VICTORIAN CIVIL AND ADMINISTRATIVE TRIBUNAL

CIVIL DIVISION

BUILDING AND PROPERTY LIST

VCAT REFERENCE NO. BP537/2018

CATCHWORDS

Building Contract – AS 4300-1995 form of contract - security - bank guarantee – injunction to restrain recourse to – when granted – interpretation of security clause – whether a mere security or also a risk allocation clause -whether entitlement to payment under contract required – allocation of risk pending determination of entitlement to payment – determination by superintendent of liquidated damages due to Principal – amount of determination paid to Principal by Contractor – Principal seeking recourse to security to obtain a further payment for liquidated damages in addition to those assessed

APPLICANT	Orange Building Solutions Pty Ltd (ACN 167 079 781)
RESPONDENT	Inkerman Property Group Pty Ltd (ACN 163 104 407)
WHERE HELD	Melbourne
BEFORE	Senior Member R. Walker
HEARING TYPE	Injunction Hearing
DATE OF HEARING	27 April 2018
DATE OF ORDER	8 May 2018
CITATION	Orange Building Solutions Pty Ltd v Inkerman Property Group Pty Ltd (Building and Property) [2018] VCAT 696

ORDERS

1. Order that the Respondent, whether by itself, its servants or agents or howsoever otherwise, be restrained until further order from having recourse to the following bank guarantees:
   - ANZ Bank Guarantee No. DG550673418 for $68,007.80
   - ANZ Bank Guarantee No. DG547383418 for $217,008.45
2. **Direct the registry to list this proceeding for directions at a date and time to be fixed in order to determine its future conduct.**

3. Liberty to apply.

4. Costs reserved.

SENIOR MEMBER R. WALKER

APPEARANCES:

For the Applicant	Mr M. Roberts, QC
For the Respondent	Mr M. Whitten, QC with Mr L. Connolly of Counsel

REASONS

Background

1. On 29 April 2015 the Applicant ("the Contractor") entered into a building contract ("the Contract") with the Respondent ("the Principal") to construct a seven storey building on land owned by the Principal in St Kilda for a price of $11,400,650.00. The Contract was generally in the form of the AS 4300-1995 contract with a number of alterations.
2. Pursuant to the terms of the Contract, the Contractor provided security in the form of four bank guarantees in amounts totalling $570,032.50. Two of these guarantees, comprising one half of the total amount, have since been returned to the Contractor in exchange for it paying to the Principal an amount of $276,000.00. This amount had been demanded by the Principal with respect to liquidated damages claimed by it against the Contractor in accordance with a determination made by the superintendent appointed under the contract ("the Superintendent").
3. The Principal is dissatisfied with the determination made by the Superintendent and claims to be entitled to a greater sum for liquidated damages. It has given notice to the Contractor of its intention to seek recourse against the two remaining guarantees to recover the further amount that it claims and the Contractor has brought this application seeking an order to restrain it from doing so.

The hearing

4. The matter came before me for hearing on 27 April 2018. Mr M. Roberts QC appeared on behalf of the Contractor and Mr M. Whitten QC with Mr L Connolly of Counsel appeared on behalf of the Principal.
5. The application was supported by two affidavits by the director of the Contractor, a Mr Grills, and there was an opposing affidavit was by a Mr Baldwin, a director of the Principal.
6. Each side provided a written submission together with a binder of authorities said to support its case. The Principal's binder contains 19 cases and the Contractor's binder contained 8, although there was some overlap. Since it was intended by the parties that I should have regard to the principles to be distilled from these authorities and because the point in issue appeared to raise complex legal issues I said that I would provide a written decision.

What must be shown

7. There is no dispute as to the general principles concerning the granting of an interlocutory injunction. I must be satisfied that:

   (a) the Contractor has demonstrated that there is a serious issue to be tried, in that there is a sufficient likelihood of success at the trial to justify the preservation of the status quo pending trial;

(b) if interlocutory relief is not granted, it is likely to suffer injury that would not be adequately compensated by an award of damages; and

(c) the balance of convenience favours the granting of an injunction.

8. It appears from the authorities that satisfying the first of these requirements in the context of an application such as this will require me to determine, finally, the proper interpretation to be placed upon the provisions of the Contract relating to the circumstances in which the Principal can have recourse to the security. That is because, in most cases, the question, whether the beneficiary of the security is entitled to recourse to it in the circumstances that have occurred, is difficult to answer. To grant interim injunctive relief on the basis that it is merely arguable that the circumstances entitling the beneficiary to access the security had not arisen might, in many cases, defeat one of the purposes of the security, if it should turn out to have been intended to be what is known as a "risk allocation device" in addition to being a mere security.

The relevant clause

9. The critical issue is to interpret the clause claimed to entitle the Principal to have recourse to the security. It is Clause 5.6 of the Contract document, which is an altered version of the clause as it stands in the standard printed contract. It is as follows:

> "**5.6 Conversion of security and recourse to retention monies**
>
> The principal may have recourse to security, retention monies or both and may convert into money all or part of the security that does not consist of money <u>where the principal has become entitled to use the proceeds or the security in accordance with the terms of the contract.</u>
>
> The principal may use the proceeds of the security, retention monies or both in connection with any costs, expenses, losses or damages of any kind which the principal has incurred or claims that it has incurred or might in the future incur in connection with what the principal contends constitutes any act, default or omission of the contractor.
>
> (a) the party has given the other party notice in writing, for the period stated in Annexure Part A of the party's intention to have recourse to the security, retention monies or both; and
>
> (b) the period stated in Annexure Part A has or have elapsed since the notice was given".
>
> The purpose of notice under this clause 5.6 is to give the contractor an opportunity to remedy the circumstances giving rise to the proposed recourse to the security. The contractor covenants with the principal and it will not institute any proceedings whatsoever or exercise any rights or take any steps whatsoever to enjoin the issuer of any security or the Principal from having recourse to the security or in any way seek to restrain the Principal from exercising its rights under this clause 5.6."

(*my emphasis*)

10. Mr Whitten drew my attention to the respects in which this clause differs from the standard clause in the original published form of contract. In its original form, the clause was as follows:

> "**5.6 Conversion of security and recourse to retention monies**
>
> The Principal may have recourse to security, retention monies or both and may convert into money a Security that does not consist of money where -
>
> (a) the Principal has become entitled to exercise a right under the contract in respect of the security, retention monies or both;
>
> (b) The Principal has given the other party notice in writing, for the period stated in Annexure Part A or, if no period is stated, five days of the party's intention to have recourse to the security, retention monies or both; and
>
> (c) The period stated in Annexure Part A or, if no period is stated, five days, has or have elapsed since the notice was given".

The Law

11. I have looked at the large number of cases to which I was referred by counsel and the conclusions that I have drawn from them are as below.

12. The two purposes that may be served by a security clause in a building contract were described in the following terms by Callaway JA in *Fletcher Construction Australia Limited v Varnsdorf Pty Ltd* [1998] 3 VR 812 at 826–7:

> "There are broadly two reasons why the beneficiary may have stipulated for a guarantee. One is to provide security. If it has a valid claim and there are difficulties about recovering from the party in default, it has recourse against the bank. The second reason, which is additional to the first, is to allocate the risk as to who shall be out of pocket pending resolution of a dispute. The beneficiary is then able to call upon the guarantee even if it turns out, in the end, that the other party was not in default ... It is a question of construction of the underlying contract whether the guarantee is provided solely by way of security or also as a risk allocation device. Remembering that we are speaking of guarantees in the sense of standby letters of credit, performance bonds, guarantees in lieu of retention monies and the like, the latter purpose is often present and commercial practice plays a large part in construing the contract. No implication may be made that is inconsistent with an agreed allocation of risk as to who shall be out of pocket pending resolution of a dispute and clauses in the contract that do not expressly inhibit the beneficiary from calling upon the security should not be too readily construed to have that effect."

13. As to the construction of such a clause, a useful summary is to be found in the case of *Sugar Australia Pty Ltd v. Lend Lease Services Pty Ltd* [2015] VSCA 98 where Kaye J said (at para 138):

“138 The principles, relating to the construction of security clauses in construction, and similar, contracts, have been discussed in a number of the authorities. They were helpfully outlined by the Full Court of the Federal Court in *Clough Engineering* (2008) 249 ALR 458. For present purposes, the principles may be stated as follows:

(1) Subject to three principal exceptions, a court will not enjoin a party from recourse to a performance guarantee. Those exceptions are:

(a) The court will enjoin a party in whose favour the guarantee has been given from acting fraudulently.

(b) The court will enjoin such a party from acting unconscionably in contravention of the *Competition and Consumer Act 2010* (Cth).

(c) The court will restrain such a party from acting in breach of a contractual promise made by it not to call on the guarantee in particular circumstances (Ibid [77]; *Reed Construction Services Pty Ltd v Kheng Seng (Australia) Pty Ltd* (1999) 15 BCL 158, 164–5 (Austin J); *Ceresola TLS AG v Thiess Pty Ltd & John Holland* [2011] QSC 115 (Daubney J)).

(2) A recourse provision should be construed in light of all the other relevant provisions of the contract, including the terms of the security which formed part of the contract (*Clough Engineering* (2008) 249 ALR 458, 480 [85]; *Fletcher Construction* [1998] 3 VR 812, 828–9 (Callaway JA); *Bachmann Pty Ltd v BHP Power New Zealand Ltd* [1991] 1 VR 420, 435–7 (Brooking JA)).

(3) In construing any contractual limitation on the exercise by a party to have recourse to its rights to the security, the court should take into account the commercial purposes served by security clauses in construction contracts, and to which I have referred (*Clough Engineering* (2008) 249 ALR 458, 479).

(4) In particular, the commercial background for the contract informs the construction of a security clause, so that the court should not too readily favour a construction, which is inconsistent with an agreed allocation of risk as to who is to be out of pocket pending resolution of the dispute about breach (*Clough Engineering* (2008) 249 ALR 458, 479;*Fletcher Construction Australia Ltd v Varnsdorf Pty Ltd* [1998] 3 VR 812, 827 (Callaway JA); *Bachmann Pty Ltd v BHP Power New Zealand Ltd* [1998] VSCA 40; [1999] 1 VR 420, 436–7 [53] (Brooking JA)).

> (5) Accordingly, clear words are required to support a construction that inhibits a beneficiary of a security clause from calling on a performance guarantee where a breach is alleged in good faith (that is, non-fraudulently)" (*Clough Engineering* (2008) 249 ALR 458, 480).

14. In *Fletcher Construction Australia Limited v Varnsdorf Pty Ltd* [1998] 3 VR 812, the contract (cl 3.13) provided that, if the Contractor had not brought certain plant to a state of handover by the due date, it was obliged to pay time damages at a prescribed rate. The owner could deduct those damages from any amount due from it to the contractor under the contract and, if that was insufficient, the Contractor was required to pay the balance within 10 business days of delivery of a notice from the owner demanding payment. If it failed to pay the balance within that period the owner could have recourse to the security to obtain the balance.

15. The owner contended that it was entitled to time damages and served a notice and, although the court accepted that there was a dispute as to whether handover had been achieved, it was held that the owner was entitled to have recourse to the security, because the notice was served as required and the purpose of the security was to allocate the risk as to who should be out of pocket pending resolution of the dispute.

16. In *Bachmann Pty Ltd v BHP Power New Zealand Limited* [1998] VSCA 40 the relevant clause was:

> "A party shall not convert into money security that does not consist of money until the party becomes entitled to exercise a right under the contract in respect of the security. The party shall not be liable for any loss occasioned by conversion pursuant to the contract".

17. Brooking JA considered that this clause qualified the purchaser's power to have recourse to the security. The only provision of the contract, which entitled the purchaser to exercise a right in respect of the security, was Clause 22.4 of the General Conditions, which provided:

> "The purchaser may deduct from monies otherwise due to the supplier any monies due from the supplier to the purchaser and if those monies are insufficient the purchaser can have recourse to the security under the contract."

18. As to this, the learned judge said (at para.53):

> "In the present case the matters of conversion of and recourse to the security are dealt with by two general conditions, which should if possible be construed so as to work in harmony. Clause 5.5 prohibits conversion into money until the purchaser becomes entitled to exercise a right under the contract in respect of the security. Clause 22.4 entitles the purchaser to deduct from moneys otherwise due to the supplier any moneys due from the supplier to the purchaser and, if those moneys are insufficient, entitles the purchaser to have recourse to the security. Like Clause 3.13(b) in *Fletcher*, it confers a right of

recourse against the security to obtain the balance if the exercise of the right of set-off which it also confers leaves a balance outstanding in favour of the purchaser. It would, as Charles, J.A. said in *Fletcher*, be strange if the clauses concerned in that case and this - Clause 3.13(b) and Clause 22.4 - conferred the practical right of recourse only where moneys were "due" from the supplier to the purchaser in some such sense as actually or indisputably due. I would treat Clauses 5.5 and 22.4 of the present contract, read in conjunction, as entitling the purchaser, as between itself and the supplier, to have recourse to the security where according to a bona fide claim made by the purchaser moneys are due to it from the supplier which exceed any moneys due from it to the supplier."

19. That the outcome of any case turns on the wording of the particular clause was emphasised by Byrne J. in *Rejan Constructions Pty Ltd v. Manningham Medical Centre* [2002] VSC 579, the principal authority relied upon by Mr Roberts.

20. In that case, the form of contract used was, as here, AS4300-1995 except that Clause 5.6 was unaltered. The principal sought to have recourse to the security following termination of the building contract in order to compensate it for alleged losses that it claimed. After noting that the clause conferred upon the principal rights with respect to the security when it became entitled to exercise all any of its rights under the contract in respect of the security, his Honour said (at para 30):

> "30. Brooking JA, in the passage from the *Bachmann* case which I have quoted, places some emphasis upon the reasoning of the Court of Appeal in the *Fletcher Construction* case. This case involved the construction of a contract very different from the present; it contained no comparable qualification upon the right to convert or to have recourse to the non-cash security. It does not appear to be a Standards Australia form of contract or, indeed, any of the standard forms then in use. Clause 3.13 in that case permitted the principal to have recourse to the security where the contractor was obliged to pay liquidated damages for late completion and where it failed to do so. In these circumstances, it is, with respect, scarcely surprising that counsel for the contractor was unable to persuade the court to infer in the contract a term which enabled the Contractor to prevent the principal from converting the security into money so as to give effect to cl. 3.13."

21. He pointed out that the right which triggered the operation of Clause 5.6 in the case before him was not a right of payment but rather, a right under the contract in respect of the security. An interlocutory injunction was therefore granted.

22. In *Clough Engineering Ltd v Oil & Natural Gas Corporation Ltd* [2008] FCAFC 136 the relevant clause provided:

> "3.3.3 The Company shall have the right under this guarantee to invoke the Banker's guarantee and claim the amount there under [sic] in the event of the Contractor failing to honour any of the commitments entered into under this Contract."

23. The Full Federal Court said (at para. 99):

> "Here, the terms of cl 3.3 of the contract, read with cl 2 of the guarantee, show that the commercial purpose of the contract was to allocate the risk of who should be out of pocket notwithstanding that there may be a genuine dispute as to whether Clough had failed to honour commitments under the contract. The risk was allocated to Clough, there being no clear words to inhibit ONGC as a beneficiary of the guarantee from invoking it: *Fletcher Construction* at [821] and [827]".

24. It should be noted that, in that case, Clause 2 of the guarantee was read together with Clause 3.3 of the contract because the contract in that case required the guarantee to be in the form set out in an appendix to the contract. As a consequence, the principal was entitled to have access to the guarantee upon demand made by it to the bank without any proof that the amount claimed was due and payable and notwithstanding any dispute as to that amount before the Court.

25. In *Thiess Pty Ltd v. Pacific National (Victoria) Pty Ltd* [2009] VSC 670 an interlocutory injunction was granted to restrain the enforcement of an unconditional performance bond from a bank where the beneficiary of the bond claimed to have suffered loss from work carried out under the contract. The injunction was granted because the court found that the wording of the clause suggested that the parties intended to limit the right of the beneficiary to call up the security until all outstanding issues between the parties under the agreement were resolved.

26. In *Central Petroleum Ltd v. Century Energy Services Pty Ltd* [2011] WASC 211, the relevant clause stated:

> "34.2 Banker's Undertaking purpose and call down procedure
>
> (a) The purpose of the Banker's Undertaking is to ensure payment due by the Company to the Contractor of all amounts due under this Document.
>
> (b) Prior to being entitled to request payment of the Banker's Undertaking:
>
> (i) the Contractor must be due a payment from the Company which remains unpaid and outstanding under the terms of this Document;
>
> (ii) the Contractor must provide the Company with written notice <u>asserting an amount is due and outstanding</u>; and
>
> (iii) 5 Business Days has passed since the Contractor's notice under clause 34.2(b)(iii) [sic (ii)] was

received by the Company and the amount due and outstanding has not been paid." *(my emphasis)*

27. The defendant sought to have recourse to the bank's undertaking to recover a liquidated sum that it claimed was due. The Plaintiff cross-claimed for substantial unliquidated damages. The judge held that, on its proper interpretation, the clause was a risk allocation provision as to who should be out of pocket pending the resolution of a dispute between the parties. The injunction was therefore refused.

28. In *Lucas Stuart Pty Ltd v. Hemmes Hermitage Pty Ltd* [2010] NSWCA 283, the relevant clause provided that the respondent may call upon the guarantee if the appellant failed to comply with the terms of a notice given under a clause in the following terms:

> "16.2 If the contractor has not materially complied with its obligations under this contract, the principal may give a written notice to the contractor stating:
>
> 16.2.1 The contractor's breach.
>
> 16.2.2 What the principal requires the contractor to do to remedy the breach.
>
> 16.2.3 A specific reasonable time in which the contractor must remedy the breach".

29. The court held that satisfaction of the condition precedent to the service of the notice would occur only if the applicant had not materially complied with its obligations under the contract. That was not established and so there was a serious question to be tried in that regard. The court also noted that certificates of practical completion had been issued by the Project Director for each of the three stages of the project.

30. In that case, in a judgment with which Campbell JA agreed, Macfarlan JA said (at paras 37–43):

> "37 The primary judge relied upon the decision in *Clough Engineering Ltd v Oil & Natural Gas Corporation Ltd [No 3]* [2007] FCA 2082 and, on appeal, at [2008] FCAFC 136; (2008) 249 ALR 458, in support of this view. In that case the Full Federal Court placed considerable weight upon the fact that the clause there under consideration required provision of a performance guarantee in the form of that set out in an appendix and that the form referred to the payment by the guarantor "notwithstanding any dispute(s) pending", without reference to the contractor and "without any demur, reservation, contest or protest" (249 ALR 458 at [30] and [88] – …). Whilst the Clause pursuant to which the bonds were provided in the present case (Clause 6.1) refers to "unconditional undertakings" the Contract does not contain any wording such as was contained in the *pro* forma performance bond regarded in *Clough* as effectively

qualifying the terms of the condition precedent stated in the relevant clause. *Clough* is accordingly distinguishable.

38 Because *Clough* is distinguishable and its correctness was not fully debated before this Court, I refrain from expressing a concluded view as to its correctness. It is appropriate however for me to indicate that I have reservations about its correctness.

39 There are at least two principal goals that parties may seek to achieve by requiring that performance bonds be provided by a contractor to a principal in circumstances such as the present.

40 One is to provide security in the event of the insolvency of the contractor. The other is to enable the principal to obtain prompt payment of amounts it claims, notwithstanding disputes raised by the contractor. Not every contract seeks to achieve both goals. The present is one in which only the first is sought to be achieved. To assist in achieving the first goal the Contract thus states that the bonds to be provided are to be "unconditional", with the consequence that the issuer is obliged to pay, without argument, if called upon by the respondent to do so.

41 So far as the second goal is concerned, Clause 16.2 however only entitles the respondent to call upon the bonds if, as a matter of objective fact, the applicant "has not materially complied with its obligations". Accordingly, it is open, as has occurred here, for the applicant to seek to restrain the respondent from calling upon the bonds upon the basis that the pre-condition has, at least arguably, not been satisfied.

42 The position would have been different if Clause 16.1 had made the respondent's entitlement to call upon the bonds dependent on the respondent's satisfaction or even simply upon the respondent's assertion that the applicant was in breach of the Contract. Provisions of this type would have gone a long way to achieving the second of the goals to which I have referred above.

43 My reservation about the decision in *Clough* is as to whether the contract in that case can truly be regarded as having been intended to achieve both purposes. Certainly the terms of the performance guarantee that the Full Court relied upon made it clear that the issuer of the guarantee could not withhold payment if a proper call were made but the condition precedent to the principal's right to call upon the guarantee was expressed in terms of objective fact, that is, "in the event of the Contractor failing to honour any of the commitments entered into under this Contract" (see clause 3.3.3 quoted at 249 ALR 458 at [24]). It is not obvious to me why the terms of the guarantee given by the issuer should have been regarded as affecting the proper construction of this provision

> which related to the circumstances in which the Principal was entitled to call on the guarantee."

31. In *Redline Contracting Pty Ltd v. MCC Mining (Western Australia) Pty Ltd* 6 January 2012 security was provided by the applicant under a pipeline construction contract. The respondent sought recourse against the security with respect to unpaid fuel invoices and interest. Recourse against the security was subject to Clause 5.2 of the agreement which provided as follows:

> "5.2 Recourse
>
> Security shall be subject to recourse by a party who remains unpaid after the time for payment where at least 5 days have elapsed since that party notified the other party of intention to have recourse."

32. The issue in the case was whether these words comprise an implied negative stipulation which prevented the respondent from seeking recourse against the security. The applicant argued that the words "time for payment" should be construed as referring to a sum which was "due and payable" and therefore did not contemplate a circumstance where the respondent could seek recourse in support of a disputed claim for liquidated damages. The respondent contended that it was a risk allocation clause.

33. In refusing the injunction, the judge considered it significant that the clause did not require the sum claimed to be "payable" or "due" or otherwise regulate the circumstances in which the respondent could have access to the security. He also noted that he was bound by the decision in *Clough*. He said that it was likely that the clause was a risk allocation clause and that it was sufficient that the respondent bona fide believed that it had a genuine claim.

34. In *Otter Group Pty Ltd v. Maria Margaret Wylaars and anor* [2013] VSC 98 the security was given by a tenant under a lease which made specific provision for the landlord to have access to the security during the tenancy and for the tenant to make good from time to time any resulting deficiency in the amount of the security. Unsurprisingly, since there was no contractual limit on the landlord's ability to draw down on the security, it was held that she was entitled to do so with respect to a bona fide claim without first having to prove her entitlement at trial. In the course of refusing injunctive relief Hollingworth J referred to a number of authorities including *Clough* and said that, insofar as *Rejan* was inconsistent with other authorities to which she referred, it should not be followed. However she did not say what the inconsistencies were.

35. In *Sugar Australia Pty Ltd v. Lend Lease Services Pty Ltd* [2015] VSCA 58, the contract was an amended version of the General Conditions of AS 4910 2002. The security clause in that case was as follows:

> "Any security provided by the Contractor in accordance with the Contract shall be available to the Principal whenever the Principal may claim (acting reasonably) to be entitled to:

> (i) the payment of monies or an indemnity by the Contractor under or in consequence of or in connection with the Contract;
>
> (ii) reimbursement of any monies paid to others under or in connection with the Contract; or
>
> (iii) other monies payable by the Contractor to the Principal (whether by way of set off or otherwise).
>
> Recourse to security shall only be subject to the Principal having given the Contractor five days' notice of its intention to have recourse to the security for the purpose of allowing the Contractor to replace the security with cash where it has been issued in a form other than cash. Where the Principal has recourse to security in accordance with clause 37.3, the Contractor shall provide replacement security in accordance with clause 37.3."

36. The appellant principal sought recourse against the security with respect to liquidated damages that had been certified by the superintendent. It contended that the words 'acting reasonably' involved a solely subjective element to be determined by reference to its motive in making the claim for the payment, so that the words 'acting reasonably' only required it to demonstrate it had a bona fide arguable claim for an amount equal to or in excess of the amount of the security. Alternatively, it argued that if 'acting reasonably' had an objective element, the respondent would need to establish that no reasonable person in the position of the appellant would have formed the view that it had a claim to the payment.

37. In holding that the construction of the clause was a critical issue that should have been finally determined at the interlocutory hearing for injunctive relief, Kaye AJ said (at para 120):

> "120 In the present case, it is not suggested that the construction of GC 5.2 would involve or require evidence as to the factual matrix in which the contract was concluded…. The construction of clause 5.2 is a discrete question, which did not involve consideration of any detailed or complex material. The resolution of the application before the court was not urgent, as the respondent's rights had been protected by an interim injunction. While it was important that the judge deliver his decision expeditiously, nevertheless the judge did have some time to consider the issues raised by the parties before him."

38. The court held that, on the proper interpretation of the clause, the entitlement to the payment, indemnity or reimbursement referred to did not have to be demonstrated by the appellant, provided that it had a 'claim' to such an entitlement and "acted reasonably" in an objective sense, based on the information and facts that it knew or ought to have known at the time.

39. In *RCR O'Donnell Griffin Pty Ltd v Forge Group Power Pty Ltd (rec and mgr appt) (in liq)* [2016] QCA 214, the contract was an amended version of

the General Conditions of Contract AS 4902-2000. The security clause was as follows:

> "*Security* shall be subject to recourse by a party who remains unpaid after the time for payment where at least 5 days have elapsed since that party notified the other party of intention to have recourse."

40. In that case the principal sought recourse to the security to satisfy its claim for an amount of liquidated damages that had been certified by the superintendent at a time when it (the principal) was in liquidation and, under the terms of the contract, there was a much greater sum due to be paid by the principal to the subcontractor pursuant to a progress claim was then outstanding. The contract contained a provision for the set-off by the principal of liquidated damages against a progress claim.

41. It was held that the clause did not provide recourse to the security unless the principal in that case was able to establish that money was due and unpaid by the subcontractor to it. In the majority judgment, Philip McMurdo AJ said (at para 95):

> "By cl 5.2 of the Subcontract in this case, the security was subject to recourse "where [the Principal] remains unpaid after the time for payment." On the ordinary meaning of those words, the precondition to recourse to the security was the fact of money being unpaid to the Principal. Clause 5.2 was not in terms which referred to a belief, or grounds for a belief, that money remained unpaid. Because recourse to the security was permitted only where in fact money remained unpaid, in my view it was necessarily implied that recourse was not permitted, and that the Principal should not attempt to have recourse to the security, where there was not money which remained unpaid to it. There was thereby a negative stipulation which could be the basis for an injunction restraining Forge from making demand on the bank guarantees."

42. In the following paragraph, the learned judge noted that, in the case before him, the right to the payment sought by the principal was to be established at trial and as a consequence, he said that, even if the clause was a risk allocation clause:

> "The implication that a security could be called upon merely where there was a claim in good faith could have no operation once the absence of merit in that claim was established."

43. In *CPB Contractors Pty Ltd v. JKC Australia LNG Pty Ltd (No.2)* [2017] WASCA 123 the relevant clauses to be construed were as follows:

> "GC 35.3 (a) Contractor may have recourse to the Bank Guarantee(s) at any time in order to recover any amounts that are payable by Subcontractor to Contractor on demand.

(b) Subcontractor waives any right that it may have to obtain an injunction or any other remedy or right against any party in respect of Contractor having recourse to the Bank Guarantee(s).

GC 35.4

(a) If Contractor calls on a Bank Guarantee or a Parent Company Guarantee at any time, the balance of the proceeds (if any) after deducting amounts due and payable to Contractor by Subcontractor must be deposited by Contractor into an interest bearing account with an Australian bank (as defined in the *Corporations Act 2001* (Cth)) in the name of Contractor.

(b) Any interest accrued on the account balance must be retained by Contractor in the account and added to the balance of the proceeds held.

(c) Contractor is entitled to withdraw from the account amounts due and payable to it by Subcontractor from time to time."

44. Recourse to the security in that case was sought in order to recover substantial liquidated damages claimed by the contractor. Although the court considered that the attempted ouster of its jurisdiction was unenforceable, it found that it was a material factor in determining whether the clause was a risk allocation clause, particularly given the possibility of the security expiring before the contractual right to liquidated damages could be finally established.

45. It was not considered that the words "on demand" and "due and payable" required a claim be established before recourse could be had to the security.

46. In *H. Troon Pty Ltd v. Marysville Hotel and Conference Centre Pty Ltd* [2017] VSC 470 the contract was an amended Australian Standard AS 2124-1992 contract in which Clause 5.5 of the standard form was deleted and replaced with the following:

"5.5 The Principal may make a demand on and use any security and/or retention moneys:

(a) to pay for any costs, expenses, loss or damage which the Principal claims it has incurred, or might in the future incur, as a consequence of any act or omission of the Contractor which the Principal asserts constitutes a breach of the Contract by the Contractor;

(b) to satisfy any amount which the Principal asserts is payable by the Contractor pursuant to the Contract;

(c) in the event of:

(i) a termination of the Contract, except where the Contract is terminated by the Principal under Clause 45A; or

(ii) an event described in Clause 44.11 affecting the Contractor; or

(d) as otherwise provided for under the Contract."

47. The principal sought recourse to the security on account of a substantial claim that it had made with respect to alleged defects in the work and had agreed to return to the contractor the balance of the security after satisfying that claim. In holding that the principal is entitled to recourse against the security, Digby J said (at paras 93 -4):

> "93 However, Clause 5.5 qualifies the Principal's claims by providing that the subject claims are claims for cost, expense, loss or damage incurred or which might be incurred in the future as a consequence of any act or omission of the Contractor which the Principal asserts constitutes a breach of the Contract by the Contractor. The parties' express requirement that the Principal's entitlement to recourse need only be triggered by such "claims" by the Principal, and which the Principal "asserts constitute a breach of the Contract by the Contractor" clearly reflects the parties' intent that the Principal may access the security without having to establish any relevant breach of Contract by the Contractor or the existence of any relevant extant contractual claim or entitlement in the Principal.
>
> 94 The Contract reflects a scheme and specific intent via Clause 5, including Clause 5.5, to allocate to the plaintiff the risk as to which of the parties to the Contract shall be out of pocket pending final determination of any dispute in respect of any costs, expenses, loss or damage which the Principal claims has been incurred, or which the Principal claims might be incurred in the future, as a consequence of the Contractor's acts or omissions which the Principal asserts constitutes a breach."

48. In *Dedert Corporation v United Dalby Bio-Refinery Pty Ltd* [2017] VSCA 368 the Contract used was an amended form of the General Conditions of Contract AS 4902-2000. The relevant security clause was as follows:

> **"5. SECURITY**
>
> **5.1 Provision**
>
> *Security* shall be provided in accordance with *Item* 14 or 15. All delivered security, other than cash or retention moneys, shall be transferred in *escrow*.
>
> **5.2 Recourse**
>
> *Security* shall be subject to recourse by a party who remains unpaid after the time for payment where at least 5 days have elapsed since that party notified the other party of intention to have recourse.
>
> ...

5.4 Reduction and release

Within 14 days of the *date of practical completion,* the *Principal* will release and return letter of credit 1 (see item 14) to the *Contractor.*

Upon payment of any amount of the *Lump Sum Amount* to the *Contractor,* the *Contractor's* entitlement to security shall be reduced by the percentage or amount In *Item* l5(d) and the reduction shall be released and returned within 14 days to the *Principal.*

A party's entitlement otherwise to *security* shall cease 14 days after *final certificate.* Upon a party's entitlement to *security* ceasing, that party shall release and return forthwith the *security* to the other party."

49. The contract contained three clauses which specifically provided for recourse by the respondent to the security, namely, Clause 5.2, Clause 39.7 and Clause 39.9. The last two of these were as follows:

"**39.7 Set off**

The Principal may set-off any amount due and payable by the Contractor to the Principal against any amount that the Principal owes the Contractor under the Contract.

If the moneys payable to the Contractor are insufficient to discharge the liability of the Contractor to pay such sum to the Principal, the Principal may have recourse to the security provided by the Contractor.

39.9 Recourse for unpaid moneys

Where, within the time provided by the *Contract*, the *Contractor* fails to pay the Principal an amount due and payable under the Contract, the Principal may have recourse to security under the Contract and any deficiency remaining may be recovered by the Principal as a debt due and payable from the Contractor to the Principal."

50. As Kaye J pointed out, both Clauses 39.7 and 39.9 were only engaged where, pursuant to their terms, an amount had been certified by the Superintendent, or was otherwise provided by the contract, to be 'due and payable' by the contractor to the principal. He said (at para. 105):

"105 The first question, then, is whether the contract contained a relevant qualification or restriction on the right of the respondent to have recourse to the guarantee. In my view, it is plain that the contract does contain such a qualification. Apart from cl 39.7 and cl 39.9, which do not apply in this case, the only other provision, contained in the contract, entitling the respondent to have recourse to the security, is cl 5.2. That clause contained the express prescription that recourse is

permitted where a party 'remains unpaid after the time of payment'. That requirement constituted a contractual qualification on the respondent's powers in relation to the exercise of the security. In terms of the authorities, it was an implied negative stipulation in the contract that the respondent would not invoke recourse to the security in the absence of there being an account 'unpaid' by the applicant to the respondent 'after the time for payment'."

51. Distinguishing the decision in *Backman*, he said (at para 134 et seq.):

> "134 The foregoing analysis of the judgment of Brooking JA, in *Bachmann*, reveals that there were three important factors which distinguish the contract in *Bachmann* from the contract in the present case.
>
> 135 First, and obviously, the relevant conditions of the contract in *Bachmann*, entitling the purchaser to have recourse to the security in that case, were expressed in different and distinct terms than cl 5.2 in this case. In *Bachmann*, cl 5.5 and cl 22 of the contract were capable of being construed, in a manner that was workable, to provide recourse to the purchaser to the security where the purchaser had a 'bona fide claim' that monies were due to it from the supplier. By contrast, in this case, if a similar approach were adopted to the construction of cl 5.2, it would not assist the respondent in the same way. A construction of cl 5.2, entitling the respondent to have access to the security where the respondent has a 'bona fide claim' that monies remained 'unpaid after the time for payment' (of those monies), would beg the questions, first, as to what monies 'remain unpaid', and, secondly, as to what the time for payment of those monies is.
>
> 136 Secondly, in *Bachmann*, Brooking JA was substantially exercised by the circumstance that, unless cl 5.5 only required the purchaser to make a bona fide claim, it could readily be rendered unworkable by any dispute raised by the supplier to the claim made by the purchaser. On the other hand, in the present case, as discussed, the contract contained a number of provisions by which monies could be made 'due and payable' by the applicant to the respondent in the absence of any adjudication in respect of a claim made by the respondent for that payment. In that way, the requirement in cl 5.2, that the money claimed by the respondent will remain 'unpaid after the time for payment', connected with other contractual mechanisms by which money might become due and payable by the applicant to the respondent under the contract.
>
> 137 The third point of distinction between the two cases is that, in *Bachmann*, one of the forms of security recognised in cl 5.3 of the contract was an approved undertaking in the form of an unconditional promise to pay on demand without reference to the supplier. The contract between the applicant and the

> respondent does not contain any such corresponding approved form of security. The provision, in *Bachmann*, of an approved form of security, payable on demand by the purchaser without reference to the supplier, was — as stated by Brooking JA — supportive of the conclusion that the parties contemplated that it was the supplier who should be out of pocket pending the resolution of any dispute between the parties."

52. He said that the essential features of the contract, in *Clough*, were that the principal in that case was entitled to have access to the guarantee upon demand made by it to the bank, without any proof the amount claimed was due and payable, and notwithstanding any dispute as to that amount before the Court.

What to make of the authorities

53. From the foregoing authorities it is apparent that each case turns upon its own facts and the wording of the particular contract. The authorities however serve as useful guidance as to what factors are considered relevant.

54. As between the beneficiary of the security and the bank or other financial institution that is to provide the money, the right to recourse is usually unconditional. However that is not a relevant factor in interpreting the right to access as between the beneficiary and the party that provides the security except, it seems, where the terms of the security are part of the contract itself, as in *Clough*.

The Principal's claim

55. In the present case recourse is sought to the security in order to recover liquidated damages claimed by the Principal in addition to those the Supervisor has determined to be due. The basis of the claim is said to be an expert's report prepared by a Mr Heazlewood of Time Planning and Programming Pty Ltd, a company based in New South Wales. This report is Exhibit "AV12" to the affidavit of Alexander Voldman, affirmed 23 April 2018 and filed herein.

56. Mr Heazlewood concluded that the Contractor was only entitled to 63 days total delay and that the Principal was entitled to 137 days of liquidated damages. This is contrary to determinations that the Supervisor made of both the Contractor's extension of time claims and the Principal's liquidated damages. The Superintendent was the person appointed under the contract to determine such a claim and was someone whom one would expect would have an intimate knowledge of the circumstances.

57. Liquidated damages are provided for by Clause 35.6 of the Contract, which is as follows:

> "**Liquidated damages for delay in reaching practical completion**
>
> If the contractor fails to reach Practical Completion by the Date for Practical Completion, the contractor shall be indebted to the principal

for liquidated damages at the rate stated in Annexure Part A for every day after the Date for Practical Completion to and including the Date of Practical Completion or the date that the Contract is terminated pursuant to Clause 44, whichever first occurs.

The Principal may recover liquidated damages progressively following the Date for Practical Completion:

(a) on demand from the Contractor; or

(b) by deducting such amount from any amount certified by the Superintendent under Clause 42.1 or from any security held under clause 5,

notwithstanding that Practical Completion has not occurred."

58. By Clause 2 and paragraph 9 of Schedule A, the Date for Practical Completion under the Contract was 28 October 2016, but if any extension of the time for Practical Completion should be granted by the Superintendent, it would be the date resulting from such an extension.

59. The Builder applied for a number of extensions of time and, on about 3 July 2017, the Superintendent issued a determination with respect to the Builder's claims, allowing a total adjustment in its favour of 94 days. As a consequence, the Date for Practical Completion became 20 April 2017.

60. On 29 June 2017 the Superintendent issued a Certificate of Practical Completion, certifying that practical completion was achieved on 27 June 2017.

61. As part of his determination of the Contractor's claims for extensions of time and in response to a request by the Principal for a determination as to the liquidated damages payable to it under the Contract, the Superintendent determined that, since Practical Completion was achieved on 27 June 2017, the Principal was entitled to liquidated damages for 69 days which, at the contract rate of $4,000.00 per day, amounted to $276,000.00.

62. Both the Principal and the Contractor have served notices of dispute pursuant to Clause 47.1 of the contract concerning this determination which have not yet been resolved.

Payment of $276,000

63. Clause 42.1 sets out the procedure for payment claims certificates. Claims for payment are to be made by the Contractor in accordance with that clause, they are required to be assessed by the Superintendent who is then to issue to both the Principal and the Contractor a payment certificate stating the amount of the payment be made by one party to the other. The certificate is to set out the Superintendent's calculations in arriving at the amount certified and, if it is more or less than the amount claimed by the Contractor, the reasons for the difference.

64. Following the determination, although no certificate has been issued by the Superintendent, the Principal threatened to have recourse to the security in

order to recover the amount of $276,000.00 assessed by the Superintendent unless it was paid by the contractor. After some negotiation, on 9 March 2018, the contractor paid to the principal the sum of $276,000.00 in exchange for the return of two of the four guarantees, totalling one half of the total sum.

65. The Contractor has since submitted further claims to the Superintendent on 14 February 2018 for a variation and an extension of time but, by letter dated 6 March 2018 the Superintendent determined that the Contractor was not entitled to the variation or the further extension of time. This further determination is the subject of a further notice of dispute from the Contractor pursuant to Clause 47.1.

66. On 11 April 2018 the Principal served a notice under Clause 5.6, stating that unless the Contractor paid to it a further amount of $272,000.00 for additional liquidated damages that it claimed beyond the $276,000 already paid, it would have recourse to the remaining guarantees. It was in response to that notice that this proceeding is brought.

How the clause should be interpreted

67. In *Dedert*, Priest JA adopted (at para 51) the following passage from the joint judgment of French CJ Nettle and Gordon JJ in in *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* (2015) 256 CLR 104 (at para 51) as follows:

> "The rights and liabilities of parties under a provision of a contract are determined objectively, by reference to its text, context (the entire text of the contract as well as any contract, document or statutory provision referred to in the text of the contract) and purpose.
>
> In determining the meaning of the terms of a commercial contract, it is necessary to ask what a reasonable businessperson would have understood those terms to mean. That inquiry will require consideration of the language used by the parties in the contract, the circumstances addressed by the contract and the commercial purpose or objects to be secured by the contract.
>
> Ordinarily, this process of construction is possible by reference to the contract alone. Indeed, if an expression in a contract is unambiguous or susceptible of only one meaning, evidence of surrounding circumstances (events, circumstances and things external to the contract) cannot be adduced to contradict its plain meaning.
>
> However, sometimes, recourse to events, circumstances and things external to the contract is necessary. ..."

68. Mr Roberts submitted that the parties had decided that the risk allocation was such that the Principal may only have recourse to the security where it has become entitled pursuant to the terms of the contract. He said that, unlike many of the cases referred to above, the requirement in the present case was an unambiguous and absolute in its terms. He said that, in order to

be able to have recourse to the security the Principal must demonstrate that it has a present contract entitlement.

69. Mr Roberts pointed out that the Principal's current contractual entitlement in regard to liquidated damages had already been determined by the Superintendent in his two determinations and that, even though no certificate had been issued so as to entitle the Principal to payment of the amount assessed, the Contractor had nonetheless paid it. He said that the mere possibility that the Superintendent's determination might be disturbed in the future does not justify the Principal in having recourse to the security now.

70. Mr Whitten submitted that the fact that the Principal's claim for the additional liquidated damages has not been certified by the Superintendent does not constitute any breach by the Principal of a negative stipulation in the contract in relation to recourse. He referred me to Clauses 42.8 and 42.9 and said that on a plain reading of those provisions, together with Clauses 5.6 and 35.6, the Principal's right to recourse against the security does not require a certified or determined amount. Instead, he said, it arises on a claim by the Principal for any costs, expenses, losses or damages of any kind incurred or which it might incur in the future, as a result of what the Principal contends constitutes any act, default or omission by the Contractor.

71. The commercial purpose or object to be secured by this part of the contract might have been simply to confer security or it might have been intended to serve the secondary purpose of allocating risk pending the determination of the parties' respective entitlements. To determine which of these was intended requires a careful examination of the clauses referred to and the contract as a whole.

72. Clause 42.8 provides as follows:

> "**Set offs by the Principal**
>
> Without limiting the Principal's other rights and remedies under the Contract or otherwise, the principal may at any time and from time to time deduct from monies otherwise due to the contractor (including from an amount certified in a payment certificate) any money due from the contractor to the principal (including liquidated damages under clause 35.6) whether under the contract or otherwise and if those monies are insufficient, the principal may, subject to clause 5.6, have recourse to retention monies and, if they are insufficient, then to security under the Contract."

73. The words "or otherwise" indicate that the principal may set-off amounts due from the contractor otherwise than under the Contract. However this is a right of set-off and does not purport to confer a right to make ex-contractual demands on the Contractor otherwise than by way of set-off. The right of recourse to the security is otherwise subject to Clause 5.6.

74. Clause 42.9 provides as follows:

> "**Recourse for unpaid moneys**
>
> Where, within the time provided by the contract, a party fails to pay the other party an amount due and payable under the contract, the other party may, subject to 5.6, have recourse to retention monies, if any, and, if those monies are insufficient, then to security under the contract and any deficiency remaining may be recovered by the other party as a debt due and payable."

75. By its clear wording, the right of recourse conferred by this clause is confined to monies that are "…due and payable under the contract" that have not been paid "…within the time provided by the contract." It does not allow the Principal to have recourse with respect to monies payable otherwise than under the contract.

Clause 5.6

76. Turning now to Clause 5.6, it will be seen that there are two substantive paragraphs, followed by two sub paragraphs and then a final paragraph having two parts.

77. Mr Whitten submitted that I should read the first two paragraphs as though they were one, so that the much wider circumstances in paragraph 2, referring to the use of the money, can be applied to expand the circumstances in which recourse can be had to the security under paragraph 1. I can see no justification for doing that. The parties have set these two paragraphs out in their contract as separate paragraphs and I must read them and interpret them objectively as they appear in the contract. Further, read separately, they make sense but they do not really well together.

78. The opening paragraph of Clause 5.6, provides that the Principal may have recourse to the security and may convert into money any part of the security that does not consist of money, where the Principal has become entitled to use the proceeds or the security in accordance with the terms of the contract.

79. Taking that paragraph on its own, the Principal must have become entitled under the terms of the contract in order to have recourse to security. If there is no such entitlement under the terms of the contract, there is no entitlement to have recourse to the security.

80. The second paragraph of the clause provides that the Principal may use the proceeds of the security in connection with any costs, expenses, losses or damages of any kind which the Principal has incurred or claims that it has incurred or might in the future incur in connection with what the Principal contends constitutes any act, default or omission of the Contractor. This provision is very wide but, by its terms, it is concerned with how the

Principal is to use the money, not the circumstances in which it is permitted to have recourse to the security in the first place.

81. There appears to be a word (possibly "where") missing immediately before subclauses (a) and (b) but it is common ground that the Principal would be required to give notice to the Contractor in accordance with the subclauses.

82. The final paragraph has two limbs. The first is a statement stating that the purpose of the notice is to give the Contractor an opportunity to remedy "the circumstances" giving rise to the proposed recourse to the security. I think that is neutral in the sense that it could equally apply whether the clause is merely a security or also a cost allocation clause. The second part is a covenant by the Contractor not to institute any proceedings to restrain recourse to the security which, on the above authorities, is interpreted to be an indication that the parties intended that access to the security should be unrestricted in the sense referred to. I accept that is the case, but the Principal must nonetheless be entitled under the terms of the contract, when interpreted, to have recourse to the security.

83. It seems to me that the clear language used in the foregoing provisions would be understood by a reasonable businessperson to mean what it says. To be entitled to have recourse against security the Principal must have an entitlement to payment under the terms of the contract.

Is there an entitlement under the contract?

84. By Clause 35.6, the Contractor shall be indebted to the Principal for liquidated damages if it fails to reach Practical Completion by the Date for Practical Completion. Under the terms of the contract, the Date for Practical Completion under the contract, is the date as defined in Clause 2 which, by reason of a determination made by the Superintendent, is 20 April 2017. Until such time as that is changed by a further determination or adjudication, it is not possible to say that any other date is the Date for Practical Completion.

85. Further, the Superintendent has issued a Certificate of Practical Completion, certifying that practical completion was achieved on 27 June 2017 and Mr Heazlewood's report would suggest that the Principal does not dispute that.

86. Of course it is possible that, as a result of the notice of dispute served by the Principal, the determination of the Superintendent might not stand and a different date might become the Date for Practical Completion. However at the present time, that is what the Date for Practical Completion has been determined to be. Consequently, it is not possible to say that the amount now sought to be recovered from the security by the Principal is due under the contract. That is fatal to the claim for recourse against the security.

The balance of convenience

87. In his affidavit sworn 13 April 2018, Mr Grills said that he was concerned that, if recourse were had to the security, it would significantly damage the

Contractor's relationship with the bank. He was also concerned that the Contractor's reputation in the building industry would be severely impacted in that its current client developers may lose confidence in its ability to meet its obligations and may also prevent the Contractor from winning further work. He said that the Contractor's current projects will work in excess of $180 million.

88. Mr Whitten raised doubts concerning reputational harm and referred me to some judicial comments in that respect. He said that the Principal had suffered significant financial losses as a result of the delay. That is something that has already been determined by the Superintendent, although since a final certificate has not yet been granted it is possible that that determination might change.

89. There is also an issue as to the future capacity of the Principal to repay any overpayment in the future. Mr Grills deposed that it was a project-specific company and it appears that the units in the development apart from a commercial unit have been disposed of.

90. I think the balance of convenience favours granting an injunction.

91. Further, as foreshadowed earlier, the determination that I have made concerning the interpretation of the relevant clauses of the contract is final for the purposes of the current proceeding. It therefore appears that it is unnecessary to consider the question of balance of convenience. In *Debert*, Kaye AJ said (at para 147:

> "147 Although, as mentioned, the application before the judge was for an interlocutory injunction, I have reached a concluded view as to the correct construction of the contract between the parties. In those circumstances, the question of which side is favoured by the balance of convenience has become irrelevant. In the course of submissions, counsel for each side accepted that if this Court were to reach a concluded view as to the meaning of the contract, as I have, then, logically, the issue of balance of convenience is otiose."

Orders to be made

92. The extent of the points of claim and the prayer for relief suggest that the Applicant seeks to have determined other matters in this proceeding beyond what has already been argued. Mr Whitten suggested that those other matters must await a certificate under s.56 of the Act. I think the parties should have an opportunity to consider and argue, if thought appropriate, whether or not it is possible and appropriate for the present proceeding to be continued or whether it must be sent for conciliation.

93. There will be orders as follows:

(a) an order that the Respondent, whether by itself, its servants or agents or howsoever otherwise, be restrained until further order from having recourse to the following bank guarantees:

- ANZ Bank Guarantee No. DG550673418 for $68,007.80
- ANZ Bank Guarantee No. DG547383418 for $217,008.45

(b) a direction that the registry to list this proceeding for directions at the date and time to be fixed in order to determine its future conduct;

(c) liberty to apply in the meantime;

(d) costs will be reserved.

SENIOR MEMBER R. WALKER