

Beware the Boiler-Plate Indemnity

In an important decision for the drafting and negotiation of contracts, the Court of Appeal held that the introduction of a boiler-plate indemnity that had not been specifically negotiated by parties cannot have the effect of overriding the negotiated commercial bargain, structure of the deal and calibrated risk allocation reflected in the contractual documents: *CIFG Special Assets Capital I Ltd (formerly known as Diamond Kendall Ltd) v Ong Puay Koon and others and another appeal* [2017] SGCA 70.

Our Comments

This case is a valuable reminder to exercise caution in the use of, and reliance on, standard or common form boiler-plate provisions.

Indemnities are included in many commercial contracts to allocate risk between contracting parties. However, even in the face of clear wording, the protection afforded by indemnity clauses may not always be what it seems. This is especially so if such indemnity clauses are mechanically inserted in the contract in a “belt and braces” or blunderbuss approach, or if they did not arise from deliberate and intentional negotiations on that precise issue of liability.

Care should be taken to ensure that all boiler-plate provisions dovetail, and are consistent, with the entirety of the contractual documentation. If not, unintended consequences can follow. As this case illustrates, the court will construe such provisions in their relevant context, which can include the entirety of the contractual documentation and the way the contract as a whole was drafted, the factual and

commercial context in which the contract was entered into, and the specific circumstances and negotiations in which such provisions were introduced into the contract.

Following from this, it is also useful to maintain accurate records of key meetings, correspondence and pre-contractual negotiations that may reflect parties’ intentions in respect of important commercial terms.

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Background

CIFG Special Assets Capital I Ltd (“**CIFG**”), an investment vehicle wholly-owned by a mezzanine investment fund, agreed to finance the acquisition of certain manufacturing companies by Polimet Pte Ltd (“**Polimet**”).

By a set of convertible bond subscription agreements (“**CBSAs**”), CIFG provided loans to Polimet by subscribing for convertible bonds issued by Polimet. The initial shareholders of Polimet (the “**Initial Shareholders**”) were party to the CBSAs.

The negotiations leading up to the entry into the CBSAs included the following discussions on how the loans were to be secured:

- There were background negotiations between parties as to the provision of personal guarantees, the extent of the guarantees and which of the Initial Shareholders were to provide such guarantees. This was reflected in the

draft term sheet (“**Term Sheet 1**”), which broadly provided that personal guarantees were required by CIFG.

- Parties eventually signed a final term sheet (“**Final Term Sheet**”) containing the agreed and material terms of the commercial bargain. The Final Term Sheet reflected the agreed term that only two of the Initial Shareholders were to provide joint and several personal guarantees and their exposure would be limited to their initial 50% stake in Polimet.
- The Final Term Sheet also contained a provision that Polimet (and not the Initial Shareholders) would indemnify CIFG. However, this was not specifically discussed by parties in the context of how the loan would be secured.
- After the Final Term Sheet was signed, CIFG’s shareholder circulated drafts of the CBSAs and the personal guarantees. The indemnity clause (the “**Indemnity Clause**”) contained in the draft CBSAs and which found its way into the executed CBSAs was reviewed for the first time by parties at a meeting in Salzburg (the “**Salzburg Meeting**”). The Indemnity Clause differed from the provision originally contained in the Final Term Sheet at least in that the indemnity was to be granted not only by Polimet but also each of the Initial Shareholders. The Indemnity Clause is reproduced as follows:

12.1 General Indemnity. The Initial Shareholders and the Issuer hereby jointly and severally agree and undertake to fully indemnify and hold the Bondholder and its shareholders and their respective fund managers, directors, officers and employees (the “**Indemnified Parties**”) harmless from and against any claims, damages, deficiencies, losses, costs, liabilities and

expenses (including legal fees and disbursements on a full indemnity basis) directly or indirectly caused to the Indemnified Parties and in particular, but without prejudice to the generality of the foregoing, for any short-fall, depletion or diminution in value of the assets of the Issuer, the Group or any Group Company resulting directly or indirectly from or arising out of any breach or alleged breach of any of the representations, warranties, undertakings and covenants given by the Initial Shareholders and/or the Issuer under this Agreement or for any breach or alleged breach of any term or condition of this Agreement.

- The executed CBSAs entered into after the Salzburg Meeting contained the Indemnity Clause. As part of the commercial bargain, CIFG also obtained as security: (i) charges over the assets of all the manufacturing companies, (ii) personal guarantees from two of the Initial Shareholders for up to 50% of Polimet’s liabilities under the CBSAs, and (iii) the Initial Shareholders’ shares in Polimet (which would be transferred back to them once the loan facility was fully discharged).

Polimet eventually defaulted on the loans. CIFG then commenced action against Polimet *and* the Initial Shareholders in respect of the entirety of Polimet’s debts under the CBSAs pursuant to the Indemnity Clause.

The High Court’s Decision

The High Court found that, on its true construction, the Indemnity Clause was not so wide as to enable CIFG to claim the entirety of its losses arising from Polimet’s default against each of the Initial Shareholders on a joint and several basis. (Please click [here](#) for our update on the High Court’s decision.)

The Court of Appeal's Decision

The Court of Appeal agreed with the High Court's findings, although it differed a little in its reasoning and the construction of the Indemnity Clause.

For starters, the Court noted that the Indemnity Clause was extremely broad, both as to the class of beneficiaries as well as to the matters conceivably covered by the indemnity. In the Court's view, such breadth made it absurd to construe the clause on its plain terms without regard to the relevant context. Evidently, the language simply could not mean what it said. It was therefore critical to consider its context.

Applying the relevant principles in the construction of contracts, the Court ruled that the Indemnity Clause, construed against the relevant context, clearly could *not* – even though the plain words on their own might allow this – make each of the Initial Shareholders liable for all of Polimet's debts under the CBSAs.

CBSAs specifically allocated risk to various parties

The Court noted that the CBSAs in their entirety specifically allocated risks variously to Polimet, the Initial Shareholders or to a combination of some or all of them. For example, the default clause of the CBSAs made Polimet liable for the loan and two of the Initial Shareholders liable under the personal guarantees to the extent that they undertook to be so liable.

It was thus inconsistent to then provide, by way of the Indemnity Clause, that Polimet, the two guarantors and each of the Initial Shareholders would additionally be liable for the entirety of the loan. In light of the obligations variously placed on Polimet, the Initial Shareholders or some combination of them, it was unlikely that the Indemnity Clause had the effect of overriding the entire allocation of the risks under the CBSAs.

Draft and executed term sheets and personal guarantees conflict with wide construction of Indemnity Clause

In addition, the Court observed that the question of security and the points agreed on by the parties were reflected in the successive term sheets. While Term Sheet 1 provided generally for personal guarantees to be furnished, the Final Term Sheet (executed by parties) required personal guarantees to be furnished by only two of the Initial Shareholders, and even then, limited to the extent of their shareholding in Polimet.

In the Court's judgment, this militated strongly against a wide construction of the Indemnity Clause that made all of the Initial Shareholders answerable for each and the entirety of the obligations under the CBSAs including Polimet's indebtedness. If so, the personal guarantees would have been unnecessary and otiose. Further, the fact that CIFG pursued and obtained the personal guarantees from just two of the Initial Shareholders, and for only half of the total liability of Polimet, undermined CIFG's case for a wide construction of the Indemnity Clause.

Circumstances in which the Indemnity Clause was introduced into the CBSAs

It was common ground among the parties to appeal that the Indemnity Clause was first introduced at the Salzburg Meeting. It was also undisputed that no one mentioned at that time that the Indemnity Clause would change the commercial structure of the deal, and that the clause was read over by those at the meeting but its scope and effect were not discussed. In fact, the Indemnity Clause was introduced as a boiler-plate provision to complete the contractual documentation.

The Court took the view that it was impossible for a common form boiler-plate provision (such as the Indemnity Clause) that made its way into the CBSAs at the last stages of negotiations could have the effect of overriding the commercial

structure of the deal and the calibrated allocation of risk that was reflected elsewhere in the suite of transaction documents that were entered into. Read in context, the Indemnity Clause was nothing more than a gap-filling provision injected

into the contract at a late stage to cover matters, if and to the extent those matters were not already covered elsewhere.

As a result, the Court dismissed the appeal.

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