be financially ineffective. Damages may be found to be an inadequate remedy in the following circumstances, among others: (a) the damage is impossible to repair; (b) the damage is not easily susceptible to be measured in economic terms; (c) the harm caused is not a financial one; (d) monetary damages are unlikely to be recovered; (e) an award of damages is inappropriate in light of the importance of the interest in issue; and (f) the harm has not yet occurred or the wrong is continuing. If there is an adequate alternative remedy, the claimant should pursue such remedy.

Examples of rare or unique subject matters might be the sale of an interest in land (as no two pieces of land are the same) or a one-off antique vase. In both scenarios, damages may not be an adequate remedy because no market substitute exists, and the innocent party would therefore be unable to secure equivalent performance (no matter what the price). Examples of circumstances where damages may be financially ineffective might be where the defaulting party is insolvent and unable to pay; if damages would be difficult to quantify (e.g., a contract to indemnify); if an order for the payment of damages would be difficult to enforce (e.g., because any enforcement would need to be in a foreign country); or if an express term of the contract restricts or limits the damages recoverable for that particular breach.

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The calling up of a demand guarantee, especially if it is an unfair or fraudulent calling, often has the following severe consequences for the principal: irreparable damage to his commercial reputation; cash liquidity problems; and the risk that the cash will be misappropriated by the beneficiary and no longer recoverable. Courts have recognised on a number of occasions that calls upon performance guarantees may cause significant damage to a contractor's reputation and financial standing that is not readily curable by an award of damages (see for example *Barclay Mowlem Construction Ltd v. Simon Engineering (Aust) Pty Ltd* (1991) 23 NSWLR 451 at 461 – 462; *Reed Construction Services Pty Ltd v. Kheng Seng (Australia) Pty Ltd* (1999) 15 BCL 158 at 167; *Lucas Stuart Pty Ltd v. Hemmes Hermitage Pty Ltd* [2010] NSWCA 283 at [45]; *Austrak Pty Ltd v. John Holland Pty Ltd* [2006] QSC 103 and *Structural Systems (Constructions) v. Hansen Yuncken Pty Ltd* [2010] FCA 1358.).

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Calling of a guarantee tends to erode the confidence banks and other financiers have in the contractor's systems and project management. It tarnishes the business image of a contractor, especially where such contractor has built its business on meeting its contractual obligations, meaning completing its obligations without the need for security ever being called upon. Irreparable damage will be done to its reputation as: (a) its clients may question its ability to meet its contractual obligations; (b) its prospects of future successful tenders will be diminished; and competitors will take advantage to the contractor's detriment.

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The fees payable in respect of the face value of each bank guarantee and the amount of the facility which the bank is prepared to advance to the contractor is directly referable to how the bank assesses the contingent risk that the bank guarantee will be called upon. As a result of a call on a guarantee, the bank will be likely to assess the contractor's contingent liability risk as being higher. If the bank were to assess that the contingent liability of the contractor in relation to bank guarantees is higher than in previous years as a result of the respondent calling the guarantee, then those fees may increase and the limit of the facility may decrease for the contractor specifically. Furthermore, in the world of commerce, a contractor's reputation is paramount. A contractor's "security" history (in the sense of whether any of its bank guarantees have ever been cashed) is an important part of that contractor's reputation, and is taken into account by prospective clients of the contractor when considering "Expressions of Interest" or tenders. If loss is suffered, for example, through failure to obtain tenders, the assessment of damages would be a difficult and unsatisfactory process.

15 The calling up of a performance guarantee is a serious matter, with the potential to irreparably damage the contractor's reputation as a competent service provider, which might be taken advantage of in future projects by the contractor's competitors. It is in that context that Hunter J in *Abigroup Contractors Pty Ltd v. Peninsula Balmain Pty Ltd 2003] HCA Trans 688* opined:

20 The question of commercial reputation and the effect of a demand on a large contractor, with a record to date which has been evidenced in that context, should not be underestimated and there is a strong legitimate entitlement on the part of such a contractor to protect that reputation to the hilt.

25 Similarly, Rolfe J in *Barclay Mowlem v. Simon Engineering (Australia) Pty Ltd (1991) 23. NSWLR 451* stated;

30 Once the evidence [of damage to reputation] is admitted....it demonstrates how inadequate a remedy in damages would be. The matter, so far as the plaintiff is concerned, which is detrimentally affected upon a performance bond being called up, is the perceived ability of the plaintiff to properly perform its obligations under a contract. If the plaintiff's ability in this regard is called in question, even improperly, it is not difficult to infer that there will be damage to its reputation in the industry in which it operates. Nor is it difficult to infer that its competitors would be quick to utilise such information in competing with the plaintiff. Finally, particularly as

matters presently stand in the commercial world, questions may be raised as to the financial viability of the plaintiff ... This would be underlined if ... there has not previously been any call upon a performance bond. In other words, people may be tempted to ask whether the plaintiff's business was "going downhill."

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Irreparable damage may be occasioned to the commercial reputation of the principal by an abusive enforcement of a first demand guarantee. For that reason, a temporary injunction may be issued in order to prevent the abusive and imminent enforcement of a first demand guarantee, pending a decision of the arbitrator. The injunction will be granted in case of a *prima facie* or
10 manifest abuse or fraud by the beneficiary, or in case of collusion of the latter with the principal. In such cases the fraud or the abuse merges with the bad faith of the beneficiary who seeks to enforce his/her guarantee while he/she/it is fully aware that the enforcement requirements are not met. While the Courts acknowledge that the beneficiary of a first demand guarantee has the right to enforce such guarantee without having to worry immediately of what the principal owes or
15 does not owe, the beneficiary may not, on the other hand, knowingly exercise his/her/its right to enforce the guarantor's commitment with a view to receiving funds that are not due to him/her/it. As such, a request for enforcement of a guarantee must be held manifestly abusive wherever there is a *prima facie* awareness of the lack of right by the beneficiary and the knowledge of such abuse by the guarantor, are both established.

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Our legal system must of necessity entail mechanisms to prevent the wrongful, fraudulent and/or otherwise unconscionable calling of performance guarantees, even on-demand performance guarantees, without compromising the independence or autonomy principle, the documents principle and the strict compliance principle underpinning their utility in commerce. The court
25 will thus now proceed to determine whether the applicant has made out a case of an unfair or fraudulent calling of the guarantee, by considering the following sub-issues; (a) whether the applicant has made out a *prima facie* case of fraud in the documents rather than the underlying transaction; (b) whether the 1st respondent could not honestly have believed in the validity of its demand under the guarantee; (c) whether the 2nd respondent knew of the fraud at the time the 1st
30 respondent sought payment under the guarantee.

- a) Whether the applicant has made out a prima facie case of fraud in the documents presented, rather than the underlying transaction.

Three core principles underpin the International Chamber of Commerce (ICC) Uniform Rules for Demand Guarantees (URDG 758): the independence or autonomy principle, the documents principle and the strict compliance principle. By virtue of those principles, demand guarantees, standby letters of credit, and commercial letters of credit are all treated as autonomous contracts whose operation will not be interfered with by courts on grounds irrelevant to the guarantee or credit itself. Guarantors are concerned with documents, rather than with goods, services or performance of the underlying contract (see *Leonardo S.p.A v. Doha Bank Assurance Company LLC* [2019] QIC (F) 6; [2020] QIC (A) 1). Under the autonomy principle, an issuing bank must make payment under a demand guarantee on receipt of compliant documents irrespective of any dispute which may have occurred in respect of the underlying transaction.

The independence or autonomy principle, insulates the bond or guarantee from the terms in the underlying contract. This is important because the autonomous nature of the bond or guarantee means that conditions giving rise to the obligation to pay are found exclusively in the bond or guarantee. This independence principle is embodied in Article 5 (a) of the URDG 758. As discussed, in by the Privy Council in *Alternative Power Solution Ltd v. Central Electricity Board* [2014] UKPC 3, there is a bias or presumption in favour of the construction which holds a performance bond to be conditioned upon documents rather than facts, but the presumption is rebuttable (see *IE Contractors v. Lloyd's Bank* [1990] 2 Lloyd's Rep. 496). However, the appropriateness of the distinction between letters of credit and demand guarantees had been doubted in a more recent English Commercial Court judgment which suggests that the intention of the URDG is that the principle of strict compliance should apply both to letters of credit incorporating UCP 600 and demand guarantees incorporating URDG (see *Teare J in Sea-Cargo Skips v. State Bank of India* [2013] EWHC 177 (Comm)).

Demand guarantee undertakings rest on two legal principles: the principle of documentary or strict compliance, and the independence principle. The first legal principle essentially means that the guarantor is obliged to pay if the documents submitted with the demand for payment comply

with the terms of the demand guarantee. The second legal principle is that the guarantor's obligations against the beneficiary are determined in the instrument itself, and are independent, or abstract, of the underlying contract between the applicant for, and the beneficiary of, the guarantee, as well as the contract of mandate between the applicant and guarantor.

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The essential characteristic of a demand guarantee is that it is independent of the underlying transaction between the applicant and the beneficiary that prompted the issuance of the guarantee. Further, a demand guarantee is also independent of the instruction relationship pursuant to the applicant having requested the guarantor to issue the guarantee in favour of the beneficiary. The conditions giving rise to the obligation to pay are found exclusively in the demand guarantee and the terms of the underlying contract are of no relevance (*see Edward Owen Engineering Ltd v. Barclays Bank International Ltd [1978] 1 All ER 976, [1978] 1 QB 159, [1977] 3 WLR 764, [1978] 1 Lloyds Rep 166*). A direct consequence brought about by the independence principle is the “pay first, argue later” rule; the beneficiary of a demand guarantee can expect payment under the guarantee as soon as it is able to tender the documents stipulated in the demand guarantee, irrespective of any dispute arising from any of the contracts other than the demand guarantee itself.

There are of course exceptions to the strict general rule that the court will not intervene to prevent a guarantor from making payment under a demand bond or guarantee following a compliant presentation of documents; the fraud exception that is more or less universally acknowledged, and illegality exception applied in some jurisdictions. In the United States of America (*see Intraworld Industries, Inc. v. Girard Trust Bank, 336 A.2d 316 (Pa. S.C. 1975); Szejn v. J. Henry Schroder Banking Corp. - 177 Misc. 719, 31 N.Y.S.2d 631 (Sup. Ct. 1941); Asbury Park & Ocean Grove Bank v. National City Bank of New York 35 N.Y.S.2d 985 (N.Y. Sup. Ct. 1942) and New York Life Insurance Co. v. Hartford National Bank & Trust Co., 378 A.2d 562 (Conn. S.C. 1977) at p. 567*), and South Africa (*see Joint Venture between Aveng (Africa) (Pty) Ltd and Strabag International GmbH v. South African National Roads Agency Soc Ltd and Another [2020] ZASCA 146*), illegality in the underlying contract is also an exception. When the issuer of a demand guarantee knows that a document, although correct in form, is, in point of fact, false or illegal, he cannot be called upon to recognise such a document as

complying with the terms of the demand guarantee. Where the documents or the underlying transaction are tainted with intentional fraud, the guarantee need not be honoured by the bank, even though the documents conform on their face and the court may grant injunctive relief restraining such honour (see *NMC Enterprises v. Columbia Broadcasting System, Inc*¹⁴ U.C.C.

5 *REP. SERV. 1427 (N.Y. Sup. Ct. 1974).*

In Australia, a contractor may restrict the beneficiary from making a call on a performance guarantee if the contractor can show that the call would be a breach of a term in the underlying contract. It is not necessary to allege any fraud on the part of the beneficiary (see *Uber Builders and Developers Pty Ltd v. MIFA Pty Ltd [2020] VSC 596*, where Nichols J re-affirmed that
10 “where the contract does impose an obligation on the right to access the security, the party seeking to restrain recourse must establish the existence of a serious question to be tried as to whether the beneficiary has in fact met the contractual requirements”).

In all the above-mentioned jurisdictions, where the beneficiary’s fraud had been called to a
15 bank’s attention, before the documents have been presented for payment, the principle of the independence of the bank’s obligation under the demand guarantee should not be extended to protect an unscrupulous beneficiary. The courts aver that when the issuer of a guarantee knows that a document, although correct in form, is false or illegal, it cannot be called upon to recognise such a document as complying with the terms of the guarantee. A bank should be vitally
20 interested in assuring itself that there is some exchange of value represented by the documents.

The Courts in England do not consider illegality in the underlying contract to be a valid exception to the autonomy principle of demand guarantees. They however attempted to acknowledge as the second exception in addition to that of fraud, situations where a beneficiary
25 seeks payment in circumstances where the underlying contract clearly and expressly prevents it from doing so. The Courts’ view in principle, was that if the underlying contract (in relation to which the bond has been provided by way of security) clearly and expressly prevents the beneficiary from making a demand under the bond, it can be restrained by the court.

30 For example, in *Simon Carves Ltd v. Ensus UK Ltd [2011] EWHC 657 (TCC)*, [2011] BLR 340, 135 Con LR 96, the underlying construction contract contained a provision stating that the

performance bond shall become null and void, and returned to the contractor, immediately upon the issue of an acceptance certificate by the employer. The employer issued an acceptance certificate prior to the expiry date of the bond and subsequently purported to make a call on the bond. The court held that the bond remained valid between the employer and the issuing bank, but as between the employer and the contractor the bond was null and void. The court, however, did not grant an injunction preventing a call on the bond per se but instead granted an injunction preventing a breach of an express term of the underlying contract which regulated the ability of the employer to call on the bond. In its passing comments the court contemplated the existence of an alternate possible ground on which a contractor might resist a call on a bond straight breach of contract.

Similarly in *Doosan Babcock Ltd v. Comercializadora de Equipos y Materiales Mabe Limitada* [2013] EWHC 3010 (TCC) the underlying construction contract contained similar provisions to those in *Simon Carves* in that the contract stated the bond was to expire on the earlier issue of a taking-over certificate by the employer or a fixed expiry date. The employer did not actually issue the taking over certificate prior to making a call on the bond. The contractor, however, sought an injunction against the employer's subsequent call on the basis that the employer ought to have issued a taking-over certificate but had not done so in breach of the underlying contract, and had it done so it would have no entitlement to call on the bond. The court granted an injunction preventing the call on the bond, relying on the common law principle that a party should not profit from its own breach of contract.

The decisions in *Simon Carves* and *Doosan*, however, indicate a departure from the traditional exceptions of fraud and illegality. Commentators have much-maligned the two decisions for their perceived broadening of the circumstances in which a court may enjoin a call on a bond beyond fraud and illegality. Nevertheless, these decisions suggest that the courts may look to provisions in an underlying contract, which regulate calls on a bond related to such contract, in a way that pierces the autonomy between the parties' obligations under the contract and the issuing banks obligation under the associated bond.

30

The distinction between *Alternative Power Solution*, on the one hand, and *Simon Carves* and *Doosan*, on the other seems not that the former concerns a letter of credit and the latter a performance bond, but that the latter concerned a contract which contained provisions regulating the beneficiaries call on the bonds, whereas the former did not. Moreover, the contractual provisions which the courts looked to in *Simon Carves* and *Doosan* were technical in nature, essentially preventing a call on the bond where the discharge of obligations under the contract meant the security afforded to the beneficiary through the bond had, or ought to have, effectively expired.

10 In *Alternative Power Solution Ltd v. Central Electricity Board & Anor (Mauritius) [2014] UKPC 31*, the Privy Council found that the Mauritian Central Electricity Board was not entitled to an interlocutory injunction to prevent payment under a letter of credit, notwithstanding its allegations of fraud and the fraud exemption. In that case, Alternative Power Solutions Ltd (“APS”) entered into an agreement (the “Agreement”) following a bid process to supply 660,000 compact fluorescent lamps (“CFLs”) to the Mauritanian Central Electricity Board (“CEB”). The means of payment was by letter of credit (“LOC”) which was issued by Standard Bank (“SB”) in favour of APS. Inspection at the place of manufacture was required under the Agreement but there was no requirement for certificates of inspection or similar documentation to be presented to SB under the LOC. APS and CEB failed to come to any arrangement relating to delivery and inspection of the CFLs. With the expiry date of the LOC approaching, the Chinese manufacturers shipped the CFLs. APS tried to claim payment under the LOC. Whilst SB considered the documentation discrepant, SB made it clear that it would be prepared to pay against compliant documents. CEB sought an injunction to prevent SB releasing the payment. CEB alleged that APS’s bid mentioned that the CFLs would be manufactured by Philips or under licence by Philips in China. It further alleged that APS was throughout in breach of the tender documents because it had not allowed CEB to inspect and verify the 660,000 CFLs at the place of manufacture in China. It was also alleged that at an initial hearing one of APS’s representatives had stated that the goods would not be shipped until the inspection took place, when the goods were, in fact, in transit. The court at first instance and the Mauritian Court of Appeal both ruled in favour of CEB as they felt that there was enough evidence to engage the fraud exemption.

On appeal to the Privy Council, it held that the test for the fraud exemption cannot be quite the same as at a trial and that the test at the interlocutory stage can properly be described as whether it is seriously arguable that, on the material available, the only realistic inference is that the beneficiary could not honestly have believed in the validity of its demands on the letter of credit and that the bank was aware of that fact. The difficulty with CEB's allegations was that they were allegations of breach of contract and thus matters for arbitration and irrelevant to the liability of SB under the LOC. In so far as the judges in the lower court relied upon them they erred in principle. In all these circumstances, the Privy Council concluded that, whatever test is applied, neither the judge nor the Court of Appeal was entitled to reach the conclusion that the fraud exception was satisfied, in the case of either APS or SB.

In Singapore, the position of the courts is similar to the position of the courts in England. Calls on on-demand Bank Guarantees can be restrained, either on the account of "fraud" or "unconscionability," which are treated as two distinct and independent grounds of restraint (see *Bocotra Construction Pte Ltd v. Attorney General (No. 2)* [1995] 2 SLR 523; *GHL Pte Ltd v. Unitrack Building Construction Pte Ltd* [1999] 4 SLR 604; *Dauphin Offshore Engineering & Trading Pte Ltd v. HRH Sheikh Sultan bin Khalifa bin Zayed Al Nahyan* [2000] SGCA 4 and *Shanghai Electric Group Co Ltd v. PT Merak Energi Indonesia* [2010] SGHC 2). In Malaysia, "unconscionability" is recognised as a separate and independent ground to issue a restraining order, which stems from the "general underlying notion.... of equity's traditional jurisdiction to grant relief against unconscientious conduct namely, that a person should not be permitted to use or insist upon his legal rights to take advantage of another's special vulnerability or misadventure for the unjust enrichment of himself..." (see *Sumatec Engineering & Construction Sdn Bhd v. Malaysian Refining Company Sdn Bhd* [2012] 3 CLJ 401).

The Courts in Singapore have defined "unconscionability" as "...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 restrain the party or refuse to assist the party. Mere breaches of contract by the party in question ... would not by themselves be unconscionable" (see *Kiso (S) Pte Ltd v. Lum Chang Building Contractors Pte Ltd* [2013] SGHC 86). A contractor applying for an injunction on the basis of "unconscionability" has to establish a "strong *prima facie* case of

unconscionability,” in which case the parties’ conduct leading up to a call on a bond and the presence of notice are all relevant considerations (see *Tactic Engineering Pte Ltd (in liq) v. Sato Kogyo (S) Pte Ltd* [2017] SGHC 103). The Singapore courts have allowed the exception of unconscionability to cater for situations where the conduct of the beneficiary was sufficiently reprehensible to justify an interdict in circumstances where the facts do not amount to fraud.

The case law canvassed here demonstrates that the principle of independence continues to be a dominant theory in demand-guarantee practice. With varying outcomes, Courts in the different jurisdictions have considered whether the application of the fraud rule should be confined to cases of forged or fraudulent documents or extend to fraud in the underlying transaction. As a general proposition, injunctions will not be granted to prevent a party from calling upon a demand bank guarantee, except in cases of fraud, unconscionability, or breach of a negative stipulation in the underlying contract. It is this court’s considered view that provisions in an underlying contract, which regulate calls on a bond, should only be considered with circumspection where events or conduct are of such degree such as to prick the conscience of a reasonable and sensible man. Resort to the underlying contract requires a certain and compelling case to be established; cases where the demand on the guarantee can be said to be “clearly untrue or false,” or “utterly without justification,” or where it is apparent there is “no right to payment.” Cases in which proof is furnished of the absence of any colourable or plausible basis under the underlying contract for the beneficiary to call the guarantee.

While the notion of fraud may elude precise definition, it is a concept well known to the law, connoting some aspect of impropriety, dishonesty or deceit. Fraud is not mistake, error in interpreting a contract; fraud is something dishonest and morally wrong, resulting in mischief or unnecessary pain. Fraud is defined as the unlawful and intentional making of a misrepresentation that causes actual prejudice or is potentially prejudicial to another. The traditional approach of English courts to the calling of Bank Guarantees is to limit injunctions to situations where there is clear evidence of “fraud,” which under English law can only be proven if it is demonstrated that a false representation has been made (i) knowingly; or (ii) without belief in its truth; or (iii) recklessly without caring as to whether it be true or false (see *Derry v. Peek* [1889] 14 App Cas 337). Fraud in relation to the calling of Performance Bonds has been extensively discussed in

cases such as *Enka Insaat Ve Sanayi v. Banca Popolare Dell'Alto Adige* [2009] EWHC 2410, which further confirms the high threshold for proving fraud under English law.

5 In light of the foregoing comparative analysis, given that the purpose of the fraud rule is to stop dishonest beneficiaries from abusing the demand guarantee system, this court is inclined to state that the test for fraud is met, not by showing breach or other non-compliance with the terms of the underlying contract, but when strong or compelling evidence is led to show that the documents presented to the Bank are forgeries or contain any express material misrepresentations. As in any other case, where fraud is alleged, it will not be inferred lightly
10 and mere error, misunderstanding, non-compliance with the terms of a guarantee or oversight does not translate into fraud and will not amount to fraud. It should rise to the level of egregious conduct; meaning conspicuously, glaringly, or staggeringly or flagrantly bad, of a nature that would vitiate the very foundation of the bank guarantee. A kind of outrageous conduct which shocks the conscience of the court, such as or where the guarantee is called upon with absolutely
15 no basis in fact. Courts will not permit a guarantee to be used for a purpose for which it was never generated. The facts of the case should depict that fraud committed by the beneficiary is of such nature that it destroys the entire underlying transaction.

A colourable claim is a plausible legal claim, one that may reasonably be asserted on the basis of
20 facts presented and current law. This means that the claim is “strong enough” to have a reasonable chance of being valid if the legal basis is generally correct and the facts can be proven in court. The insolvency of the contractor and/or the automatic determination of the employment of the contractor usually constitutes an event of default for the purposes of calling the bond. That the underlying contract was terminated before completion, in the absence of any fraud, bad faith
25 or other special circumstances, usually presents a justifiable basis for a beneficiary of a performance guarantee, to make a call thereon. To overcome that seemingly valid or genuine basis for the plausible call, the applicant must present a case of manifest fraud to justify an injunctive interim relief. A manifest fraud is one that is obvious or easily demonstrable without extensive investigation. The alleged fraud should be so obvious as to admit of no difference of
30 opinion. It is one that can be demonstrated immediately and almost conclusively. This relatively

high standard is intended to avoid applications introduced only as a subterfuge or means of evading a call.

5 In the instant case, it is not in dispute that the applicant had not executed the contract fully at the time of its termination whereafter a call was made on the guarantee. That a call thereon is subject to a prior joint audit which is yet to be undertaken as claimed by the applicant, but disputed by the 1st respondent, is not a fact of a nature that is easily demonstrable without extensive investigation. On basis of the evidence availed to court at this stage, the applicant has not furnished proof of the absence of any colourable or plausible basis under the contract as
10 originally executed, or the Mutual Release and Settlement agreement, for the 1st respondent to call on the guarantee. It is not seriously arguable that on the material available the only realistic inference is that the 1st respondent, as beneficiary, could not honestly have believed in the validity of its demands. The possibility of invoking a claim against the beneficiary by way of set-off does not constitute a denial of the legitimacy of the beneficiary's demand or constitute a
15 manifest fraud.

Although the merits of the parties' respective cases and their relative strengths are not to be considered at this stage, the court is of the view that the applicant has not established a strong *prima facie* case of manifest fraud, or that the guarantee was called upon with absolutely no basis
20 in fact. The applicant has not satisfied this requirement.

b) Whether the 1st respondent could not honestly have believed in the validity of its demand under the guarantee.

25 Other than in cases of illegality, a court may only step-in to enjoin a call on a guarantee in the case of fraud on the part of the beneficiary. An injunction will only be granted against a bank if there is a seriously arguable case that the person calling on it, did not honestly believe the validity of the cause (see *United Trading v. Allied Arab Bank [1981] 2 Lloyds 256, at para 257*). When determining this in interlocutory proceedings, the Courts apply a two-stage test: (a) that
30 the beneficiary could not honestly have believed in the validity of its demand under the guarantee and (b) that the bank knew of the fraud at the time the beneficiary made the demand. It

must be seriously arguable on the material available that the only realistic inference is that 3rd respondent could not honestly have believed in the validity of its demand under the guarantee.

The correct test is stated in *United Trading Corporation S.A. v. Allied Arab Bank Ltd* [1985] 2
5 *Lloyd's Rep* 554, namely; whether it is seriously arguable that, on the material available, the only realistic inference is that the beneficiary could not honestly have believed in the validity of its demands and that the bank was aware of that fact. To successfully rely on fraud, a party has to go further and show that the beneficiary made the call, in bad faith, knowing it to be incorrect. If a beneficiary makes a false representation without actual knowledge that it is false, but with no
10 honest belief in its truth, this too could constitute a fraud in terms of the fraud exception. This is because fraud connotes the absence of an honest belief in either the entitlement to claim under the guarantee or in the amount claimed.

An injunction will be granted where, for the purpose of drawing on the guarantee, the beneficiary
15 fraudulently presents to the bank documents that contain, expressly or by implication, material representations of fact that to his knowledge are untrue (see *United City Merchants (Investments) Ltd. v. Royal Bank of Canada*, [1983] 1 A.C. 168 at 183). A material fraudulent misrepresentation occurs where the beneficiary makes a false statement or representation, knowing the representation to be false, or without belief in its truth; or recklessly, careless
20 whether it be true or false. The word “material” means “material to the bank’s duty to pay, so that if the document stated the truth the bank would be obliged to reject the document.

Demanding payment in the knowledge of the absence of material entitlement, constitutes fraud. There must be no honest belief in the validity of a demand for the fraud exception to apply (see
25 *Uzinterimpex JSC v. Standard Bank plc* [2007] 2 *Lloyd's Rep* 187 para 107; *Intraco Ltd v. Notis Shipping Corporation (The Bhoja Trader)* [1981] 2 *Lloyd's Rep* 256 and *National Infrastructure Development Co Ltd v. Banco Santander SA* [2016] EWHC 2990 *Comm* para 11). The fraud must be clearly illustrated, or it must be the only realistic inference that may be drawn from the available circumstantial evidence. Conduct whereby the beneficiary’s submission of the demand
30 rests on statements of fact which, to its own positive knowledge, are incorrect or contain misrepresentations, may translate into fraud.

Although counsel for the applicant argued that a call thereon was subject to a prior joint audit which was yet to be undertaken, this was refuted by counsel for the 1st respondent. Indeed, it is following a joint audit that the parties agreed it was the applicant who was indebted to the 1st respondent, whereby the amount so ascertained was to be paid in twelve (12) equal monthly instalments from 30th June 2021 until payment in full. In the event that the payments were not made for three (3) consecutive months, it was agreed further that the 1st respondent would be entitled to recover the amounts owing from any money payable to the applicant from M/s Cascadia Development (their sister Company in Kenya); in the further event of failure of all the above, the 1st respondent would be entitled to make a call on the performance guarantee.

It appears the 1st respondent made a call on both the advance payment and the performance guarantees. Advance payment guarantees manage the risk of the contractor's failure to earn the whole of any advance payment from the employer by failing to provide services to an equivalent value. The failure may result from the contractor's insolvency, fraud or default through using the advance payment for another purpose. Such guarantees, as happened in this case, usually contain a reduction clause, whereby the amount of the guaranteed reduces in accordance with monthly certificates until the certified value of work done exceeds the advance payment. It appears that in this case by the time the contract was terminated, the applicant had supplied services of a value that exceeded that of the advance payment guarantee, so as to effectively discharge it.

That aside, a demand guarantee will always have an expiration date, which the beneficiary must respect. The right to invoke the guarantee is only for a default of the contractor which occurs during the validity period of the bank guarantee (see *Yuanda (UK) Co Ltd v. Multiplex Construction Europe Ltd (formerly known as Brookfield Multiplex Construction Europe Ltd) & Anor [2020] EWHC 468 (TCC)*). The claim period is a contractually agreed period of time between the beneficiary and the contractor which provides a grace period beyond the validity period to make a demand on the guarantor for a default which has occurred during the validity period. A claim period may or may not exist in the guarantee. Unless a call under the guarantee is filed before the date of expiry, all the beneficiary's rights under the said guarantee are forfeited and the guarantor is relieved and discharged from all liability thereunder. Considering that the

advance payment guarantee expired on 9th December, 2021, the 1st respondent could not honestly have believed in the validity of its demand when it made a call based on that guarantee. However, as regards the call on the performance guarantee which has an expiry date of 1st April, 2023, it cannot be stated that the 1st respondent could not honestly have believed in the validity of its demand under the performance guarantee. The applicant has not satisfied this requirement as well.

c) Whether the 2nd respondent knew of the fraud at the time the 1st respondent sought payment under the guarantee.

10

It is necessary that at the time of the calling of the guarantee, the guarantor should have notice of the fraud. Moreover, such fact of notice along with its evidence has to be averred in the application. A guarantor should not pay where a fraud by the beneficiary of the guarantee has been sufficiently brought to its knowledge before payment or demonstrated to a court called on by the beneficiary to issue an interlocutory injunction to restrain the guarantor from honouring the draft (see *Bank of Nova Scotia v. Angelica-Whitewear Ltd [1987] 1 SCR 59*). In the instant case, having found that the applicant has not established a strong *prima facie* case of manifest fraud, or that the guarantee was called upon with absolutely no basis in fact, this element does not arise at all.

20

iii. Balance of convenience (whether the threatened injury to the applicant outweighs the threatened harm the injunction might inflict on the respondents).

When the court is in doubt considering the outcome of its consideration of the first two factors, the third part of the test involves the court assessing which of the parties would suffer greater harm from the granting or refusal of the injunction pending arbitration. Unless the material available to the court at the hearing of the application for an interlocutory injunction fails to disclose that the applicant has any real prospect of succeeding in his or her claim at the arbitration, the court should go on to consider whether the balance of convenience lies in favour of granting or refusing the interlocutory relief that is sought.

30

This part of the test is referred to as the “balance of convenience.” Balance of convenience means comparative mischief or inconvenience that may be caused to the either party in the event of refusal or grant of injunction. It is necessary to assess the harm to the applicant if there is no injunction, and the prejudice or harm to the respondent if an injunction is imposed. The courts
5 examine a variety of factors, including the harm likely to be suffered by both parties from the granting or refusal of the injunction, and the current *status quo* as at the time of the injunction. The court should then take whichever course appears to carry the lower risk of injustice if it should turn out to have been “wrong.” It is thus necessary to weigh in the balance of convenience the public interest as well as the interest of the parties.

10

The Court has the duty to balance or weigh the scales of justice by ensuring that the arbitration is not rendered nugatory while at the same time ensuring that a respondent is not impeded from the pursuit of his or her contractual rights. No doubt it would be wrong to grant a an injunctive interim protective measure pending disposal of the arbitration where the claim is frivolous or
15 where such order would inflict greater hardship than it would avoid. Save in the simplest cases, the decision to grant or to refuse an injunctive interim protective measure will cause to whichever party is unsuccessful on the application, some disadvantages which his or her ultimate success at the arbitration may show he or she ought to have been spared and the disadvantages may be such that the recovery of damages to which he or she would then be entitled would not
20 be sufficient to compensate him or her fully for all of them.

25

The extent to which the disadvantages to each party would be incapable of being compensated in damages in the event of his or her succeeding at the arbitration is always a significant factor in assessing where the balance of convenience lies. The governing principle is that the court should
25 first consider whether if the applicant were to succeed at the arbitration in establishing his or her right to a permanent injunction, he or she would be adequately compensated by an award of damages for the loss he or she would have sustained as a result of the respondent’s continuing to do what was sought to be enjoined between the time of the application and the time of the arbitration. If damages in the measure recoverable at common law would be adequate remedy
30 and the respondent would be in a financial position to pay them, no interlocutory injunction should normally be granted, however strong the applicant’s claim appears to be at this stage.

If, on the other hand, damages would not provide an adequate remedy for the applicant in the event of his succeeding at the arbitration, the court should then consider whether, on the contrary hypothesis that the respondent were to succeed at the arbitration in establishing his right to do that which was sought to be enjoined, he would be adequately compensated by the applicant for the loss he or she would have sustained by being prevented from doing so between the time of the application and the time of the arbitration. If damages would be an adequate remedy and the applicant would be in a financial position to pay them, there would be no reason upon this ground to refuse an interlocutory injunction.

10

Even if a party is able to establish the fraud exception, it still faces an insuperable difficulty, in that it will have an adequate remedy against the bank in damages if it pays despite being on notice of fraud. By contrast, an injunction might cause greater damage to the bank than the party seeking the injunction could pay on their undertaking as to damages. In these circumstances, the balance of convenience will almost always be in favour of allowing the bank to pay. The balance of convenience will almost always militate against the grant of an injunction. The reasons for this disinclination become readily understandable when one contrasts the uncertainty in which a court finds itself with respect to the merits at the interlocutory stage, with the sometimes far-reaching albeit temporary practical consequences of an injunction, not only for the parties to the arbitration but also for the public at large.

20

In the instant case an injunction would have the effect of providing the applicant with the entire relief that is sought in the arbitration itself, which may not be undone by an award favourable to 1st respondent on the merits. On the other hand, the guarantee was issued on the understanding that if the applicant failed to complete the contract, then it would be the 2nd applicant as guarantor's obligation to perform the principal's task. The performance guarantee serves as a risk management tool for the beneficiary, as the guarantor assumes liability for financing the completion of the contract to the limit of the guarantee, should the contractor default on its contractual obligations.

30

Secondly, a performance guarantee serves as an agreed allocation of risk as to which of the parties is to be out of pocket pending resolution of the dispute about breach of the underlying contract (see *Clough Engineering Ltd v. Oil & Natural Gas Corp Ltd (2008) 249 ALR 458*; *Fletcher Construction Australia Ltd v. Varnsdorf Pty Ltd [1998] 3 VR 812, 826*; *Marcon Pty Ltd v. Kerman Contracting Pty Ltd [2015] WASCA 7* and *Sugar Australia Pty Ltd v. Lend Lease Services Pty Ltd [2015] VSCA 98*). It is a promise by the guarantor that it will pay to the beneficiary named in the guarantee an amount up to the limit set out there in unconditionally or on specified conditions, without reference to the terms of the contract between the parties. Most obviously the 1st respondent's loss will be the costs of completing the works since the applicant can no longer do so, yet there is a danger that the guarantee may have expired by that date arbitration concludes.

Although the beneficiary can claim under a guarantee in respect of any claims which have been notified to the guarantor on or before the expiry date but which have not been determined by the expiry date, claims under guarantees are often made immediately prior to the expiration date. This usually means that the beneficiary has one shot to make a complying presentation, and if the guarantor rightfully rejects the claim after the expiration date, the beneficiary has lost his rights to claim. I therefore find that the balance of convenience is in favour of not granting the interim measure of protection sought. The application is accordingly dismissed with costs to the 1st respondent.

Delivered electronically this 9th day of January, 2023
Mubiru.....

.....**Stephen**

Stephen Mubiru
Judge,
9th January, 2023.