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DREW & NAPIER LLC

LEGAL UPDATE

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CASE UPDATE

SINGAPORE HIGH COURT AFFIRMS THAT AN APPLICATION FOR INJUNCTION TO RESTRAIN A CALL ON AN ON-DEMAND BOND IS A SUBSTANTIVE MATTER

Shanghai Electric Group Co Ltd v PT Merak Energi Indonesia and Anor [2010] SGHC 2

Executive summary

The grant of an injunction restraining a beneficiary of an on-demand bond from making a call on the bond is a substantive matter and is governed by the law to which the court is directed by its choice of law rules, and not the procedural law of the forum.

The (Chinese) Plaintiff in this case had applied for and obtained, on an *ex-parte* basis, an injunction to restrain the (Indonesian) 1st Defendant from making a call on an on-demand advance payment bond issued by a Singapore bank.

The 1st Defendant applied to set aside the injunction. The Court applied English law, being the law governing the bond, to determine whether there was basis to maintain the injunction. The 1st Defendant's application was allowed, and the injunction set aside.

The Plaintiff is appealing against the decision.

Hri Kumar, SC, Tham Feei Sy and **Kristine Ang** of Drew & Napier LLC acted for the successful 1st Defendant in setting aside the injunction.

Background

By a contract dated 10 August 2007 (the "**Contract**"), PT Merak Energi Indonesia (the "**1st Defendant**") engaged Shanghai Electric Group Co Ltd (the "**Plaintiff**") to, *inter alia*, design and construct a power plant in Indonesia for the sum of US\$108 million.

It was a term of the Contract that the 1st Defendant would make an advance payment of US\$10.8 million to the Plaintiff to enable the latter to commence work. In return, the Plaintiff procured an on-demand advance payment bond for the same amount (the "**Bond**") in favour of the 1st Defendant. The Bond was issued by a Singapore bank (the "**Bank**").

Both the Contract and the Bond expressly provided that the governing law was English law.

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A dispute subsequently arose between the parties. The 1st Defendant terminated the Plaintiff's appointment under the Contract, and made a demand under the Bond.

The Plaintiff obtained an *ex-parte* injunction (the "**Injunction**") to restrain the 1st Defendant from receiving any monies from the Bank pursuant to the call on the Bond. The 1st Defendant applied to set aside the Injunction.

The High Court's decision

The court set aside the Injunction.

In reaching its decision, the court had to determine the applicable law governing the restraint on the calling of an on-demand bond. This depended on whether the grant of such an injunction was a procedural or substantive matter.

If it was a procedural matter, the *lex fori*, (the procedural law of the forum), ie. Singapore law, applies. If it was a substantive matter, then the proper law of the Bond, ie. English law, applies.

Divergence between Singapore law and English law

The determination of the appropriate law to apply was important as Singapore law and English law are not the same in respect of the grounds upon which the court will restrain a call on an on-demand bond.

Under English law, the only ground upon which a court will restrain a call on an on-demand bond is fraud. However, the threshold under Singapore law is lower - in addition to fraud, unconscionability is an additional ground. It would therefore be more difficult to obtain, or sustain, an injunction under English law.

The grant of an injunction is a substantive matter which is governed by the parties' choice of law

After an extensive review of the law, the court concluded that the grant of an injunction to restrain the call on an on-demand bond was a *substantive* matter. This is because a restraint on a beneficiary's right to receive payment upon a demand on an on-demand bond would effectively deprive the beneficiary of his right to immediate payment, which is the fundamental purpose of such bonds. English law therefore applied.

No fraud or unconscionability on the part of the 1st Defendant

In any event, on the facts, the court found that the demand made by the 1st Defendant was neither fraudulent nor unconscionable. The Injunction would therefore have been set aside regardless of whether English or Singapore law applied.

Comment

This is the first time the Singapore courts have determined the proper law to apply in bond injunctions. The case highlights the importance of giving careful thought to the choice of law when drafting on-demand bonds and the underlying contract.

Parties however risk having their choice of law struck down on the grounds of public policy if they choose laws which are viewed as an attempt to circumvent the laws of the relevant jurisdiction.

If you would like more information about this case or wish to discuss how it may potentially affect you or your business, please feel free to contact the litigation and dispute resolution lawyers in Drew & Napier LLC (please refer to the Directors' profiles on our [website](#)), or:

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