

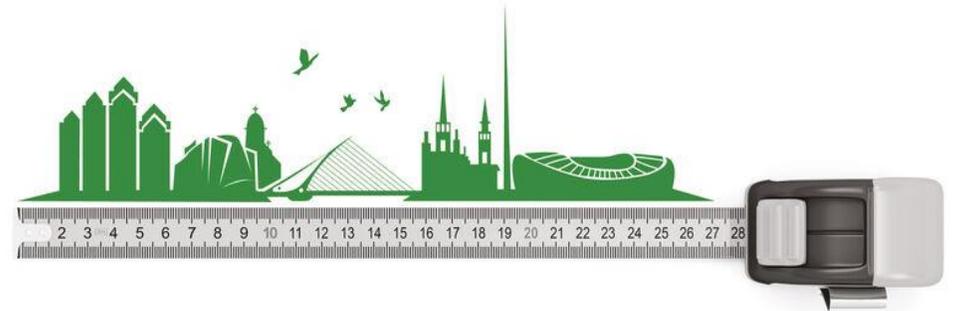
Calls and Enforcing Performance Bonds on Irish Construction Projects: a Practical Approach

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Calls and Enforcing Performance Bonds on Irish Construction Projects

- *In what circumstances will a Bond be called and what happens in practice once a dispute arises, what are the steps and what approach are the Courts taking to the enforcement of performance bonds, and what strategies/circumstances will change the dial in a dispute?*



Overview of performance bonds

– What is a bond?

- Financial instrument issued by insurers / Surety Companies in the construction sector to provide comfort against the cost risks of a contractor's failure to complete a project by

– Types of performance bonds

- conditional bonds
- unconditional or on demand bonds

– When will a bond be called?

- When the contractor is no longer willing or is able to deliver their contractual obligations **or** where the contractor is in material default in the performance of its contractual obligations



The established and ascertained principle

- There is a perception of a lack of transparency with the ability to enforce a performance bond – is it real or imagined?
- Growing concern that judicial interpretation of wording of a performance bond creates the perception of a double standard in Ireland and in the UK and that Bonds are increasingly difficult to recover upon.
- Court's interpretation differs depending on the facts of each case, resulting in recovery becoming increasingly difficult and expensive.
- Knock on effect that funders will question the rationale behind bonds, ultimately effecting completion of projects.
- Judges are more frequently confronted with enforcement issues, specifically when determining that a loss is "*established and ascertained*" pursuant to the contractual terms
- Case law presently distinguished on the basis of individual facts - leaving a lacuna and divergence for practitioners



Ziggurat (Claremont Place) LLP v HCC International Insurance Company PLC

EWHC 3286 (TCC)

- Contractor was terminated and the employer sought to call on the bond to recover damages arising from the breach and necessity to appoint an alternative contractor.
- Surety argued that actual evidence of the breach of contract was required, and that no payment was due by them on the Bond pending a “*formal decision*” by way of separate judgment.
- The bond was the instrument which provided the employer with the ability to recover losses and the requirement for another judgment would circumvent the **commercial purpose** behind the bond.
- It was held that the surety’s actions were in contravention of its obligations under the Bond and it was in breach of those obligations.
- The TCC **rejected** this argument that a separate judgment would be required before a demand could be made on the Bond, indicating it would “*destroy the commercial value and purpose of the bond*”.

Yuanda v Multiplex Construction Europe Ltd and another

(2020) EWHC 468 (TCC)

- The TCC examined the wording in the underlying building contract to determine if it could permit the enforcement of a conditional performance bond.
- The Building Contract provided for utilisation of a specific dispute resolution procedure clause.
- Fraser J (in the TCC) held that an adjudicator's decision would be sufficient to establish and ascertain damages to claim on the bond (no separate judgment required as against the contractor).
- The upshot was that when seeking enforcement it was evident that Courts were open to analysing the bond by reference to the instrument as a whole, and not looking at the demand /bond in isolation.
- What was clear was that parties should be extremely careful in ensuring that they had considered the actual terms of the performance bond in issue, and also they had considered the related contractual mechanisms provided for in the Contract – **Query** were the courts correct and was this a sensible halfway house to facilitate recovery, but to be fair to the surety too?

Clarington Developments Limited v HCC International Insurance Company PLC (2019) IEHC 630

- Clarington (an Irish case) was confronted with a requirement to decide what did the parties agree when it was agreed that to enforce the bond the loss had to be “*established and ascertained*” principle
- Here the employer had sought to recover damages following a termination of the contractor, and it argued that the Court was capable of assessing the loss itself without looking elsewhere or the necessity for a separate judgment.
- The surety countered that there was a “*condition precedent*” dispute resolution mechanism in the contract which required the parties to refer to arbitration or conciliation to resolve the dispute.
- Judge Simons placed considerable emphasis on the language contained in the clause and he found that the language of the contract obliged the employer to meet **all the provisions** (including any condition precedent) in the contract, before it would consider enforcing an obligation for payment under the bond.
- The upshot being that there is a reluctance by Irish Courts to permit recovery on a conditional bond, unless the party seeking enforcement has satisfied all of the individual requirements on the bond and of the contract.

Gembira Limited v Amtrust Europe Limited (2024) IEHC 188

- This case involved an application by the employer for summary judgment against the contractor where the contract provided that an employer could recoup its losses (on termination) where it hired a replacement contractor to finish the project
- The employer **relied** on an **architect's certificate** to ground their application for summary judgment, but the certificate was qualified.
- Judge Quinn found that the certificate relied upon was **not effective** for the purpose of establishing a debt under the building contract and instead that it was "*an estimate*" of the debt and could therefore not be taken as "*conclusive evidence of the debt*"
- Judge Quinn also found numerous grounds on which he was satisfied that the defendant surety had demonstrated a credible and bona fide defence to the summary claim.
- Significantly, Judge Quinn made it clear that there was **no requirement** for the employer to first pursue the contractor for the debt as a first step, but the debt must still be established and ascertained.

Circumstances that will change the dial to avoid future disputes?

- Knowing that the Court will take a strict approach to contractual interpretation and the bond will not crystallise immediately there is loss claimed.
- The parties must take care to understand the limitations or what is being purchased – is it an on demand or conditional instrument, and what hurdles will have to be overcome to make a valid claim.
- When dealing with a conditional bond, familiarise self with any condition precedents that apply, and what steps proofs will be required to crystallise the debt to secure payment, - such that it is established and ascertained.
- Even if it is not a strict judicial requirement, securing an award against a contractor – possibly even an adjudicator's award may expedite recovery on the bond.
- Ultimately the Courts will seek to determine the objective meaning of the contract and ambiguity will be resolved by reference to the background / factual matrix of the contract.

Key take aways

1. Ziggurat demonstrates the rigours a claiming party must meet – and compliance with the language of the instrument before enforcement will be permissible.
2. Yuanda accepted that an adjudicator’s award would suffice to demonstrate loss on the contract – if this were followed in Ireland it may lead to easier and more cost-effective enforcement applications – but remembering that the courts will look to the wording in the instruments when looking at enforcement applications.
3. Clarington was aligned at looking at the wording in the instruments and ensuring there had been compliance (with the condition precedent) but recognised that there was not prerequisite to have a decision for an independent court against a contractor to enforce.
4. Finally, Gembira emphasised the need for a Court to focus on the specific language of the wording in the bond/contract and to understand each bond is a bespoke instrument when faced with applications to enforce.
5. There is no easy pickings and Insurers will most likely robustly defend applications for payment on bonds, unless all the proofs are satisfied and in order. Claims on bonds involve significant work in terms of time and cost.



Questions?



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