SUPREME COURT OF QUEENSLAND

CITATION:	*Lucas Drilling Pty Limited v Armour Energy Limited* [2013] QCA 111
PARTIES:	**LUCAS DRILLING PTY LIMITED** ACN 093 489 671 (appellant) **v** **ARMOUR ENERGY LIMITED** ACN 141 198 414 (respondent)
FILE NO/S:	Appeal No 9253 of 2012 SC No 7983 of 2012
PROCEEDING:	General Civil Appeal
ORIGINATING COURT:	Supreme Court at Brisbane
DELIVERED ON:	14 May 2013
DELIVERED AT:	Brisbane
HEARING DATE:	15 April 2013
JUDGE:	Margaret McMurdo P and White JA and Daubney J Separate reasons for judgment of each member of the Court, each concurring as to the orders made
ORDERS:	**1. The appeal is allowed.** **2. The orders made on 7 September 2012 are set aside.** **3. The moneys paid into Court by the respondent pursuant to the orders of 7 September 2012 in substitution of the Performance Bond are to be paid to the appellant together with any accretions thereon.** **4. The respondent is to pay the appellant's standard costs of and incidental to the appeal and the application at first instance.**
CATCHWORDS:	APPEAL AND NEW TRIAL – PRACTICE AND PROCEDURE – QUEENSLAND – POWERS OF THE COURT – ORDERS SET ASIDE OR VARIED – where there was a contract under which the respondent undertook to provide drilling services to the appellant – where the appellant was granted an interlocutory injunction to restrain the respondent from calling on a bank guarantee which the appellant had procured in favour of the respondent – where the learned primary judge had established that there was a serious question to be tried and that the balance of

convenience favoured the granting of injunctive relief, conditional upon the appellant (in this proceeding) paying the amount of the guarantee into court – where the appellant contended that the learned primary judge erred in the exercise of the discretion to grant interlocutory relief – whether the primary's judge's discretion miscarried

CONTRACTS – BUILDING, ENGINEERING AND RELATED CONTRACTS – THE CONTRACT – CONSTRUCTION OF PARTICULAR CONTRACTS AND IMPLIED CONDITIONS – OTHER MATTERS – where there was a contract under which the respondent undertook to provide drilling services to the appellant – where the appellant was granted an interlocutory injunction to restrain the respondent from calling on a bank guarantee which the appellant had procured in favour of the respondent – where the appellant contended that the learned primary judge erred in the exercise of the discretion to grant interlocutory relief – where there was a dispute about the proper construction of the contractual clause concerning the performance bond – where the appellant contended that, by virtue of its accrued rights, it was not obliged to return the performance bond, notwithstanding termination of the contract by the respondent – where the respondent contended that the appellant had no accrued rights and was obliged to return the performance bond – whether the proper construction of the contract obliged the appellant to return the performance bond – whether serious case to be tried

Australian Broadcasting Corporation v O'Neill (2006) 227 CLR 57; [2006] HCA 46, cited
Clough Engineering Ltd v Oil and Natural Gas Corporation Ltd (2008) 249 ALR 458; [2008] FCAFC 136, cited
Fletcher Construction Australia Ltd v Varnsdorf Pty Ltd [1998] 3 VR 812, cited
House v The King (1936) 55 CLR 499; [1936] HCA 40, cited
Kennedy Taylor (Vic) Pty Ltd v Baulderstone Hornibrook Pty Ltd [2000] VSC 43, cited
Redline Contracting Pty Ltd v MCC Mining (Western Australia) Pty Ltd (No 2) [2012] FCA 1, cited
Southern Cross Constructions (NSW) Pty Ltd (Administrators Appointed) v Bucasia Pty Ltd [2012] NSWSC 1419, applied

COUNSEL: G A Thompson SC, with A P J Collins, for the appellant
G J Gibson QC, with GA Beacham, for the respondent

SOLICITORS: HWL Ebsworth for the appellant
Hopgood Ganim for the respondent

[1] **MARGARET McMURDO P:** I agree with Daubney J's reasons for allowing this appeal. I observe, however, that the primary judge has not referred to Stevenson J's helpful reasons in *Southern Cross Constructions (NSW) Pty Limited (Administrators*

Appointed) v Bucasia Pty Limited[1] as that case was determined after the primary judge's decision in the present case.

[2] I agree with Daubney J's proposed orders.

[3] **WHITE JA:** I agree with Daubney J's reasons that the appeal be allowed. I agree with the other orders which he proposes.

[4] **DAUBNEY J:** On 1 November 2011, the appellant, Lucas Drilling Pty Ltd (then known as "AJ Lucas Coal Technologies Pty Ltd") ("Lucas"), entered into a written Onshore Rig Services Agreement ("the Agreement") with the respondent, Armour Energy Ltd ("Armour"), by which Lucas was contracted to provide specified oil and gas drilling services to Armour at certain well sites.

[5] On 7 September 2012, Armour sought an interlocutory injunction to restrain Lucas from calling on a bank guarantee which Armour had procured in favour of Lucas pursuant to the Agreement.

[6] The learned primary judge concluded that Armour had established that there was a serious question to be tried and that the balance of convenience favoured the granting of injunctive relief, conditional upon Armour paying the amount of the guarantee into Court. On Armour having given the usual undertaking as to damages, his Honour made the following orders:

> "1. In substitution for the security provided by the Performance Bond dated 4th April 2012 ('the Performance Bond') provided by the Applicant pursuant to clause 19 of the contract dated 31 October 2011 entered into between the Applicant and the Respondent, the Applicant shall pay the sum of $750,000 into Court on or before 12 September 2012.
>
> 2. The money paid into Court pursuant to paragraph 1 aforesaid shall not be paid out other than by an order of this Court or the agreement in writing of the Applicant and the Respondent.
>
> 3. The Respondent is restrained from calling upon the Performance Bond until 4pm on 13 September 2012.
>
> 4. Upon compliance with paragraph 1 above, the Respondent shall forthwith return the Performance Bond to the Applicant."

Directions were also made for the further conduct of the proceeding.

[7] Lucas has appealed, contending that the learned primary judge erred in the exercise of the discretion to grant such interlocutory relief because:

(a) on the case presented to the judge, there was no serious question to be tried, and

(b) the balance of convenience did not favour the grant of the interlocutory orders.

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1 [2012] NSWSC 1419.

The Agreement

[8] In the Agreement, Armour was described as "the Company" and Lucas as "the Contractor".

[9] Clause 19 of the Agreement is central to the dispute:

> "**BANK GUARANTEE**
>
> 19.1 The Company must, on or before the delivery of the Commencement Notice to the Contractor, procure the issue to the Contractor of a Performance Bond which:
>
> (a) is issued by an Issuer with a Required Rating and approved by the Contractor (which approval must not be unreasonably withheld);
>
> (b) has a face amount which is no less than the Performance Bond Amount;
>
> (c) expires no earlier than the 15th day of December 2012; and
>
> (d) is payable at an office of the Issuer in Brisbane.
>
> 19.2 In the event that the Company:
>
> (a) has not paid a payment that the Company is obligated to pay under this Agreement delivered by the Contractor within the time provided in this Agreement; and
>
> (b) the Contractor has provided with 7 days prior written notice that the Company intends to makes a demand under the Performance Bond which specifies the Contractor's reasons for making such demand,
>
> the Contractor may make a demand under the Performance Bond on account of, and apply the Performance Bond against, any amount of a valid invoice which is undisputed by the Company.
>
> 19.3 The Contractor must, subject to any rights the Contractor may have in relation to the Performance Bond, return the Performance Bond (less any amounts drawn under clause 19.2) to the Company within the earlier of 30th November 2012 or within 3 days after the termination of this Agreement.
>
> 19.4 The Contractor must, as soon as practicable after he has made a demand under the Performance Bond, give a notice to the Company specifying the Contractor's reasons for making the demand.
>
> 19.5 The Contractor may only make a demand under the Performance Bond in accordance with this clause 19.

> 19.6 Provided that the Contractor has complied with this Clause 19, the Company must not take any steps to restrain or injunct the Contractor from making a demand under the Performance Bond or the Issuer paying any amounts under the Performance Bond."

[10] It is clear enough that cl 19.2(b) was misworded. It was uncontentious before this Court that that clause ought be read as follows:

> "In the event that the Company:
>
> ...
>
> (b) has been provided with seven days prior written notice that the Contractor intends to make a demand under the Performance Bond which specifies the Contractor's reasons for making such demand, ..."

[11] In cl 1 of the Agreement:

(a) "Performance Bond" was defined to mean "an irrevocable bank guarantee, letter of credit or insurance bond callable by the Contractor materially in the form set out in Schedule or any other form approved by the Contractor", and

(b) the Performance Bond Amount was set at $750,000.

[12] The form of the Performance bond was specified in Annexure "O" to the Agreement.

[13] The terms of invoicing and payment under the Agreement were set out in cl 7, which included:

> "7.4 The Contractor must submit invoices at the Company's address set out in the relevant Schedule or such other address as may be nominated by the Company for that purpose. Invoices must state and include:
>
> (a) the period to which the invoice relates;
>
> (b) the amount of the invoice;
>
> (c) details of the Rates or other charges that are comprised in the invoice;
>
> (d) if applicable or relevant, copies of each of the daily reports required by Clause 13 signed by the Company's Representative; and
>
> (e) the well name and number the invoice relates to.
>
> 7.5 Payment of an invoice will be due and payable by the Company within 14 days of receipt by the Company of the invoice and in the event that the Company fails to pay the undisputed invoice

amount within that time the Company must pay the rate of interest which is two percent above the ANZ Banking Group Reference Rate from the due date until the date of payment.

7.6 If the Company disputes any item invoiced, it must notify the Contractor of every item in dispute within 14 days of the receipt of the invoice, specifying the basis for the objection. The Company must pay the undisputed portion of that invoice. The Contractor will not be entitled to discontinue work under this Agreement by reason of non-payment of a disputed invoice where such dispute has not been resolved. If the Company fails to notify the Contractor that an item of the invoice is disputed within 14 days of the receipt of the invoice, it will be deemed to accept the invoice.

7.7 Within 2 days of the Company notifying the Contractor of matters in dispute pursuant to Clause 7.5, the Parties will meet to use their reasonable endeavours to resolve the disputed issues. If the disputed issues are resolved and it is determined that amounts are owed by the Company to the Contractor or by the Contractor to the Company, those amounts must be paid within 14 days. If the disputed issues are not resolved within 21 days of the notification of the dispute by the Company, Clause 26 will apply.

7.8 If it is determined that amounts are owed by the Company to the Contractor or by the Contractor to the Company the interest referred to in clause 7.5 is payable on the amount determined as owed, from the due date until the date of payment. For the avoidance of doubt the calculation of interest on any amount determined as owed does not cease because that amount was disputed."

[14] Clause 9 conferred on Armour the right to suspend the Agreement in the event of unsatisfactory performance by Lucas, and to terminate the Agreement if the unsatisfactory performance was not remedied:

"**9. SUSPENSION IN EVENT OF DEFAULT BY CONTRACTOR**

9.1 If the Company is, on reasonable grounds, dissatisfied with the performance of the Contractor on account of incompetence or unreasonably slow progress in the performance of the Contractor's obligations and the cause of those matters is reasonably within the control of the Contractor, the Company may give the Contractor written notice in which the Company must specify in reasonable detail the cause of its dissatisfaction.

9.2 If the Contractor fails, or refuses to commence and to continuously and diligently continue to remedy the matters specified in the notice given by the Company within 10 days after such written notice is received by the Contractor, the

Company will have the right at its option to direct the Contractor to suspend all Services forthwith until the matters specified in the notice have been remedied to the satisfaction of the Company.

9.3 No remuneration or compensation other than that which is owing at the time the Company directs the Contractor to suspend the Services will be payable by the Company during any period of suspension under this Clause 9.

9.4 If the matters specified in the notice given by the Company under Clause 9.1 have not been remedied within 21 days, or such longer period as the Company may allow, from the date when the notice is received by the Contractor, the Company will have the right to terminate this Agreement."

Background

[15] On 4 April 2012, Macquarie Bank Ltd issued a bank guarantee addressed to Lucas at the request of Armour. The maximum aggregate sum to be paid under the bank guarantee was $750,000. The bank guarantee was in the following terms:

"***BANK GUARANTEE***

At the request of Armour Energy Limited ACN 141 198 414 (the 'Customer') and in consideration of AJ Lucas Coal Technologies Pty Limited ABN 98 093 489 671 (the 'Beneficiary') accepting this Guarantee in relation to the obligations of the Customer in respect to the Onshore Rig Services Agreement (the 'Transaction') between the Customer and the Beneficiary, Macquarie Bank Limited ABN 46 008 583 542 (the 'Bank') unconditionally undertakes to pay on demand any sum or sums which may from time to time be demanded in accordance with this Guarantee by the Beneficiary to a maximum aggregate sum of $750,000.00 (the 'Sum').

The Sum is automatically reduced by the amount of any claim paid under this Guarantee.

This Guarantee and the obligations of the Bank are to continue until the earlier of:

a) The Bank receives written notification from the Beneficiary that the Sum is no longer required by the Beneficiary; or

b) this undertaking is returned to the Bank at its offices at Level 25, Central Plaza One, 345 Queen Street, Brisbane QLD 4000; or

c) payment to the Beneficiary by the Bank of the Sum or such part as the Beneficiary may require; or

d) 4.00 p.m. Brisbane time on the 30 November 2012 provided that any letter of demand for payment must be delivered into the hands of a Manager of the Bank at Level 25, 345 Queen Street, Brisbane QLD 4000 prior to that time.

Should the Bank be notified in writing at its office at Level 25, Central Plaza One, 345 Queen Street, Brisbane QLD 4000 such notice purporting to be signed for and on behalf of the Beneficiary, that the Beneficiary desires payment to be made of the whole or any part or parts of the Sum, the Bank will make such payment or payments to the Beneficiary;

i) without further reference to the Customer; and

ii) notwithstanding any notice given by the Customer to the Bank not to pay the same; and

iii) irrespective of the performance or non-performance by the Customer or the Beneficiary of the terms of the Transaction.

Provided always that the Bank may at any time without being required to do so pay to the Beneficiary the Sum less any amount or amounts it may previously have paid under this undertaking or such lesser sum as may be required and specified by the Beneficiary and thereupon the liability of the Bank hereunder shall immediately cease and determine.

The obligations of the Bank under the Guarantee will not be affected or discharged by any alteration to the terms of the Transaction or any extension of time or forbearance by the Customer or the Beneficiary to the other.

This Guarantee is governed by the laws of Queensland."

[16] In the course of performing its work under the Agreement, Lucas issued a number of invoices to Armour.

[17] On 27 July 2012, Lucas sent an invoice to Armour by email – this was invoice number 300486 in the amount of $473,379.29 for services provided between 1 July 2012 and 15 July 2012.

[18] Under cover of an email dated 13 August 2012, Lucas sent Armour a further invoice in the sum of $796,593.46 for services between 15 July 2012 and 31 July 2012. This particular invoice, however, did not bear a tax invoice number – in fact, it noted specifically "Tax Invoice to be sent". On 20 August 2012, Lucas sent Armour precisely the same invoice but with the tax invoice number inserted. That was tax invoice number 300552. The invoice was otherwise in all respects identical to that which had been emailed on 13 August 2012.

[19] Armour did not pay on either of these invoices. Nor did Armour raise any dispute in respect of amounts payable under those invoices until after the events of 29 August 2012, described below.

[20] In the meantime, however, Armour had, on 3 August 2012, issued to Lucas a notice under cl 9.1 of the Agreement. This was in the form of a lengthy letter, in which Armour articulated a range of issues concerning Lucas' performance under the Agreement about which Armour was dissatisfied. The details of those matters are not relevant for present purposes. It is sufficient to note that the letter stated:

> "Despite face-to-face meetings and telephone communications, there has been no tangible progress on rectifying the issues and concerns identified by Armour. Therefore, Armour is providing this letter as notice in accordance with clause 9.1 of our rig services agreement dated 31 October, 2011 (Agreement). Set out below are items that Armour is dissatisfied with and also a number of specific defaults of Lucas' obligations under our Agreement."

[21] Two relevant events then occurred on 29 August 2012:

(a) At 9.29 am, Armour's solicitors sent Lucas' solicitors an email attaching a letter by which Armour gave notice of termination of the Agreement. The letter stated:

> "Pursuant to clause 9.4 of the Onshore Services Agreement dated 31 October 2011 (the **Agreement**), our client hereby terminates the Agreement. Your client has failed to remedy to our client's satisfaction the complaints referred to in the notice issued on 3 August 2012 pursuant to clause 9.1 of the Agreement (**Notice**)."

This letter also made demand, pursuant to cl 19.3 of the Agreement, for the return of the Performance Bond;

(b) At 4.50 pm, Lucas sent Armour a "Notice of Intention" in the following terms:

> "Pursuant to clause 19.2 of the agreement between Lucas Drilling Pty Ltd (formerly A J Lucas Coal Technologies Pty Ltd) and Armour Energy Limited dated 31 October 2011, ("Agreement") Lucas hereby notifies you that after 7 days from today Lucas intends to make a demand under the Performance Bond for the following reasons:
>
> 1. Invoice 3000486 for $430,344.81 was due on 11th August 2012 but remains unpaid; and
>
> 2. Invoice 3000552 for $796,593.46 was due on 28th August 2012 but remains unpaid.
>
> By reason of clause 7.6 of the Agreement the abovementioned invoices are not in dispute.
>
> Please note that Lucas will also be claiming interest pursuant to clause 7.5 of the Agreement.
>
> As at 29th August 2012 interest is:
>
> 1. $2,597.63 for Invoice 3000486 and thereafter at the daily rate of $144.31; and
>
> 2. $242.85 for Invoice 3000552 for $796,593.46 and thereafter at the daily rate of $242.85."

[22] In subsequent correspondence between the parties' solicitors, Armour's solicitors threatened to apply for an injunction if Lucas did not withdraw its notice of intention to call on the Performance Bond.

[23] The present proceeding was then commenced on 3 September 2012 by an originating application filed on behalf of Armour. That was originally returnable on 5 September 2012. The originating application sought, *inter alia*, the following relief:

> "2. A declaration that the Respondent had no entitlement under the contract between the Applicant and the Respondent dated 31 October 2011 ('**the Contract**') to:
>
> (a) serve the notice of intention to make a demand on the Performance Bond dated 29 August 2012 and served on the Applicant on the same date (**the Notice**);
>
> (b) make a demand on the Performance Bond held under the Contract, in relation to invoices 3000486 and 3000552 (**the Invoices**), described in the Notice.
>
> 3. An order restraining the Respondent from making a demand on the Performance Bond in reliance upon the Notice, or the Invoices.
>
> 4. An order restraining the Respondent, until trial or further order, from making a demand on the Performance Bond in reliance upon the Notice, or the Invoices."

[24] As events transpired, the matter came on before the learned primary judge on 7 September 2012. The only relief sought by Armour at that hearing was an interlocutory injunction to restrain Lucas from calling on the Performance Bond.

The decision below

[25] After summarising the relevant factual background, the learned primary judge set out the three bases on which Armour relied in contending that there was a serious question to be tried as to whether the proposed call by Lucas on the Performance Bond was in breach of cl 19:

(a) That cl 19.3 required Lucas to return the Performance Bond within three days of termination of the Agreement; Lucas had not done so, and its ability to call on the Performance Bond was directly attributable to its own breach of cl 19.3; whilst cl 19.3 was subject to any rights Lucas had in relation to the Performance Bond, Lucas had no such rights when the Agreement was terminated, and only gave notice of intention to call on the Performance Bond after the Agreement had been terminated;

(b) The two invoices on which Lucas relied were not "undisputed" within the meaning of cl 19.2;

(c) The notice of intention to call on the Performance Bond was invalid because it was issued before the time for payment of the second invoice had expired.

[26] His Honour noted the authorities supporting the proposition, which was conceded before him by Armour, that the courts are slow to restrain a party from calling on a performance bond issued in its favour under contracts such as the present – his

Honour referred particularly to *Clough Engineering Ltd v Oil and Natural Gas Corporation Ltd*[2], and said:

> "Whether it is appropriate to restrain a party from calling upon a performance bond granted in its favour pursuant to express written contractual terms agreed between the parties requires a consideration of the terms of the contract to determine whether its provision was merely for security or was an exercise, as between the parties, in risk allocation pending resolution of any dispute.
>
> Although the performance bond was issued for a specified period, the contract expressly provided for its return within three days after termination of the agreement. That provision is arguably consistent with the performance bond, although unconditional, being provided only as security for payment whilst the agreement is operative.
>
> Further, although the return is subject to any rights the respondent may have in relation to the performance bond, it is reasonably arguable that the 'rights' referred to are rights accrued prior to termination. If that were not the case, the bond would be expected to continue to its specified date so as to allow the respondent to enforce any rights accruing after termination.
>
> A conclusion that the performance bond was to provide security rather than to allocate risk as to who shall be out of pocket pending resolution of any dispute is also consistent with the requirement in clause 19.1 that the contactor (sic) may make a demand under the performance bond 'on account of any amount of a valid invoice which is undisputed by the company.' If the performance bond represented an allocation of risk pending resolution of a dispute, the bond would be available to be called upon in respect of all amounts outstanding, not merely the undisputed amount."

[27] The learned primary judge returned to the contention by Armour that "a proper interpretation of cl 19 leads to the conclusion that [Lucas] is not entitled to call on the Performance Bond after termination as it had no right to do so at the date of termination". His Honour then concluded:

> "It is not my function to determine the proper construction of the contract. There is no application by either party for a declaration as to the construction of the contractual term. The issue before me is whether there is a serious question to be tried as to the correct interpretation of clause 19 of the contract.
>
> Having considered all of the material, I am satisfied there is such a question. The applicant has established it has 'a sufficient likelihood of success' in its claim, that the respondent's claimed ability to call upon the performance bond at this time is due to its own failure to return the bond in accordance with its obligations under the contract.
>
> This conclusion renders it unnecessary to consider the other bases sought to be relied upon. Suffice it to say, those bases seem inconsistent with the clear mechanism provided by the contract for the disputing of invoices."

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2 (2008) 249 ALR 458.

[28] By that final paragraph, it is clear enough that his Honour, whilst not considering it necessary to decide the points for the purposes of the application before him, clearly expressed disinclination to accept the second and third arguments which had been advanced by Armour.

[29] His Honour then turned to consider the balance of convenience, and said:

> "Having considered the material, I am satisfied there is a legitimate concern as to the ability of the respondent to repay any moneys it received as a result of any call upon the performance bond. That alone is a compelling reason not to allow the respondent to call upon the performance bond which was granted as security rather than as part of a considered allocation of risk.
>
> That conclusion is particularly compelling where conditions can be imposed on the grant of any relief which will ensure the respondent continues to have security of a similar value."

[30] The learned primary judge noted that the concern by Lucas to protect the position concerning the large amounts of money owed to it could be addressed by requiring that Armour pay into Court the amount of the Performance Bond, and made the orders described in [3] above.

This appeal

[31] This being an appeal against what was, in effect, the grant of an interlocutory injunction, the question for this Court is whether the learned primary judge's discretion miscarried, having regard to the principles enunciated in *House v The King*[3].

[32] For the purposes of the present appeal:

(a) Counsel for Lucas accepted that Armour's notice terminating the Agreement on 29 August 2012 was validly given, and that it could be assumed for present purposes that the Agreement had been thereby terminated;

(b) Counsel for Armour confirmed that there was no challenge to the proposition that the two invoices on which Lucas had relied were undisputed, and conceded that any claim which Armour might otherwise have to set off against monies payable by Armour to Lucas were not relevant to the operation of the provisions of cl 19.

[33] The issues before this Court were thereby reduced to relatively narrow ones of contractual construction.

[34] The argument for Lucas was that, on a proper construction of cl 19.3, Lucas was not obliged to return the Performance Bond, notwithstanding the termination of the Agreement by Armour on 29 August 2012, because at the time of termination Lucas had accrued rights in relation to the Performance Bond by reason of the operation of cl 19.2.

[35] Armour argued that, on a proper construction of the Agreement, Lucas had no accrued rights in relation to the Performance Bond when the Agreement was

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3 (1936) 55 CLR 499.

terminated, that cl 19.3 therefore obliged Lucas to return the Performance Bond, and the refusal of Lucas to return the Performance Bond, in breach of cl 19.3, rendered it appropriate for the "negative stipulation" in cl 19.3 to be enforced by injunction.

[36] Much of the argument in this Court was directed, as it was before the learned primary judge, to cases concerned with performance bonds or performance guarantees required to be given by or on behalf of contractors in favour of principals to secure the proper performance by the contractors of their contractual obligations. As is noted in Dorter & Sharkey "*Building and Construction Contracts in Australia*"[4]:

> "The contractor is not the only one who regards the construction industry as a high risk one. The principal likes some commercial comfort in addition to the legal rights and obligations under the contract. The general concept of such commercial comfort is 'security', although it is wrongly used according to its strict sense. Such 'security' includes performance bonds, retention funds and guarantees. The latter term is also a misnomer because it is strictly inconsistent with the elements of suretyship: compare the criticisms by Barwick CJ in *Wood Hall Ltd v Pipeline Authority* (1979) 141 CLR 443; 53 ALJR 487 at 445 (CLR)."

[37] The commercial essence of a performance bond, as conventionally described, is to ensure the due and proper performance of the contract by the contractor.

[38] In the present case, and despite being described as a "performance bond", the bank guarantee which Armour was required to provide in favour of Lucas was, in truth, a form of security for Lucas for payment on undisputed invoices to the value of the bank guarantee. In other words, it was a security for payment for the benefit of the contractor, not security for performance for the benefit of the principal.

[39] *Clough Engineering Ltd v Oil and Natural Gas Corporation Ltd*[5] was a case in which performance guarantees had been given to secure a contractor's performance. In January 2005, Clough entered into a contract with the principal for the development of certain gas and oil fields off the coast of India, and for the construction of associated onshore facilities. It was a term of the contract that, within two weeks of signing, Clough would provide the principal with an unconditional and irrevocable performance bank guarantee for the performance of the contract. The principal had the right to call on the performance guarantees "... in the event of [Clough] failing to honour any of the commitments entered into under this contract". The parties fell into dispute. The principal terminated the contract and called on the bank guarantees. Clough sought an injunction to restrain the principal from making the demand and to restrain the banks from paying. It was unsuccessful at first instance, and appealed to the Full Federal Court. In dismissing Clough's appeal, the Full Federal Court had occasion to examine the principles relating to performance bank guarantees. The Court commenced this analysis by noting:

> "[75] The principles under which a court will construe the terms of a bank's undertaking in a performance guarantee, and the

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4 Thomson Reuters Loose Leaf Service at [10.370].

5 (2008) 249 ALR 458.

> contract between a contractor and an owner, have been stated in a series of authorities over the last 30 years. The seminal decision is that of the High Court in *Wood Hall Ltd v Pipeline Authority* (1979) 141 CLR 443; 24 ALR 385 (*Wood Hall*).
>
> [76] Reference was made in *Wood Hall* to the commercial purpose of the guarantees, which in that case was that they be equivalent to cash: see Barwick CJ (at CLR 445; ALR 387); Gibbs J (at CLR 453; ALR 393-4); Stephen J (at CLR 457-8; ALR 396-7). As Stephen J observed, to introduce a qualification on the entitlement of the owner to call upon the performance guarantees (at CLR 457; ALR 397):
>
> ... would be to deprive them of the quality which gives them commercial currency.
>
> Barwick CJ and Gibbs J expressed similar views to Stephen J. Gibbs J stated the argument made on behalf of the contractor, which was that the performance guarantee must be construed in light of the contract between the authority and the contractor (at CLR 450; ALR 391). His Honour rejected the submission that the right to invoke the guarantee was conditional upon the contractor having committed a breach of its primary obligations under the contract. He placed emphasis upon the express statement in the guarantee that the undertaking of the bank was unconditional (at CLR 451; ALR 391-2)."

[40] The Court then observed that the authorities have recognised three principal exceptions to the rule that a court will not enjoin the issuer of a performance guarantee from performing its unconditional obligation to make payment. The first two exceptions, relating to fraud and unconscionability, are not relevant for present purposes. In respect of the third exception, the Court said[6]:

> "*Third* – the most important exception for present purposes, is that, while the court will not restrain the issuer of a performance guarantee from acting on an unqualified promise to pay (*Reed Construction Services* at 164 per Austin J):
>
> > ... if the party in whose favour the bond has been given has made a contract promising not to call upon the bond, breach of that contractual promise may be enjoined on normal principles relating to the enforcement by injunction of negative stipulations in contracts.
>
> It may be preferable not to describe this as an exception but rather as an over-riding rule because it emphasises that the 'primary focus' will always be the proper construction of the contract: *Bateman Project Engineering Pty Ltd v Resolute Ltd* (2000) 23 WAR 483; [2000] WASC 284 per Owen J at [30]. Stephen J recognised this in *Wood*

6 At [77].

> *Hall* at CLR 459; ALR 398-9 by observing that the provisions of the contract may qualify the right to call on the undertaking contained in a performance guarantee."

[41] It was within the rubric of this third exception that Armour sought to cast the present case – its contention was that Lucas had, by cl 19.3, promised contractually to return the Performance Bond after termination of the Agreement, and that the breach by Lucas of that contractual promise could be enjoined on normal principles.

[42] The Court in *Clough Engineering* then turned to consider the rationale for a performance bond of the kind before it, particularly by reference to the judgment of the Victorian Court of Appeal in *Fletcher Construction Australia Ltd v Varnsdorf Pty Ltd*[7]. The Full Federal Court said:

> "[79] In *Fletcher Construction*, Charles JA at 821 and Callaway JA at 826 recognised that there are generally two commercial reasons why a beneficiary of a performance guarantee may have stipulated for such an entitlement. One is to provide security for a valid claim against the contractor. The second, which is additional to the first, is to allocate the risk between the parties as to who shall be out of pocket pending the resolution of a dispute between them. Callaway JA went on to observe that 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. He went on to say (at 827):
>
> Remembering that we are speaking of guarantees in the sense of standby letters of credit, performance bonds, guarantees in lieu of retention moneys 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. As I have already indicated, they may simply refer to the kind of default to which, if it is alleged in good faith, enables the beneficiary to have recourse to the security or its proceeds.
>
> [80] It seems to us that his Honour's reference to a default 'alleged in good faith' was intended to embrace the first exception we have set out above. That is to say, the breach relied upon to support a call on the performance guarantee must not be asserted fraudulently because the court will enjoin a party from so acting. Thus, subject to the exceptions of fraud and unconscionability, the beneficiary of a performance guarantee granted in its favour as a risk allocation device, will be entitled to call upon the guarantee even if it turns out, ultimately, that the other party was not in default: Fletcher Construction at 827."

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7 [1998] 3 VR 812.

[43] The Full Federal Court referred to the authorities which had noted the importance of performance bonds in the construction industry, but observed that, notwithstanding the importance of commercial practice, there was no suggestion that the Court should depart from the task of construing the terms of the contract in each case. Their Honours went on to state the following propositions:

(a) At [83], that clear words will be required to support a construction which inhibits a beneficiary from calling on a performance guarantee where a breach is alleged in good faith, i.e. non-fraudulently;

(b) At [85], that the question of construction as to whether the underlying contract contains a qualification on the right to call upon the security must be determined in light of the contract and the form of the performance guarantee as contained in the contract.

[44] Other cases to which this Court was referred in argument included *Fletcher Construction v Varnsdorf* (supra), *Redline Contracting Pty Ltd v MCC Mining (Western Australia) (No 2)*[8], *Kennedy Taylor (Vic) Pty Ltd v Baulderstone Hornibrook Pty Ltd*[9] and *Southern Cross Constructions (NSW) Pty Ltd (Administrators Appointed) v Bucasia Pty Ltd*[10].

[45] All of these were cases concerning bonds or guarantees given to secure the performance of contractors, and each case turned on the construction of the particular contractual provisions in that case. Several of those cases (*Kennedy Taylor v Baulderstone Hornibrook* and *Southern Cross Constructions v Bucasia*) dealt with whether, under the particular terms of the contracts under consideration, a party's entitlement to call on a performance bond survived termination of the contract.

[46] In the present case, the learned primary judge's decision to grant the interlocutory relief hinged on his conclusion that Armour had established a sufficient likelihood of success in its claim that Lucas' "claimed ability to call upon the Performance Bond at this time is due to its own failure to return the bond in accordance with its obligations under the contract".

[47] That conclusion was founded on the obligations imposed on Lucas by cl 19.3. But those obligations to return the Performance Bond were expressly "subject to any rights [Lucas] may have in relation to the Performance Bond". This exception clearly contemplated that Lucas may have accrued rights in relation to the Performance Bond when the Agreement was terminated, and that if Lucas did have any such accrued rights then it was excepted from the obligation to return the Performance Bond.

[48] Lucas' contention was that it was excepted from the obligation imposed by cl 19.3 because it had accrued rights in relation to the Performance Bond pursuant to cl 19.2.

[49] Lucas argued that, as a consequence of the non-payment of the two invoices by Armour (it being accepted for present purposes that those invoices were

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8 [2012] FCA 1.
9 [2000] VSC 43.
10 [2012] NSWSC 1419.

undisputed), Lucas had accrued rights in relation to the Performance Bond because of the operation of cl 19.2(a), that the termination by Armour on the morning of 29 August 2012 did not preclude Lucas from giving the notice under cl 19.2(b) later that day, and that Lucas was consequently relieved of the obligation to return the Performance Bond under cl 19.3.

[50] For Armour, it was argued that no rights had accrued for Lucas under cl 19.2 because both cl 19.2(a) and cl 19.2(b) were conditions precedent to the accrual of the right to make demand under the Performance Bond, the notice under cl 19.2(b) had not been given when the Agreement was terminated by Armour, and therefore Lucas had no accrued rights in relation to the Performance Bond which exempted it from the obligation under cl 19.3 to return the Performance Bond.

[51] *Southern Cross Constructions v Bucasia* was, as I have already noted, concerned with security which had been provided by a contractor. The particular security in that case comprised two unconditional insurance bonds. The contract between the principal and the contractor provided that the principal could have recourse to the security in the following circumstances:

> "5.2 **Recourse**
>
> The Principal may have recourse to Security after first giving not less than 5 Business Days [sic] notice to the Contractor where:
>
> a) the Principal has become entitled to exercise a right or power under the Contract in respect of the Security;
>
> b) the Contractor is in default or breach of the Contract;
>
> c) the Contractor has repudiated or given notice of intention to repudiate the Contract;
>
> d) the Contractor has failed to pay the Principal amount certified as owing by the Contractor to the Principal in accordance with clause 37.2A; or
>
> e) the Contractor is otherwise indebted to the Principal and the Principal remains unpaid after 5 business days has [sic] elapsed since the Principal issued an invoice to the Contractor seeking payment of the debt."

[52] The contractor terminated the contract on 23 October 2012 when it gave a notice of termination. On 24 October 2012, the principal issued a notice of intention to call on the security. Stevenson J was required to determine the following separate question:

> "Whether, on the proper construction of the Contract, and assuming Southern Cross terminated the Contract on or before 23 October 2012, Bucasia was entitled to issue a notice of intention to have recourse to security under clause 5.2 of the Contract."

[53] His Honour noted:

> "14 The separate question raises for consideration the nature of Bucasia's accrued rights under the Contract assuming, as the parties do for the purpose of the determination of the separate question, that Southern Cross was entitled to, and did, terminate the Contract.
>
> 15 Where a contract is terminated, the parties are not divested of such rights as they had already 'unconditionally acquired': per Dixon J in *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457 at 476-477. Such rights are often referred to as 'accrued rights': e.g. *Macquarie International Health Clinic Pty Ltd v Sydney South West Area Health Service* [2010] NSWCA 268 at [217] per Hodgson JA (Allsop P and Macfarlan JA concurring at [1] and [389] respectively). See generally Seddon, Bigwood & Ellinghaus *Cheshire & Fifoot, Law of Contract* 10th Ed (2012) at [21.38].
>
> 16 The principle is that where one party to a contract terminates the contract for breach, the contract is not rescinded as from the beginning. Both parties are discharged from further performance of their obligations under the contract; but accrued rights are preserved."

[54] The principles stated in paragraphs 15 and 16 of this passage, which I respectfully adopt, are apposite to the present case.

[55] In relation to the accrual of rights under cl 5.2 in that case, Stevenson J said:

> "22 In my opinion, the nature of Bucasia's right was to have recourse to the security as soon any of the events specified in clauses 5.2(a) to (e) occurred 'after' giving the requisite notice. But the giving of the notice was not a condition precedent to the accrual of the right. It was merely the manner in which the right was to be exercised. And the right accrued, in my opinion, as soon as any of the events specified in clauses 5.2(a) to (e) occurred.
>
> 23 The words used by the parties in clause 5.2 make clear to me that their intention was that the words 'after first giving not less than 5 Business Days [sic] notice to [Southern Cross]' were intended to do no more than provide that Bucasia could not exercise that accrued right until the expiry of the notice.
>
> 24 There are many reasons why the parties might have made this provision. One might be to allow Southern Cross time to organise its affairs (whether with any third party provider of the security or otherwise) in readiness for Bucasia's recourse to the security. Another might be to allow Southern Cross an opportunity to challenge Bucasia's recourse to the security on some basis arising from their dealings together."

[56] In my view, a similar construction applies with respect to cl 19.2 in the present case. A plain reading of cl 19.2 reveals that the right to make demand under the

Performance Bond arose when the contingency contemplated by cl 19.2(a) was fulfilled. So much is clear not only from the wording of cl 19.2(a) but also from the concluding words of cl 19.2, which specify the object of the right which accrued, namely to apply the Performance Bond "against any amount of a valid invoice which is undisputed by [Armour]". The giving of the notice under cl 19.2(b) was not, and could not be, a separate condition precedent to the accrual of the right to call on the Performance Bond – the notice could only be given after the fulfilment of the contingency in cl 19.2(a). The notice procedure specified in cl 19.2(b) regulated the way in which the right was to be exercised.

[57] Accordingly, on the undisputed facts, when Armour terminated the Agreement on the morning of 29 August 2012, Lucas was possessed of rights "in relation to the Performance Bond". Lucas was, therefore, exempted from the obligation under cl 19.3 to return the Performance Bond.

[58] It follows that the learned primary judge erred in reaching his central conclusion that Armour had established a sufficient likelihood of succeeding on its argument that Lucas was in breach of cl 19.3 by failing to return the Performance Bond, and consequently the exercise of the discretion to grant interlocutory relief miscarried. Whilst the matter was not beyond argument, when one has regard to the terms of cl 19.2 and cl 19.3, I do not consider that, having regard to the principles confirmed in *Australian Broadcasting Corporation v O'Neill*[11], it can be said that Armour had, or has made out, a *prima facie* case (as that term is explained in *ABC v O'Neill*) that Lucas was in breach of its obligation to return the Performance Bond. This was and is not a case for the grant of the interlocutory relief sought by Armour.

[59] There being no *prima facie* case made out on Armour's argument for interlocutory relief, it is not necessary to consider the question of the balance of convenience.

[60] The appeal should be allowed. Having regard to the orders which were made by the learned primary judge at the request of the parties, I would now make the following orders:

1. The appeal be allowed;

2. The orders made on 7 September 2012 be set aside;

3. The moneys paid into Court by the respondent pursuant to the orders of 7 September 2012 in substitution of the Performance Bond be paid to the appellant together with any accretions thereon;

4. The respondent pay the appellant's standard costs of and incidental to the appeal and the application at first instance.

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11 (2006) 227 CLR 57 at [19] (Gleeson CJ and Crennan J) and [65] – [72] (Gummow and Hayne JJ).