

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

Case No. 2023/009986

**(1) REPORTABLE: NO
(2) OF INTEREST TO OTHER JUDGES: NO
(3) REVISED.
DATE: 7 March 2023**

In the matter between:

THE CONSORTIUM COMPRISING:

First Applicant

KC COTTRELL CO. LTD

ELB ENGINEERING SERVICES (PTY) LTD (in liquidation)

ELB EDUCATIONAL TRUST FOR BLACK SOUTH AFRICANS

KC COTTRELL CO. LTD

Second Applicant

and

SANTAM LIMITED

First Respondent

NGODWANA ENERGY RF LTD

Second Respondent

NEDBANK LIMITED C/O NEDBANK INCORPORATED

Third Respondent

JUDGMENT

WILSON J:

The dispute

1 The applicants, to whom I shall refer as KC Cottrell, seek interim relief restraining the first respondent, Santam, from paying out on a guarantee given in favour of the second respondent, Ngodwana, for the performance of KC Cottrell's obligations under a contract facilitating the construction of a twenty-five megawatt biomass power plant in Mpumalanga. The power plant is presently operational, but by all accounts there are significant defects in the construction work that require rectification, and which mean that the plant, while operational, is not running optimally.

2 The construction contract, like most agreements of its sort, provides for the contractor, KC Cottrell, to be paid in instalments once the employer, Ngodwana, has certified that certain payment "milestones" have been reached. As the construction work went on, Ngodwana certified that a number of these milestones had been reached, and paid out substantial sums of money to KC Cottrell in respect of the construction work.

3 However, Ngodwana has now taken the view that the defects it has identified in the construction work are so serious as to justify the reversal of the payment milestones it previously certified had been reached, and the reclamation of much of the money it paid over under those certificates. It gave notice of its intention to do so in a document referred to before me as "Interim Payment Certificate 36" ("IPC 36"). In that document, Ngodwana certified that KC Cottrell is now liable to it in the sum of R222 362 236.68. In a letter dated 31 January 2023, Ngodwana stated that it intended to make a call in that amount on the guarantee. That will, in turn, result in Santam claiming the full amount from KC Cottrell.

4 It is not necessary for me to consider the nature and extent of the defects in the construction work, or how they are to be rectified, in any detail. The only issue of substance before me is whether KC Cottrell has established a *prima facie* right to restrain Santam from paying out on the guarantee.

5 Santam does not oppose the application, but Ngodwana does. Ngodwana does not suggest that the defects it has identified in the construction work cannot be rectified. Nor does it suggest that it will cost anything like the R222 million it seeks to call up to rectify them, or that the defects have caused it losses in anything approximating those amounts. Ngodwana instead relies on what it says are the clear terms of the guarantee: viz. that all it needs to establish, in order to call up the guarantee, is that KC Cottrell is in breach of the construction contract. That fact is hardly in dispute. The defects in the work are essentially common cause. That, Ngodwana says, means that it is entitled to call up whatever amount it likes up to the limit of the guarantee.

6 Mr. Redman, who appeared for KC Cottrell before me, accepted that the defects in the work were such that Ngodwana was probably entitled to make a call on the guarantee in some amount. He argued, however, that the amount Ngodwana threatens to call up – just over R222 million – is so grossly disproportionate to any amount to which Ngodwana could honestly believe it was entitled, that the call Ngodwana threatens would be fraudulent. It is on that basis – that any call on the guarantee based on IPC 36 would constitute an act of fraud – that KC Cottrell says it has a *prima facie* right to interdict Santam from paying out on the call.

The law

7 It was common ground between the parties that the guarantee at issue in this case is an “on demand” guarantee. Guarantees of this nature provide an especially strong form of security for an employer under a construction contract. “On demand” guarantees – sometimes referred to as “call bonds” – provide for the employer to call up the guarantee in any amount on the mere notification to the guarantor that an event specified in the guarantee has taken place. In other words, all that is needed is a demand that conforms to the terms of the guarantee. It is not incumbent upon the

employer to establish the nature and extent of the contractor's liability to it (*Minister of Transport and Public Works Western Cape v Zandbuild* 2011 (5) SA 528 SCA, paragraph 16). Nor does the employer have to allege that there is any specific amount due to it at all, unless, of course, the amount owing by the contractor to the employer itself constitutes part of the event specified in the guarantee.

8 So, for example, if a guarantee states that it may be called upon on a breach of contract, all the employer has to allege is that there is such a breach. In that event, the full amount due in terms of the guarantee becomes payable if that is what the employer demands. If, however, the guarantee states that the employer may call up the bond on breach only to the extent that it is necessary to remedy the breach, then the employer must allege both that there is a breach and the amount it considers necessary to remedy the breach. In neither case, however, is the employer required to establish that there is a breach, or the nature and extent of the amount necessary to cure it. The guarantee is called up on the mere say-so of the employer.

9 Accordingly, it does not matter to the guarantor whether there is actually a breach of contract, or whether the amount called up is necessary to cure the breach. The guarantor is not entitled to go behind the employer's demand, so long as the demand conforms to the terms of the guarantee itself. The guarantor's obligation to pay out on the guarantee is wholly independent of the underlying contract between the employer and the contractor. Any disputes between the employer and the contractor about whether there really is a breach, and the extent of the liability arising from it, are irrelevant to the guarantor's duty to pay on demand from the employer (see *Coface South Africa Insurance Co Ltd v East London Own Haven t/a Own Haven Housing Association* 2014 (2) SA 382 (SCA) ("Coface"), paragraphs 13 to 16, 22 and 25 to 26).

10 The one exception to this position is fraud. If the employer makes a call on the guarantee knowing full well that the event specified in it has not occurred (for example that there is not actually a breach of contract), then the guarantor has no duty to pay out on the call, and the contractor is entitled to an interdict restraining it from doing so (see *Guardrisk Insurance Company v Kentz (Pty) Ltd* [2014] 1 All SA 307 (SCA) paragraph 17).

The guarantee in this case

11 Ngodwana's right to call up the guarantee in this case depends on the construction to be given to it. If, as Ngodwana contends, the guarantee is such that all that need be alleged is a breach of contract, then the case ends there. There is no serious dispute that there is such a breach, and accordingly no suggestion that Ngodwana's call on the guarantee could in that event be fraudulent.

12 If, however, the guarantee requires Ngodwana to go further, and allege an amount that is needed to remedy the defects that it has identified in the construction work, then it is necessary to consider whether Ngodwana honestly believes that it is entitled, in view of the defects, to the amount it has threatened to call up.

13 Clause 4 of the guarantee states as follows –

We, SANTAM LIMITED (Reg. No. 1918/001680/06) ("Guarantor"), hereby irrevocably and unconditionally undertake with you that whenever you or the Facility Agent gives a written notice to us demanding payment by way of original letter (a "Demand"), without further proof or condition (which notice shall state that Contractor has failed to comply with its obligations in respect of the Contract, including any remedy periods stipulated therein), we will, notwithstanding any objection which may be made by the Contractor and without any right of set-off or counterclaim, immediately, but within no later than 5 (five) Business Days, pay to you

(a) in respect of amounts claimed as delay liquidated damages into the Operating Account (Account Number 1120842514, Branch Code 198765) with the Facility Agent;

(b) in respect of all other amounts into the Compensation Proceed Account (Account Number [...], Branch Code 198765) with the Facility Agent; or

(c) into such other account as the Facility Agent may direct, such an amount as you or the Facility Agent may in that Demand require not exceeding (when aggregated with any amount(s) previously so paid, under this Guarantee) the Guaranteed Sum ("Guarantee").

14 The terms of this guarantee seem self-evident to me. All that Ngodwana is required to allege is an unremedied breach of contract. Mr. Redman pressed the argument, however, that the word “require” in the phrase “may in that Demand require” at the end of the clause means “required to remedy the breach alleged”. As sympathetic as I am to that position (it seems obvious on the facts before me that Ngodwana’s threat to call up the amount specified in IPC36 is oppressive) I do not think that the interpretation Mr. Redman pressed is tenable. There is no difference, in my view, between the amount Ngodwana “demands” and the amount it “requires”.

15 Bearing in mind that this is an application for interim relief, I have given some thought to whether, though it is in my view untenable, Mr Redman’s interpretation is at least arguable. But I regret that I cannot conclude that there is even a *prima facie* basis on which the word “require” could be read as anything other than synonymous with “demand”. Far more would need to be said in the guarantee to enable it to be read as limiting the amount that could be called up to that which Ngodwana reasonably requires to remedy the breach it alleges. In light of the nature and purpose of performance guarantees of this nature, it is, in my view, not realistic to read-in an internal limitation on Ngodwana’s right to call up the guarantee of the kind Mr. Redman suggests, without at least some explicit indication of that intent. I can find no such indication in the text of the guarantee.

16 For all of these reasons, and with some reluctance, I dismiss the application with costs, including the costs of two counsel.

S D J WILSON

Judge of the High Court

HEARD ON: 28 February 2023

DECIDED ON: 7 March 2023

For the Applicant: NP Redman SC
M Desai

Instructed by: LNP Attorneys, Sandton c/o
PPN Attorneys, Parktown

For the Second Respondent: PHJ Van Vuuren SC
DS Hodge

Instructed by: Tiefenhalter Attorneys c/o
Dockrat Inc, Dunkeld