

# Performance Bonds in Qatar: Contracts Strike back

**Hani Al Naddaf** - Partner, Head of Litigation - Qatar - Arbitration / Litigation / Construction and Infrastructure / Insurance

h.alnaddaf@tamimi.com - Doha

In light of the importance of this topic, this article intends to shed some light on the treatment of Performance Bonds under Qatari law. In particular, we will identify the ways in which a contractor may resist the arbitrary encashment of such instruments.

## The Nature of the Performance Bond under Qatari Law

All standard form construction contracts (and many bespoke contracts) require the Contractor to submit a Performance Bond to the Employer as a form of guarantee in respect of the former's performance of the contract works. In the event that a Contractor breaches its contractual obligations, the Employer has the option to recoup some or all of his losses by making a call on the Performance Bond, in addition to having recourse to any other available contractual or legal remedies. As such, Performance Bonds are merely intended to operate as guarantees, and not advance payments in respect of monies which a court or arbitral tribunal may or may not later award to the Employer at a merits hearing.

In this jurisdiction, it is common practice for employers to request that a Performance Bond takes the form of an "on demand" Letter of Guarantee from the Contractor's bank ('the Bank') – a document which will unambiguously stipulate that the Bank will remit the full amount of the bond to the Employer upon receipt of written confirmation from the Guarantee's beneficiary (the Employer) that the Contractor has breached its obligations under the contract.

Articles 406 to 413, inclusive, of Qatar's Commercial Law (Law No. (27) of 2006) deal with "on demand" letters of guarantee. Article 406 of the Commercial Law stipulates that:

*"A letter of guarantee is a **written, irrevocable** commitment **issued by a bank** pursuant to the request of one of its clients... **to pay a specified** amount or an amount that can be specified later to... the "beneficiary", if the beneficiary requests it to do so, within the period specified in the letter, **without taking any objection into consideration**. The letter of guarantee shall specify the purpose for which it was issued."* (emphasis added)

Thus, where the contractual wording confirms that the performance guarantee is to take the form of an unconditional on-demand bond – meaning that the full amount of same is payable upon written demand without being subject to any condition – and the beneficiary (Employer) submits such demand to the guarantor (the Bank), the Bank is obliged to honour the call, even if the Contractor disputes liability for the alleged breach, or if the Employer does not know or believe that he is entitled to call on the Bond, or is simply reckless as to whether he is entitled to payment of the sum demanded.

The requirements of the aforementioned Article 406 are further supported by Article 409 of the Commercial Law, which states that a bank shall not be entitled to refuse to pay the beneficiary due to any reason connected to the Bank's relationship with the applicant (that is, the Contractor) or the applicant's relationship with the beneficiary (the Employer).

Based on the above-referenced provisions of Qatari law, it is clear that a bank does not have discretion to decide whether or not a call on a Performance Bond is justified, or whether such a call is arbitrary or fraudulent. Further, the bank is not entitled to refuse to honour a call on a Performance Bond for any reason whatsoever.

## **Remedies Available to the Contractor**

A Contractor has two layers of defence against an arbitrary call by an Employer on a Performance Bond, as follows:

### **A. Taking Action Before the Call is Made**

If a Contractor has serious concerns that the Employer may make a call on the Bond, he can seek injunctive relief from the Court, which would suspend the Employer's right to encash the bond pending the outcome of a hearing on the merits of the Contractor's claim – that is, if the Contractor has filed, or is about to file, a claim against the Employer on the merits.

For the purposes of increasing the likelihood of success in relation to an application for an injunction, the documents submitted by the Contractor in connection with such application will need to persuade the Court that there is a prima facie case to be heard, thus enabling the Court to grant interim relief without making any determination as to the substance, or merits, of the dispute at issue.

The Contractor should look to convince the Court, by way of solid, written evidence, that the Employer is likely abusing his right to call on the Bond. Of particular usefulness here would be evidence confirming that the contract works have been performed substantially or in full (such as, for example, interim or practical completion certificates), or documents which would substantiate an assertion that the Employer's motivation in making the call is to gain some leverage over the Contractor. The nature of the supporting documents will differ from one case to another; however, this kind of injunctive relief is very rarely awarded by the Qatari Courts.

### **B. Acting After the Call**

After an Employer makes a call on a Performance Bond, the Contractor may have recourse to one of the following two remedies:

1. The Contractor may seek an injunction from the Court, on an urgent basis, which would have the effect of estopping the bank from making any payment on foot of the Bond until completion of a full hearing on the merits of the dispute between the parties, assuming that such proceedings have been, or are imminently to be filed by the Contractor against the Employer. However, this option often proves impractical, depending as it does on the speed with which the bank in question reacts to the Employer's written demand for payment of the bond's sum; it may be that the Contractor will not have sufficient time to file injunctive proceedings before payment is remitted to the Employer. In light of the foregoing, it is highly advisable that, where such a call appears imminent, the Contractor undertakes all advance preparations required to support his application for an injunction, such as executing a Power of Attorney in favour of his chosen legal representative(s), and translating any documents to be submitted to the Court into Arabic.
2. If the Contractor fails to obtain an injunction before or after the call on the Bond, he may defend the Employer's allegations as to contractual breach(es), in addition to making any claims he may wish to raise under the Contract, by initiating Court or arbitral proceedings (as appropriate). In the course of such proceedings, in addition to claiming any available contractual or legal rights or remedies, the Contractor may claim the full amount of the Performance Bond paid to the Employer.

## **Conclusion**

Notwithstanding the recent spate of case law on this issue, the treatment of Performance Bonds in Qatar remains largely uncertain. While there appears to be a noticeable reticence on the part of the Qatari Courts to issue injunctions preventing demands against such guarantees being honoured by banks. We have, on occasion, been successful in obtaining such injunctive relief for contractor clients following an arbitrary bond call by an Employer.