

URDG – do these rules help?

Having earlier highlighted the pitfalls in implementing the Uniform Rules for Performance Guarantees 2010 (URDG), STUART JORDAN* here cites the instances of two regional disputes where there were lapses in the drafting of contracts.

MY comments aren't often prescient so I'll take credit where I can. In September 2019, we looked at the Uniform Rules for Performance Guarantees 2010 (URDG). These rules are published by the International Chamber of Commerce (ICC) and they seek to bring clarity to the management of on-demand bonds – covering notification, amendments, assignment, expiry and demands.

Whilst supportive of that objective, I thought it was worth mentioning that it can cause trouble when a set of rules is incorporated by reference, that is, without being expressed in the executed documents. Things can easily get missed.

Well, things got missed in two recent disputes, both involving Middle East projects.

The first one centered on an Advance Payment Bond securing a payment from Tecnicas Reunidas (TR) to a subcontractor for electro-mechanical works on a project in Saudi Arabia. The subcontractor obtained the bond from the Korean Development Bank and it incorporated URDG.

TR made a call on the bond, having already terminated the subcontract for alleged breach. The bank refused to pay on the basis that a condition of the bond had not been met: namely, that the advance payment was to have been made into a specific numbered account at HSBC, but it was, in fact, made into an account with the same number at the Saudi British Bank (SABB).

The matter came to the Technology and Construction Court in England, which decided in favour of TR on the basis that the parties intended to refer to the SABB account: this was the bank which actually had an account with the stated account

number; and SABB was also a partly-owned subsidiary of HSBC.

So the decision can be understood in terms of rectifying a simple drafting mistake. More interesting were the other TR arguments that were opened up by the incorporation of URDG. Firstly, URDG Article 7 requires (in summary) that any bond condition, apart from a date or time limit, must include reference to a document which will indicate compliance with that condition. Without that, the condition is to be ignored unless compliance can be determined from the guarantor's own records or from an index specified in the bond.

Since the bond did not specify what document TR needed to demonstrate compliance, the court said that the condition should be ignored. The court also liked TR's argument that the bank had failed to give notice of rejection to TR in time. This contravened URDG Article 24 which requires such notice (setting out the discrepancies on which the rejection is based) to be given within five business days of presentation of the demand. Article 24 also states that failure to give a valid notice of rejection will prohibit the guarantor from refusing the demand on the basis of its non-compliance with the bond conditions. Pretty tough!

Very similar issues arose in another dispute on bonds also incorporating URDG. This began with several calls on both a performance bond and an advance payment bond by the beneficiary, Leonardo



Jordan ... rules need to be expressed in the executed documents.

SpA. The calls related to alleged failures by Leonardo's subcontractor PAT Engineering Enterprises Company WLL and those demands were all refused by the issuing bank, Doha Bank Assurance Company LLC.

This eventually came to the Appellate Division of the Civil and Commercial Court of the Qatar Finance Centre (QFC). Among the issues put forward: on the basis that the bond covered sums that Leonardo "might have to claim in writing" from PAT, the bank argued that Leonardo should have sent a written claim to PAT before calling any bond. However, this brought URDG Article 7 into play again. If the bond did require a prior written demand, it did not specify what document would be needed to evidence compliance with that condition. The Appellate Division decided that the requirement for a prior written demand was a "non-documentary condition" and could, therefore, be disregarded.

URDG Article 24 also reappeared here. The bank's above argument was not raised in the initial rejection, so Leonardo argued that the bank had lost the opportunity to object to the bond call because they had failed to notify their rejection within five days, stating each discrepancy on which that rejection was based.

So what should we take from that? URDG and other uniform rules are endorsed by numerous international and construction bodies including Fidic, whose proforma on-demand bonds incorporate URDG. They are supposed to harmonise practice and bring certainty of outcome, but in the above cases, two tripwires (Articles 7 and 24) were tripped over. Parties need to understand the effect of incorporating a lengthy set of rules, especially rules that contain tough consequences for breach; or make an informed decision not to incorporate URDG at all. ■

** Stuart Jordan is a partner in the Global Projects group of Baker Botts, a leading international law firm. Jordan's practice focuses on the oil, gas, power, transport, petrochemical, nuclear and construction industries. He has extensive experience in the Middle East, Russia and the UK.*