

Contracting out of unconscionability

The Singapore Court of Appeal (CA) has overturned the High Court (HC) and ruled that parties can contractually exclude the unconscionability exception to calls on on-demand bonds (*CKR Contract Services Pte Ltd v Asplenium Land Pte Ltd and another and another appeal and another matter* [2015] SGCA 24).

Under Singapore law, a party may seek the assistance of the Courts to restrain calls on on-demand bonds on two grounds - on the ground of fraud, or on the separate ground of unconscionability. In this recent ruling, the CA found that where parties to a construction contract agree to limit the circumstances in which a contractor is entitled to seek an injunction restraining a call on a performance bond (ie to fraud only), Singapore courts will respect the parties' freedom to agree to such terms and enforce the restriction where it is reasonable.

The facts of the case

A clause in the construction contract between Asplenium Land Pte Ltd (Asplenium, the developer of a residential project in Singapore) and CKR Contract Services Pte Ltd (CKR, the main contractor in that project) stipulated that CKR was not entitled to restrain Asplenium on any ground except in the case of fraud (see relevant portion of clause, in adjacent box).

Disputes arose between Asplenium and CKR, and Asplenium called upon the bond provided by CKR. In the face of the Clause, CKR sought to restrain Asplenium's call on the ground of unconscionability.

This raised the intriguing legal question of whether the courts would uphold an agreement between parties to exclude the unconscionability exception to calls on on-demand bonds.

Given its obvious implications on industry practice, the decision by the CA was closely watched.

The Clause in question:

In keeping with the intent that the performance bond is provided by [the contractor] in lieu of a cash deposit, [the contractor] agrees that except in the case of fraud, [the contractor] shall not for any reason whatsoever be entitled to enjoin or restrain:

- (a) [the employer] from making any call or demand on the performance bond or receiving any cash proceeds under the performance bond; or*
- (b) [the bank] under the performance bond from paying any cash proceeds under the performance bond*

on any ground including the ground of unconscionability.

(the Clause)

The HC decision

At the first instance, the HC held that the Clause was unenforceable for three reasons:

- (a) the Clause was an impermissible attempt to oust the equitable jurisdiction of the court;
- (b) the courts' equitable power to grant injunctions could not be curtailed by contract; and
- (c) the unconscionability exception was based on policy considerations which cannot be brushed aside by contract.

The HC's view was understandable. After all, the creation of the unconscionability exception to on-demand bonds was a reaction to the inequitable results that may sometimes arise from a strict adherence to the contractual position under the bond.

Notwithstanding, the HC held that the unconscionability exception was not made out on the facts of the case, and decided not to restrain the call on the bond.

The CA decision

CKR appealed against the HC's finding that Asplenium did not make the call unconscionably. Asplenium cross-appealed against the HC's holding that the Clause was unenforceable.

On appeal, the CA overturned the HC on the part of the HC's decision that the Clause was unenforceable.

CKR's position on appeal was that, first, the Clause was an ouster of the jurisdiction of the court, and second, Singapore law had "developed a public policy" of protecting contractors from oppressive calls on on-demand bonds which could not be contracted out of.

The CA held that the Clause did not oust the court's jurisdiction, but rather limited the equitable remedies (of injunction) available to CKR. It was therefore akin to an exemption clause. Such clauses are not void and unenforceable.

The CA also held that public policy will void contracts only on rare occasions. The "policy" that underlies the unconscionability exception is different from the public policy which renders contracts void and unenforceable. There was therefore no reason to find that the Clause is unenforceable as it is contrary to public policy.

At the same time, the CA was careful to highlight that such a Clause could potentially be unenforceable, if, depending on the facts, it were to be unreasonable under the Unfair Contract Terms Act (Cap 396) (the UCTA). This was not an issue which arose in the appeal.

What this means for the construction industry

On-demand or unconditional performance bonds are already a ubiquitous mode of security for parties "up the line" in construction contracts in Singapore.

The availability of a potential avenue to sidestep the unconscionability exception (subject to unfair contract terms legislation) further strengthens the position of the beneficiary of the bond.

It is to be expected that, going forwards, parties "up the line" will be keen to include in their construction contracts a clause that excludes unconscionability or similar clauses that seek to bar any challenge to the security of an on-demand bond.

It is also to be expected that there will be a chilling effect on parties seeking to restrain payment upon on-demand bonds on the ground of unconscionability.

That said, members of the construction industry will need to be

careful with the language of the clause to be inserted, which will need to be carefully tailored and calibrated to the facts. In particular, they will need to come up with a way to try and avoid the clause being held to be unreasonable under the UCTA.

Concluding thoughts

This appears to be the latest in a trend of cases where parties will be held to their commercial bargain, barring fraud (which is said to "unravel all").

This is not an entirely surprising outcome, as this decision comes on the heels of an earlier decision by the HC which in effect allows parties to try and contract out of the unconscionability exception by providing for the performance bond to be governed by English law ie under which unconscionability is not a ground to restrain calls on that bond (*Shanghai Electric Group Co Ltd v PT Merak Energi Indonesia & Anor* (2010)).

The CA's decision in the present case in effect acknowledges that parties are free to expressly contract for what they could previously do indirectly, via a governing law clause.

The CA's clarification is therefore a timely one which avoids any inconsistency between the two strands of authority.

Read our other publications

If you would like to receive copies of our other publications on this topic, please email: sara.castelnuovo@cliffordchance.com

- **Court of Appeal accepts frustration in 'Sand Ban' case appeal** (July 2014)
- **Construction Case Watch** (May 2014)
- **Supplier Beware: An abnormal increase in costs will not frustrate a contract** (July 2013)

Contacts



Paul Sandosham
Partner

T: +65 6661 2055
E: paul.sandosham
@cliffordchance.com



Wei Xian Kelvin Teo
Senior Associate

T: +65 6661 2059
E: Kelvin.teo
@cliffordchance.com



Jerald Foo
Associate

T: +65 6661 2063
E: Jerald.foo
@cliffordchance.com

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

Clifford Chance Asia

Clifford Chance Asia is a Formal Law Alliance between Clifford Chance Pte Ltd and Cavenagh Law LLP.
12 Marina Boulevard, 25th Floor Tower 3,
Marina Bay Financial Centre,
Singapore 018982
© Clifford Chance and Cavenagh Law LLP, 2015
500986-4-6902-v0.3

www.cliffordchance.com
www.cavenaghlaw.com.sg

Abu Dhabi ■ Amsterdam ■ Bangkok ■ Barcelona ■ Beijing ■ Brussels ■ Bucharest ■ Casablanca ■ Doha ■ Dubai ■ Düsseldorf ■ Frankfurt ■ Hong Kong ■ Istanbul ■ Jakarta* ■ Kyiv ■ London ■ Luxembourg ■ Madrid ■ Milan ■ Moscow ■ Munich ■ New York ■ Paris ■ Perth ■ Prague ■ Riyadh ■ Rome ■ São Paulo ■ Seoul ■ Shanghai ■ Singapore ■ Sydney ■ Tokyo ■ Warsaw ■ Washington, D.C.

*Linda Widyati & Partners in association with Clifford Chance.