

REPUBLIC OF SOUTH AFRICA



**IN THE HIGH COURT OF SOUTH AFRICA
GAUTENG LOCAL DIVISION, JOHANNESBURG**

CASE NO: 8731/2020

(1)	REPORTABLE: YES / NO
(2)	OF INTEREST TO OTHER JUDGES: YES / NO
(3)	REVISED.
<i>24/11/20</i>	
Date	<i>ML Twala</i>
	ML TWALA

In the matter between:

BUFFALO CITY METROPOLITAN MUNICIPALITY

APPLICANT

And

FUSION GUARANTEES (PTY) LTD

RESPONDENT

JUDGMENT

Delivered: This judgment was handed down electronically by circulation to the parties' legal representatives by e-mail. The date and time for hand-down is deemed to be 11h30 on the 24th November 2020.

TWALA J

- [1] Before this Court, is an application launched by the applicant wherein it sought an order against the respondent for payment of the sum of R1 518 273.70 and interest at the prescribed legal rate *a tempore morae* together with the costs of the action based on the performance guarantee issued by the respondent on behalf of Kubela-Meladi Civil Construction currently known as Mmutla Civil and Plant Hire cc ("the Contractor") in favour of the applicant. The application is opposed by the respondent for the reasons that will appear hereunder.
- [2] It is common cause that on the 20th of March 2015 the applicant awarded the contractor the contract to carry out the works on a sewer line extension between Berlin and Lingilitsha in the Eastern Cape for the project amount of R15 182 737 in 2015 ("the Building Contract"). Furthermore, in terms of the building contract the contractor was required to procure and obtain a performance guarantee in favour of the applicant. On the 5th of June 2015, the respondent issued the performance guarantee on behalf of the contractor and in favour of the applicant. It is further not in dispute that the contractor failed to complete its scope of work and the completion certificate was not issued. As result on the 20th of August 2018 the applicant terminated the building

contract. On the 23rd of October 2015 the applicant demanded payment of the guaranteed amount of R1 518 273.70 from the respondent based on the performance guarantee.

- [3] It is apposite at this stage to mention that, after the respondent had filed its answering affidavit in these proceedings, the applicant launched an application to strike out certain paragraphs of the respondent's answering affidavit for being irrelevant or tendering hearsay evidence. However, the applicant did not file an affidavit in support of the application stating exactly which paragraphs of the answering affidavit were irrelevant and which tendered hearsay evidence. The application was to be heard together with the main application.
- [4] At the hearing of this case, Advocate Mc Aslin SC, assisted by Advocate Ntoane on behalf of the applicant did not persist with the application to strike out submitting that the issues in the main application can be determined by simply ignoring the irrelevant and hearsay evidence as appears on the respondent's answering affidavit.
- [5] Advocate van Niekerk submitted on behalf of the respondent that the application to strike out was ill-conceived and premature since it was filed without a founding affidavit to establish any prejudice that the paragraphs complained of in the answering affidavit are causing the applicant. The paragraphs, so it was argued, are not even mentioned as to which are irrelevant and which are tendering hearsay evidence. There is a live application before this Court which must be determined and it cannot just be ignored. The application should be dismissed with the applicant to pay the costs since it cannot be simply ignored.

[6] It is trite law that an application in motion proceedings shall be brought by way of notice of motion supported by an affidavit stating the facts upon which it is relied for the relief sought. Put differently, an applicant in motion proceedings must make out its case in the founding affidavit which is attached to the notice of motion in support of the application.

[7] The Uniform Rules of Court provide the following regarding applications:

“Rule 6 Applications

(1) Save where proceedings by way of petition are prescribed by law, every application shall be brought on notice of motion supported by an affidavit as to the facts upon which the applicant relies for relief.

(2)

[8] I am unable to disagree with counsel for the respondent that the application is defective in its current form and does not comply with the rules of Court. Furthermore, the application is live before the Court and has not been withdrawn by the applicant and therefore should be determined not only to be gleaned over and be left at that. I am therefore inclined to dismiss the application to strike out with costs for it does not comply with the rules of Court.

[9] Advocate Mc Aslin SC submitted that there was no reason for the applicant to join the contractor in these proceedings for it has no interest whatsoever. It was up to the respondent to join the contractor if it so wished. The applicant's claim is based on the performance guarantee which is completely independent of the building contract. The guarantee creates, so it was argued, a principal obligation on the part of the respondent and is autonomous and the only defence available to the respondent is if the demand is fraudulently

made by the applicant. The guarantee is an instrument of security for the contractor's performance and not a suretyship.

- [10] It was contended further that the applicant has met all the requirements of the guarantee – hence it was entitled to call up the guarantee and to payment as demanded. The guarantee is independent of the underlying contract and the respondent cannot say the demand is fraudulent based on the disputed facts of the underlying contract. The applicant has no discretion to make the demand but is entitled only to make the demand once the trigger facts come into existence. Fraud would be if the applicant makes the demand when there are no trigger facts in extant. The fact that the demand is for the full amount as per the guarantee does not mean that the applicant is committing fraud if the amount finally proven in the end is less than the amount demanded. The demand would be fraudulent if the applicant knowingly misrepresented the facts when the demand is made.
- [11] Advocate Van Niekerk submitted for the respondent that the termination of the building contract is in dispute for the applicant failed to pay the contractor causing its failure to perform its obligations in terms of the contract. The demand is fraudulent because at the time the demand was made, the outstanding works were worth about R100 000 whereas the demand is for the full guaranteed amount. The demand was made long before the applicant quantified the indebtedness of the contractor to be R9.5 million. Therefore, so it was argued, the applicant committed fraud when it made the demand knowing that it owes the respondent a sum of more than R900 000 but claims the full amount of the performance guarantee.
- [12] Before considering the submissions made in this case, it is necessary to restate our jurisprudence on the nature and effect of performance guarantees. It is

now settled that the performance guarantee is autonomous from the underlying contract. The performance guarantee is a unique contract in that whatever disputes may subsequently arise between the employer and the employee or contractor, the guarantor undertakes to pay the employer provided only that the condition specified in the guarantee are met.

- [13] To put matter in the proper context, it is essential for me to restate the provisions of the performance guarantee which are relevant for the purposes of the determination of this case which read as follows:

“3. The guarantor hereby acknowledges that:

3.1 Any reference in this Performance Guarantee to the Contract is made for the purpose of convenience and shall not be construed as any intention whatsoever to create an accessory obligation or any intention whatsoever to create a suretyship;

3.2 Its obligation under this Performance Guarantee is restricted to the payment of money:

4. Subject to the Guarantor’s maximum liability referred to in 1, the Guarantor hereby undertakes to pay the Employer the sum certified upon receipt of the documents identified in 4.1 to 4.3

4.1 A copy of a first written demand issued by the Employer to the Guarantor stating that payment of a sum certified by the Engineer in an Interim or Final Certificate has not been made in terms of eh Contract and failing such payment within seven (7) calendar day, the Employer

intends to call upon the Guarantor to make payment in terms of 4.2

- 4.2 *A first written demand issued by the Employer to the Guarantor at the Guarantor's physical address with a copy to the Contractor stating that a period of seven (7) calendar days has elapsed since the first written demand in terms of 4.1 and that the sum certified has still not been paid;*
- 4.3 *A copy of the aforesaid payment certificate which entitles the Employer to receive payment in terms of the Contract of the sum certified in 4*

5. *Subject to the Guarantor's maximum liability referred to in 1, the Guarantor undertakes to pay the Employer the Guaranteed Sum or the full outstanding balance upon receipt of a first written demand from the Employer to the Guarantor at the Guarantor's physical address calling up the performance Guarantee, such demand stating that;*

- 5.1 *the contract has been terminated due to the Contractor's default and that this Performance Guarantee is called up in terms of 5; or*
- 5.2 *.....*
- 5.3 *the aforesaid written demand is accompanied by a copy of the notice of termination and or the provisional/final sequestration and or the provisional liquidation court order;*

- [14] In *Lombard Insurance Company Ltd v Landmark Holdings (Pty) Ltd* 2010 (2) SA 86 (SCA) the Court stated the following:

“Para 20 The guarantee by Lombard is not unlike irrevocable letters of credit issued by banks and used in international trade, the essential feature of which is the establishment of a contractual obligation on the part of the a bank to pay the beneficiary (seller). This obligation is wholly independent of the underlying contract of sale and assures the seller of payment of the purchase price before he or she parts with the goods being sold. Whatever disputes may subsequently arise between buyer and seller is of no moment insofar as the bank’s obligation is concerned. The bank’s liability to the seller is to honour the credit. The bank undertakes t pay provided only that the conditions specified in the credit are met. The only basis upon which the bank can escape liability is proof of fraud on the part of the beneficiary. This exception falls within a narrow compass and applies where the seller, for the purpose of drawing on the credit, fraudulently presents to the bank documents that to the seller’s knowledge misrepresent the material facts.”

- [15] In *Dormell Properties 282 CC v Renasa Insurance Co Ltd and Others* NNO 2011 (1) SA (SCA) the Court stated the following:

“Para 63 The appellant complied with the provisions of clause 5. It was not necessary for the appellant to allege that it had validly cancelled the building contract due to the second respondent’s default. Whatever disputes there were or might have been between the appellant and the second respondent were irrelevant to the first respondent’s obligation to perform in terms of the construction guarantee.....

“Para 64 Once the appellant [the beneficiary] had complied with clause 5 of the guarantee, the first respondent [the guarantor] had no defence to a claim under the guarantee. It still has no defence. The fact that an arbitrator has determined that the appellant was not entitled to cancel the contract, binds the appellant – but only vis-à-vis the second respondent [the employer]. It is res inter alios acta so far as the first respondent is concerned. As the cases to which I have referred above make abundantly clear, the appellant did not have to prove that it was entitled to cancel the building contract with the second respondent, as a precondition to enforcement of the guarantee given to it by the first respondent. Nor does it have to do so now.”

- [16] The autonomy principle of the guarantee was again emphasised in *Guardrisk Insurance Company Ltd v Kentz (Pty) Ltd* (92/2013) [2013] ZSCA 182 which judgment was in the same year quoted with approval by the Supreme Court of Appeal in *Coface South Africa Insurance Co Ltd v East London Own Haven t/a Own Haven Housing Associatin* (050/2013) [2013] ZSCA 202; [2014] 1 All SA 536 (SCA); 2014 (2) SA 382 (SCA) (2 December 2013) where the Court stated the following:

“Para 13 The terms of the guarantees are clear. They create an obligation on the part of the guarantor (Guardrisk) to pay Kentz (the employer) on the happening of a specified event. It was recorded in the guarantees that notwithstanding the reference to the construction contract, the liability of the bank as principal is absolute and unconditional, and should not be construed to create an accessory or collateral obligation. The guarantees go further and specifically state that the bank may not delay making payment in terms of the guarantees

by reason of a dispute between the contractor and the employer. The purpose of the guarantees was to protect Kentz in the event that Brokrew could not perform its obligation in terms of the construction contract.”

- [17] Although the Court was dealing with a different issue arising out of the performance guarantee in *Joint Venture Between Aveng (Africa) (Pty) Ltd and Strabag International GmbH v South African National Roads Agency Soc Ltd and Another* (577/2019) [2020] ZSCA 146 (13 November 2020) the Court stressed the autonomy principle with regard to the performance guarantees as follows:

“Para 7 Before I consider the Joint Venture’s submission before us, it is necessary to restate our jurisprudence on the nature and effect of letters of credit (which applies equally to performance guarantees). Our law is well settled, and firmly recognises the autonomy principle, ie the autonomy of the performance guarantee from the underlying contract. The principle is best expressed in the oft-quoted passage from Lord Denning MR’s speech in Edward Owen:

‘The unique value of a documentary credit, therefore, is that whatever disputes may subsequently arise between the issuing bank’s customer (the buyer) and the beneficiary under the credit (the seller) in relation to the performance or, for that matter, even the existence of the underlying contract, by issuing or confirming the credit, the bank undertakes to pay the beneficiary provided only that the conditions specified in the credit are met. The liability of the bank to the beneficiary to honour the credit arises upon presentment to the bank of the documents specified in the

credit, including typically a set of bills of lading, which on their face conform strictly to the requirements of the credit. In the event of the documents specified in the credit being so presented, the bank will escape liability only upon proof of fraud on the part of the beneficiary. ’’

- [18] I understand the above authorities to be saying that the purpose of the performance guarantee is to provide security and to allocate the risk as to who, between the employer and the contractor shall be out of pocket pending resolution of the dispute between them. The guarantee creates an obligation on the part of the guarantor to pay the employer, the applicant in this case, a predetermined sum of money on the happening of an event, once the conditions of the performance guarantee as stated therein have been complied with. The guarantee is absolutely independent of the building contract between the applicant and the contractor and is payable on demand. Whatever issues that may arise between the contractor and the applicant in terms of the underlying contract are of no moment with regard to the guarantee.
- [19] I am unable to disagree with counsel for the applicant that there is no merit in the respondent's contention that the contractor should have been joined in these proceedings for there is a dispute between the applicant and the contractor with regard to payments and outstanding amounts. The applicant is suing on the bases of the provisions of the guarantee and the issues arising from the underlying contract between the applicant and the contractor are irrelevant. Furthermore, I do not understand the respondent to be saying that the applicant has not complied with the conditions of the performance guarantee nor that the underlying contract provides for the contractor to be joined in proceedings involving the performance guarantee.

- [20] In the Joint Venture case quoted above, the Court referred to the decision of the Victoria Court of Appeal in *Uber Builder and Developers v MIFA Pty Ltd* [2020] VSC 596 where Nichols J stated the following:

“Where the contract does impose a condition on the right to access the security, the party seeking to restrain recourse must establish the existence of a serious question to be tried as to whether the beneficiary has in fact met the contractual requirements.”

- [21] It has been stated in the above authorities that the only defence available to the guarantor in cases involving the performance guarantee is when the employer has committed fraud. In casu, I do not agree with the respondent that the applicant has committed fraud by demanding payment of the full guaranteed amount when the outstanding works were only worth R100 000 and there was a judgment in favour of the contractor in the amount of over R900 000. It is my respectful view that these issues are not relevant to the determination of the issues regarding the performance guarantee. They are issues arising from the underlying contract and the liability arising from the performance guarantee is absolute, unconditional and independent of the underlying contract. Whatever disputes existed between the applicant and the contractor at the time the demand was made are irrelevant to the respondent’s obligation to perform in terms of the performance guarantee.

- [22] In the case of Guardrisk quoted above the Supreme Court of Appeal stated the following at paragraph 18:

“Insofar as the fraud exception is concerned, the party alleging and relying on such exception bears the onus of proving it. That onus is an ordinary civil one which has to be discharged on a balance of

probabilities, but will not lightly be inferred. In Loomcraft Fabrics CC v Nedbank Ltd and Another, it was pointed out that in order to succeed in respect of the fraud exception, a party had to prove that the beneficiary presented the bills (documents) to the bank knowing that they contained material misrepresentations of fact upon which the bank would rely and which they knew were untrue. Mere error, misunderstanding or oversight, however unreasonable, would not amount to fraud. Nor was it enough to show that the beneficiary's contentions were incorrect. A party had to go further and show that the beneficiary knew it to be incorrect and that the contention was advanced in bad faith."

[23] I hold the view that, for the respondent to succeed with its defence that the applicant has committed fraud when making the demand, it is required to establish facts that the applicant knowingly misrepresented material facts when it made the demand. However, the respondent has failed establish facts to prove that the applicant misrepresented material facts when it made the demand. Furthermore, it does not mean that the applicant has committed fraud when it demanded the full guaranteed amount when the outstanding works was only R100 000. The contractor still has recourse against the applicant if it proves its claim in future proceedings between itself and the applicant. It follows ineluctably therefore that the applicant is entitled to call up the guarantee and has succeeded in its claim against the respondent.

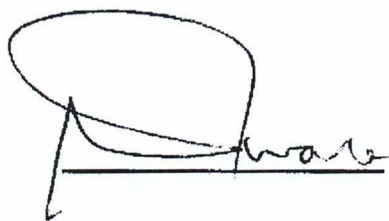
[24] I am persuaded by the submissions of counsel for the applicant to award a special costs order against the respondent for devoting almost ninety percent of its answering affidavit dealing with issues that are irrelevant in this case. At the hearing of this case counsel for the respondent did not even spend any time in arguing about the irrelevant issues as to what happened between the

applicant and the contractor as contained in the answering affidavit. It is my respectful view that it was not necessary for the respondent to raise all these issues but did that only, if I may borrow the phrase, to muddy the waters.

[25] Furthermore, I do not agree with the respondent that the applicant is not entitled to costs for both counsel because, so it was argued, the issues were crisp and uncomplicated. The Courts, including the Supreme Court of Appeal, are extremely busy dealing with matters involving the performance guarantees in building contracts. In almost every case new and different issues are raised and our law is still developing for it relies mostly on decision of foreign jurisdictions. I am of the view therefore that it was necessary for the applicant to engage the services of two counsel.

[25] In the circumstances, I make the following order:

1. The respondent is to pay the applicant the sum of R1 518 273.70
2. The respondent is to pay the applicant interest on the sum of R1 518 273.70 calculated at the rate of 10% per annum from the 23rd of October 2018 to the date of final payment
3. The respondent is to pay the costs of suit on an attorney and client scale including costs of senior counsel.

A handwritten signature in black ink, appearing to read 'Twala M L', is written over a horizontal line.

TWALA M L

JUDGE OF THE HIGH COURT OF SOUTH AFRICA

GAUTENG LOCAL DIVISION

Date of hearing: 16th November 2020

Date of Judgment: 24th November 2020

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