



**THE IMPACT OF THE AMENDMENT TO THE  
PRINCIPLE OF SURETYSHIP UNDER THE CIVIL AND  
COMMERCIAL CODE AMENDMENT ACT, (NO.20 AND  
NO.21), ON THE SECURITY FORMS UNDER THE  
CONSTRUCTION CONTRACT FOR LARGE PROJECT**

**BY**

**MR. PAKORN SIRINANTHANANON**

**A THESIS SUBMITTED IN PARTIAL FULFILLMENT OF THE  
REQUIREMENTS FOR THE DEGREE OF MASTER OF LAWS  
IN BUSINESS LAWS (ENGLISH PROGRAM)**

**FACULTY OF LAW**

**THAMMASAT UNIVERSITY**

**ACADEMIC YEAR 2015**

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THESIS

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MR. PAKORN SIRINANTHANANON


ENTITLED

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UNDER THE CIVIL AND COMMERCIAL CODE AMENDMENT ACT, (NO.20  
AND NO.21), ON THE SECURITY FORMS UNDER THE CONSTRUCTION  
CONTRACT FOR LARGE PROJECT


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Thesis Title	THE IMPACT OF THE AMENDMENT TO THE PRINCIPLE OF SURETYSHIP UNDER THE CIVIL AND COMMERCIAL CODE AMENDMENT ACT, (NO.20 AND NO.21), ON THE SECURITY FORMS UNDER THE CONSTRUCTION CONTRACT FOR LARGE PROJECT
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## **ABSTRACT**

A guarantee, which is given by any third party, is one of the important securities required under a construction contract for large projects. Throughout the terms of construction contract, the contractor has many duties, responsibilities and obligations which are executed in accordance with the terms and conditions thereunder. Significant duties of the contractor are (i) the duty to complete the construction work within the schedule, which can be divided into sub schedules, called milestones, and (ii) the duty to achieve all guaranteed figures of the construction work. If the contractor fails to make the construction work in accordance with their duties, the owner shall be entitled to claim the damages from the contractor. In order to ensure that the contractor has capability to pay the damages to the owner, the owner shall require an additional security from the contractor and it is most likely a third party guarantee is one.

There are many types of third-party guarantee which are used in the construction business in Thailand, for instance, a performance guarantee, a retention money guarantee, and an advance payment guarantee, but most of these third-party

guarantees, which are used, are subject to the law of suretyship under Thai Civil and Commercial Code (“CCC”). The amendment to significant principles of the law of suretyship in 2014 and 2015 introduced (i) additional duties, for instance, duty to notify the guarantor when the contractor has defaulted or the contractor and the owner have an agreement concerning the reduction of the secured amount, and (ii) the prohibition against an agreement that the guarantor binds himself as primary obligor or grants an advance consent on the time extension, although exceptions thereof were added by the latter amendment.

This thesis studied (i) the suitability of the third-party guarantee, which is governed by the amendments to the principle of suretyship under the CCC, to be an additional security under the construction contract for large projects and (ii) the possibility of using the guarantees from the third party under international laws or practices, namely a standby letter of credit in accordance with International Standby Practices (ISP98) and an independent guarantee and a stand-by letter of credit in accordance with United Nations Convention on Independent Guarantees and Stand-by Letters of Credit (Convention), in lieu of this third party guarantee by comparing the advantages and disadvantages on issues of third-party guarantees.

From the study, it is found that the additional duty of the owner, as a creditor to the construction contract, to notify the guarantor is dissimilar from international laws and practices that the construction contract for large projects mostly has to comply with. Hence, if the third-party guarantee was used in the construction contract, as suretyship, related parties have to educate himself and understand this amended principle to practice accordingly. The thesis also explored whether the additional duties and prohibitions under the amended principle of suretyship can be relieved by the use of a standby letter of credit covered by the ISP 98 and an independent guarantee and a stand-by letter of credit covered by the Convention, but, either of them also has an issue concerning the application mechanism under Thai Law. If parties to the construction contract wish to use these international laws and practices, such parties have to take this issue into consideration, and apply international laws and practices, whether the ISP 98 or the Convention which is fitted for their fact and situation.

**Keywords:** Guarantee, Suretyship, Amended Principle of Suretyship, Standby Letter of Credit, Independent Guarantee, ISP 98, United Nations Convention on Independent Guarantees and Stand-by Letters of Credit, Construction Contract, Large Projects



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## TABLE OF CONTENTS

	Page
ABSTRACT	(1)
ACKNOWLEDGEMENTS	(4)
LIST OF ABBREVIATIONS	(9)
CHAPTER 1 INTRODUCTION	1
1.1 Background and Issues	1
1.1.1 Background	1
1.1.2 Issues	5
1.2 Hypothesis	10
1.3 Objectives of Study	11
1.4 Scope of Study	12
1.5 Methodology of Study	15
1.6 Anticipated Benefits	16
CHAPTER 2 THE THIRD PARTY GUARANTEE UNDER THE CONSTRUCTION CONTRACT	17
2.1 Construction Contract	17
2.1.1 Definition of Construction Contract	17
2.1.2 Types of Construction Contract	17
2.1.3 FIDIC® Conditions of Contract	22
2.1.3.1 FIDIC Red Book	23
2.1.3.2 FIDIC Yellow Book	24
2.2 Obligations and Liabilities of the Contractor to the Construction Contract	25



2.2.1	Obligation of the Contractor	25
2.2.1.1	Obligation to Complete	25
2.2.1.2	Obligation upon the Design and Quality of Materials and Work	25
2.2.1.3	Obligation upon the Progress	26
2.2.1.4	Obligation as to Cost	27
2.2.2	Liabilities of Contractor	27
2.3	Third Party Guarantees under the Construction Contract	30
2.3.1	Types of the Third Party Guarantee under the Construction Contract	30
2.3.1.1	Performance Guarantee	30
2.3.1.2	Advance Payment Guarantee	31
2.3.1.3	Retention Money Guarantee	32
2.3.1.4	Parent Company Guarantee or Corporate Guarantee	33
2.3.2	Principles of Guarantee under the Construction Contract	34
2.3.2.1	Parties to the Third Party Guarantee	35
2.3.2.2	The Status of Guarantor	35
2.3.2.3	Payment Condition	35
2.3.2.4	Extension of Time	36
2.3.2.5	Withdrawal of the Third Party Guarantee	36
2.3.2.6	Expiration of the Third Part Guarantee	37
<b>CHAPTER 3 THE INTERNATIONAL PRACTICES OF THE THIRD PARTY GUARANTEE</b>		<b>38</b>
3.1	The Standby Letter of Credit covered the ISP 98	38
3.1.1	Purpose of the Standby Letter of Credit covered the ISP 98	38
3.1.2	Significant Principles of the Standby Letter of Credit covered by the ISP 98	39
3.2	The Independent Guarantees or Stand-by Letters of Credit covered by the Convention	43
3.2.1	Purpose of the Convention	43

3.2.2 Significant Principles of the Undertaking covered the Convention	43
3.3 The Third Party Guarantee under the CCC and International Practices	47
3.3.1 Comparison of the Third Party Guarantee under the CCC, the ISP 98 and the Convention	47
3.3.1.1 Scope and Application of the Rule to the Third Party Guarantee	48
3.3.1.2 Independent feature of the Third Party Guarantee	48
3.3.1.3 Internationality of the Third Party Guarantee	49
3.3.1.4 The Documentary Characteristic	50
3.3.1.5 Responsibility of Guarantor or Issuer as Joint Debtor	50
3.3.1.6 Duty of Beneficiary when Principal/Applicant is in Default	51
3.3.1.7 Duty of Beneficiary when Reduction of the Amount of Secured Debt	52
3.3.1.8 Extension of Time	52
3.3.1.9 Exception to the Payment Obligation	53
 CHAPTER 4 THE AMENDMENT OF SURETYSHIP AND EFFECTS	 55
4.1 Principal of Suretyship under the CCC	55
4.1.1 Relationship between Suretyship and Third Party Guarantee under the Construction Contract	55
4.1.2 Principle of Suretyship	55
4.1.2.1 The Primary Principle of Suretyship	56
4.1.2.2 The Amended Principle of Suretyship	57
4.2 The Effect of the Amended Principle of Suretyship under the CCC to the Third Party Guarantee under the Construction Contract	65
4.2.1 Details of the Third Party Guarantee	65
4.2.2 Joint Liability of Guarantor	66

4.2.3 Extension of Time	67
4.2.4 Default of the Contractor	69
4.2.5 Reduction of the Debt for the Contractor	72
4.2.6 The enforceability of the Third Party Guarantee made during the period after the effective date of CCC Amendment NO.20 to the date before the effective date of CCC Amendment No.21	73
4.3 Mitigation of the Effect of the Amendment of Principle of Suretyship under the CCC to the Third Party Guarantee by Using the Third Party Guarantee under the ISP, 98 and the Convention	75
 CHAPTER 5 CONCLUSIONS AND RECOMMENDATIONS	 78
5.1 Conclusions	78
5.2 Recommendations	80
 REFERENCES	 83
APPENDICES	88
 APPENDIX A Form of security under the FIDIC Red Book	 89
APPENDIX B Form of security under the FIDIC Yellow Book	94
APPENDIX C Table: Comparison of the use of the Third Party Guarantee governed by the amendment principle of suretyship under the ccc, the standby letter of credit covered by the ISP 98 and the undertaking covered by the Convention	99
 BIOGRAPHY	 102

## LIST OF ABBREVIATIONS

<b>Symbols/Abbreviations</b>	<b>Terms</b>
CCC	Civil and Commercial Code of Thailand
CCC Amendment No.20	Civil and Commercial Code Amendment Act, (No.20), B.E. 2557
CCC Amendment No.21	Civil and Commercial Code Amendment Act, (No.21), B.E. 2558
Convention	United Nations Convention on Independent Guarantees and Stand-by Letters of Credit
EIT	The Engineering Institute of Thailand Under H.M. The King's Patronage
FIDIC	International Federation of Consulting Engineers
FIDIC Red Book	FIDIC <sup>®</sup> Conditions of Contract for Construction for Building and Engineering Works designed by the Employer
FIDIC Yellow Book	FIDIC <sup>®</sup> Conditions of Contract for Plant and Design Build for Electrical and Mechanical Plant, and for Building and Engineering Works designed by the Contractor
ISP 98	International Standby Practices
UNCITRAL	United Nations Commission on International Trade Law
URDG 758	ICC Uniform Rules for Demand Guarantees (URDG 758) and Model Forms

# CHAPTER 1

## INTRODUCTION

### 1.1 Background and Issues

#### 1.1.1 Background

One of the significant obligations of the parties to the construction contract for large projects is an obligation to guarantee. Under the construction contract, many kinds of guarantee were given by a contractor to the construction contract (“Contractor”) to an owner to the construction contract (“Owner”), for instance, (i) the completion guarantee wherein the Contractor guarantees that a construction work under the construction contract will be completed within the agreed timeline, or (ii) the performance guarantee wherein the Contractor guarantees that the completed construction work will be achieved or will meet any and all guarantee figures, which the parties have agreed upon. To the extent that any guarantee that was given by the Contractor is not achieved for reason attributable to the Contractor, the Owner shall be entitled to request the Contractor to pay the damages whether the actual damages or the liquidated damages in accordance with the terms of the construction contract. However, in order to ensure that the Owner will receive such damages, when executes their right, from the Contractor, a guarantee from any third party, as the guarantor, for instance, the parent company of the Contractor, a commercial bank, or a financial institution, (“Third Party Guarantee”) shall be required by the Owner from the Contractor.

The process of the construction can be divided into three major stages as follows:

(1) The Pre-Construction stage<sup>1</sup>

At this stage, the main responsibility of the Owner is to prepare (i) the bid documents containing technical specifications and commercial specifications and (ii) the draft construction contract, while, main responsibilities of

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<sup>1</sup> Weerapong Srinawakul and Tanaporn Srinawakul, **Construction Management and Method**, (Bangkok: Datum Thai Construction Company Limited, 2550), 2-3.

the Bidder, are to (i) prepare and submit the bid proposal which, in practice, consist of the technical and commercial proposals and (ii) review and comment upon the draft construction contract and submit the adjusted draft construction contract to the Owner within the schedule. After the Owner receives the bid proposal from all Bidders, the Owner has to consider whether the bid proposal comply with the terms of the bid documents or not. Then, the negotiation between the Owner and a potential Bidder concerning the terms and conditions under construction contract shall be executed and finalized. After that, the potential Bidder will be awarded to be the Contractor.

(2) The Construction stage<sup>2</sup>

At this stage, the main responsibility of the Contractor is to perform and complete the construction work in accordance with (i) all specifications and guarantees of the construction work and (ii) all terms and conditions under the construction contract, while, the main responsibility of the Owner is to manage and control the construction work (“Construction Managements”).

(3) The Post-construction stage<sup>3</sup>

At this stage, main responsibilities of the Contractor are (i) to hand over the completed construction work to the Owner and (ii) to warrant that the completed construction work shall be in compliance with the terms and conditions under the construction contract for the agreed period after such construction work is accepted by the Owner (“Warranty Period”), while, main responsibilities of the Owner are (i) to inspect the completed construction work, (ii) to consider whether the completed construction work is in accordance with the terms and conditions of the construction contract, and (ii) to accept such construction work. The Contractor shall be released from their contractual obligations under the construction contract when the Warranty Period expires without any claim from the Owner.

The Third Party Guarantee is used through every stage of the construction process from the beginning until the completion of the construction work, where the Contractor is discharged from their obligations. For example, (i) during the bidding process, in addition to the proposal, the Bidder shall provide a

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<sup>2</sup> *Id.*

<sup>3</sup> Wisoot Jiradamkerng, **Construction Planning and Scheduling**, 4<sup>th</sup> Edition, (Bangkok: Wan Kawee 2003), 16.

Third Party Guarantee to the owner to guarantee that if the Bidder is selected to be a contractor to the construction contract, the Bidder will enter into the construction contract with the Owner under the terms and conditions as provided under the proposal which are accepted by the Owner. If the awarded Bidder does not enter into such construction contract, the Owner shall be entitled to claim damages whether from the Bidder himself or the Third Party Guarantee, (ii) during the negotiation of the construction contract, the Contractor may request the Owner that after signing the construction contract, the Contractor shall be entitled to receive advance money from the Owner. If the Owner agrees with such request, even if the Owner is entitled to receive such advance money back by proportional reduction from any payment made to the Contractor during the construction period, in practice, the Owner will request the Contractor to provide a Third Party Guarantee in the amount which is equal to such advance money as an additional security, or (iii) during the construction phase where the Contractor has to execute the construction work in accordance with the terms of the construction contract, the Owner might request the Contractor to provide a Third Party Guarantee to guarantee that the Contractor shall completely perform their in accordance with the construction contract, otherwise the Owner shall be entitled to claim from said Third Party Guarantee in addition to the Contractor himself.

In general, the Third Party Guarantee shall consist of the following terms:

(1) "... we agree unconditionally to irrevocably guarantee as primary obligator, the payment to the owner on its first demand, without whatsoever right of objection on our part and without its first claim on the contractor in the amount of not exceeding..... in the event of any damages, liquidated damages (penalty), expenses or if any obligations expressed in the above mentioned Contract has not been fulfilled by the contractor".<sup>4</sup>

Since there is no specific law concerning Third Party Guarantees or independent guarantees in Thailand, the principle of law which is used to govern or

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<sup>4</sup> The Office of Prime Minister, "Letter Number NorRor (KorWorPor) 1202/Vor 112 Examples of Bid Documents for Sale and Service Contracts, Letter of Guarantee, Material Accounts and Equipment Lists," 1 April B.E. 2535, 2-29.

interpret the Third Party Guarantee should be the principle of suretyship under the Civil and Commercial Code of Thailand (“CCC”) as the provision closest to the case. A suretyship under the CCC is a contract in which a third party, who is called the surety, agrees to bind himself to a creditor in order to satisfy an obligation in the event that the debtor fails to perform it.<sup>5</sup> Under the principle of suretyship, the creditor shall be entitled to demand performance of the obligation from the surety only when the debtor is in default<sup>6</sup> but, even when the creditor has demanded performance from the surety, the surety is entitled to require the creditor that the debtor shall be first demanded to perform.<sup>7</sup> As governed by this principle, the guarantor to the Third Party Guarantee also has such refusal right.

Since the Third Party Guarantee is intended to use conveniently by the Owner, as the creditor, in order to avoid the use of the foregoing right by the guarantor, the guarantor shall agree to guarantee under the Third Party Guarantee as the primary obligor, which means that the guarantor does not have such refusal right under the principle of suretyship.<sup>8</sup>

(2) “If, at any time in the course of the execution of the above mentioned Contract, the owner grants a time extension, or allows the contractor to deviate from any terms and conditions of the Contract without our knowledge, it shall be deemed that such grants shall have been made with our consent”.<sup>9</sup>

Under the principle of suretyship, in the event that the obligation under the underlying transaction is to be performed at a definite time, if the creditor grants an extension of time of such obligation to the debtor, the surety shall be discharged, unless the surety has agreed to such extension of time.<sup>10</sup> Thus, in order to avoid the event that the guarantor under the Third Party Guarantee is discharged due to the extension of time by the Owner, the Owner shall request the guarantor to grant the extension of time in advance.

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<sup>5</sup> Section 680 paragraph 1 of the CCC.

<sup>6</sup> Section 686 of the CCC.

<sup>7</sup> Section 688 of the CCC.

<sup>8</sup> Section 691 of the CCC.

<sup>9</sup> The Office of Prime Minister, *Supra* note 4.

<sup>10</sup> Section 700 of the CCC.



(3) “This Letter of Guarantee shall be valid and in full force and effect from the date of execution of the above-mentioned Contract until all obligations on the part of the contractor have been fulfilled”.<sup>11</sup>

(4) “We shall in no event withdraw this letter of Guarantee for any reasons so far as the contractor is still liable under the above mention Contract”.<sup>12</sup>

Under the principle of suretyship, if the obligations under the underlying transaction are extinguished by any whatsoever cause, the surety shall be discharged.<sup>13</sup> Hence, in order to avoid the interpretation argument that may happen when the Contractor has many obligations under the construction contract and some of obligations are extinguished, on whether the guarantor is discharged, the Third Party Guarantee shall expressly specifies that the suretyship is valid until all obligations of the Contractor are fulfilled or extinguished and that the guarantor shall not withdraw the Third Party Guarantee prior to such event.

Having considered the details of the foregoing terms that are generally specified in a form of the Third Party Guarantee, it is found that many terms of the Third Party Guarantee rely on the principle of suretyship under the CCC.

### **1.1.2 Issues**

The principle of suretyship under the CCC is one of the legal principles that had not been amended since Book 3 of the CCC was firstly proclaimed in B.E. 2471. However, in B.E. 2557, the first amendment to the principle of suretyship was laid down by Civil and Commercial Code Amendment Act, (No.20), B.E. 2557 (“CCC Amendment No.20”) that was proclaimed in the Royal Gazette on 13 November B.E. 2557 and became effective on 11 February B.E. 2558. This amendment is due to the fact that existing principles of suretyship are not enough to protect the surety which is not the primary debtor and, in practice, the creditor, who mostly has more bargaining power, often requests the surety to be liable as the primary obligor. This renders the surety unprotected under the principle of suretyship. The followings are some of the significant principles of suretyship that are amended under the CCC Amendment No.20:

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<sup>11</sup> The Office of Prime Minister, *Supra* note 4.

<sup>12</sup> The Office of Prime Minister, *Supra* note 4.

<sup>13</sup> Section 698 of the CCC.

(1) A future or conditional obligation may be secured for the event in which it would have effect, provided that the following information shall be specified in the contract of suretyship: (i) a purpose of creation of the obligation secured; (ii) a character of the obligation secured; (iii) the maximum amount of the suretyship; and (iv) a period of suretyship unless it is the suretyship for series of transaction, as specified in the Section 699, such period of suretyship shall not be specified.<sup>14</sup>

To the extent that the suretyship is given for a future or conditional obligation, this amended principle of suretyship requests, in addition that, the foregoing facts, as specified in (i) to (iv), must be specified. The suretyship for the future of conditional obligation which does not specified such facts shall be void under this amended principle.<sup>15</sup>

(2) Neither the surety agrees to be jointly liable with the debtor, nor to be liable as primary obligor to the creditor.<sup>16</sup>

The rationale of the CCC Amendment No.20 reflects directly to this Section. This amended principle of suretyship absolutely prohibits an agreement that requests the surety to be jointly liable with the debtor or binds himself as a primary obligor. As the result of this amended principle, the surety will always have the following refusal rights: (i) the right to request the creditor to demand performance from the debtor first,<sup>17</sup> (ii) the right to request the creditor to make an execution against the property of the debtor first,<sup>18</sup> and (iii) the right to request the creditor to make an execution against the real security of the debtor which the creditor has already held first.<sup>19</sup> This amended principle with the provision of the Third Party Guarantee means that clause in which the guarantor agrees to guarantee as a primary obligor shall be void. Hence, this amended principle of suretyship makes the massive effect to the material function of the Third Party Guarantee, which is intended to be used conveniently by the Owner.

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<sup>14</sup> Section 681 paragraph 2 of the CCC that was amended by the CCC Amendment No.20.

<sup>15</sup> Section 685/1 of the CCC that was amended by the CCC Amendment No.20.

<sup>16</sup> Section 681/1 of the CCC that was amended by the CCC Amendment No.20.

<sup>17</sup> Section 688 of the CCC.

<sup>18</sup> Section 689 of the CCC.

<sup>19</sup> Section 690 of the CCC.

(3) To the extent that the debtor is in default, the creditor shall notify such default to the surety within 60 days from the default date. If the creditor fails to notify the surety, the surety shall be released from any interest and compensation of such underlying obligation which occur after 60 days from the default date.<sup>20</sup>

The amended principle of suretyship adds this duty of the creditor in order to protect the surety from the interest and compensation, including charges which occur without limit when the credit does not execute their right to demand the performance from the surety or the debtor while the surety may not be aware of the debtor's default. This is the duty of the Owner to the Third Party Guarantee, as additional duty; if the Contractor is in default of any of their duties in the construction contract, which causes the right to the Owner to claim the damages from the Contractor, the Owner shall notify such default to the guarantor within 60 from the default date.

(4) To the extent that any act of the creditor causes the reduction of the amount of underlying obligation, including interest, compensation, or charges, the surety shall also receive such reduction.<sup>21</sup>

The amended principle of suretyship extends this privilege of reduction, granted from the creditor and the debtor, to the surety in order to protect them, as a secondary debtor, from being more liable than the debtor. This privilege is extended to the guarantor to the Third Party Guarantee; if the Owner agrees to waive any penalty under the construction contract to the Contractor, the guarantor shall be also receive such privilege.

(5) To the extent that the underlying obligation is to be performed at a definite time, if the creditor grants an extension of time to such underlying obligation, the surety shall be discharged unless the surety has agree with such extension of time. However, the consent of an extension of time which is made in advance is not enforceable.<sup>22</sup>

The amended principle of suretyship prohibits the advance consent to the extended time of specified underlying obligation. The amended principle does not,

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<sup>20</sup> Section 686 of the CCC that was amended by the CCC Amendment No.20.

<sup>21</sup> Section 691 of the CCC that was amended by the CCC Amendment No.20.

<sup>22</sup> Section 700 of the CCC that was amended by the CCC Amendment No.20.

however, prohibit the consent to the extended time given at or after the time when creditor grants such extension of time. Thus, the advance consent for an extension of time specified in the Third Party Guarantee is no longer enforceable.

Since the terms of the Third Party Guarantee rely on the principle of suretyship the amendments of the principle of suretyship significantly affect the provisions of the Third Party Guarantee including the duties or liabilities of any related parties. Some amendments, e.g. the prohibition of the surety to be a primary obligor, bring the suitability of Third Party Guarantee for the construction contract for large projects into question; if the Contractor is in default on his obligation under the construction contract, e.g. if the construction work is delayed from the schedule of work due to a reason attributable to the Contractor, the Owner is entitled to demand for the penalty. And if the Owner decides to demand such penalty from the guarantor under the Third Party Guarantee, the guarantor shall have the right request the Owner to demand from the Contractor first. If the Owner demands such penalty from the Contractor, it may affect the cash flow of the Contractor or the Contractor may defend against such demand or claim of the Owner. Both events will affect or interrupt the execution of the construction work. This situation which the Owner, normally, tries to avoid and they may be compelled by such effect to do nothing.

However, after the CCC Amendment No.20 was proclaimed, there were requests from commercial banks, financial institutions or other persons involved with the Third Party Guarantee, to amend the amended principle of suretyship under the CCC Amendment No.20 due to various rationales; some of them have been described above.

Consequently, the Civil and Commercial Code Amendment Act, (No.21), B.E. 2558 (“CCC Amendment No.21”) was proclaimed in the Royal Gazette on 14 July B.E. 2558 and became effective on 15 July B.E. 2558. The rationales of this amendment are to conform with current business practice by allowing juristic persons to bind themselves as the primary obligors to the suretyship and financial institutions or a person who undertakes suretyship business for remuneration to give the advance consent for an extension of time.<sup>23</sup> This means the CCC Amendment

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<sup>23</sup> Remark of the CCC Amendment No.21.

No.20 was amended. The followings are some of significant principles of suretyship that are amended under the CCC Amendment No.21:

(1) The surety cannot agree to be jointly liable with debtor or cannot be liable as primary obligor to the creditor, unless the surety is a juristic person who agrees with such agreement.<sup>24</sup>

The amendment to the principle of suretyship under the CCC Amendment No.21 (“Amendment No.2”) adds an exception of the amendment to the principle of suretyship under the CCC Amendment No.20 (“Amendment No.1”). Under the Amendment No.1, the surety cannot agree to be jointly liable with the debtor nor can they bind himself as a primary obligor to the creditor. However, under the Amendment No.2, if the surety is a juristic person and agrees to bind himself as a primary obligor, such prohibition does not apply. So, if the guarantor to the Third Party Guarantee is a juristic person, such guarantor can agree to bind himself as a primary obligor. The Amendment No.2 can correct most of the obstacles which occur from the prohibition under the Amendment No.1. Nevertheless, if the guarantor is an ordinary person, such obstacle remains.

(2) To the extent that an agreement between the creditor and the debtor causes the reduction of the amount of underlying obligation, including interest, compensation, or charges, the surety shall be notified by the creditor of an agreement in writing within 60 days from the date of the said agreement and shall receive the same reduction.<sup>25</sup>

Aside from additional privileges of the surety under the Amendment No.1, the Amendment No.2 adds the creditor’s duty to notify the surety, in writing, of the agreement within 60 days from the date of agreement.

(3) To the extent that the underlying obligation is to be performed at a definite time, if the creditor grants an extension of time to such underlying obligation, the surety shall be discharged unless the surety has agree with such extension of time. However, the consent of an extension of time which is made in

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<sup>24</sup> Section 681/1 paragraph 1 and 2 of the CCC that was amended by the CCC Amendment No.21.

<sup>25</sup> Section 691 of the CCC that was amended by the CCC Amendment No.21.

advance is not enforceable, unless the surety is a financial institution or a person who undertakes suretyship business for remuneration.<sup>26</sup>

The Amendment No.2 adds some exceptions to the Amendment No.1. If the surety is a financial institution or a person who undertakes suretyship business for remuneration, they can give the advance consent concerning the extension of time to the underlying obligation. So, if the guarantor to the Third Party Guarantee is a financial institution or a person who undertakes suretyship business for remuneration, such guarantor can give the advance consent to the creditor. However, if the guarantor is not a financial institution or a person who undertakes suretyship business for remuneration, the advance consent shall not be enforceable.

Even though the proclamation of the CCC Amendment No.21 can correct some significant effects, caused by the CCC Amendment No.20, on the Third Party Guarantee under the construction contract, others significant effects still exist; for instance, (i) the duty of the Owner, as the creditor, to notify the guarantor at any time that the Contractor is in default under the terms of the construction contract, (ii) the duty of the Owner to notify the guarantor at any time that the Owner and the Contractor reach an agreement concerning the reduction or waiver of the underlying obligation, and the privilege that the guarantor can receive by virtue of such an agreement, and (iii) an unenforceability of the advance consent that is given by the guarantor, who is an juristic person but is not a financial institution, such as the parent company of the Contractor. More detail of the forgoing effects shall be described in the later Chapter. The foregoing effects, which are not corrected by the CCC Amendment No.21, still lead to the problem; whether the Third Party Guarantee, which is governed by the CCC, is suitable for the use as a security under the construction contract for large projects.

## **1.2 Hypothesis**

Even though a construction work is only a part of the manufacture business, the business may not carry on if the construction work is not completed. So,

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<sup>26</sup> Section 700 of the CCC that was amended by the CCC Amendment No.21.

the simple aims of any construction work are that the construction work must (i) be completed within the prescribed time, and (ii) meet the guarantee figures. If the Contractor cannot complete any part of the construction work within the prescribed time, the Owner shall be entitled to claim the liquidated damages from the Contractor. Sometimes, in order to encourage the Contractor to speed up their performance, the Owner may agree to reduce such liquidated damages. However, under the amended principle of suretyship under the CCC Amendment No.21, if the Owner and the Contractor agree to reduce the underlying obligation, the Owner shall notify an agreement to all guarantors. So, if the Owner wishes to make such agreement with the Contractor, the Owner shall take the result, which arises from the amended principle of suretyship, into consideration. The foregoing is only one situation that occurs in a construction contract when the Third Party Guarantee is used as additional security of the Contractor, due to the CCC Amendment No.21.

Thus, the hypothesis of this thesis is that the Third Party Guarantee, which is governed by the amended principle of suretyship under the CCC Amendment No.20 and the CCC Amendment No.21, is no longer suitable to be an additional security under the construction contract for large projects and there is a possibility of using the guarantee from the third party under the international law or practice, i.e. ISP 98 and the Convention, in lieu of such Third Party Guarantee.

### **1.3 Objectives of Study**

The followings are the objectives of this research

- (1) To study the general principle concerning the Third Party Guarantee, governed by the CCC, under the construction contract.
- (2) To study significant effects from the amendments of the principle of suretyship under the CCC by the CCC Amendment No.20 and the CCC Amendment No.21, including significant effects from such amendments to the Third Party Guarantee under the construction contract.
- (3) To study the international laws and practices concerning the guarantee from the third party and compare such international laws and practices and the amendments of the principle of suretyship under the CCC.

(4) To compare and summarize the advantages and disadvantages among the selected guarantee from the third party under the international laws and practices and the Third Party Guarantee which is governed by the CCC, as amended, including giving the conclusion and suggestions concerning this issue.

#### **1.4 Scope of Study**

This thesis focuses on (i) the principle of the Third Party Guarantees, governed by the CCC, under the construction contract for large projects, (ii) the comparison of the Third Party Guarantee which is governed by the CCC, as amended by the CCC Amendment No.20 and the CCC Amendment No.21, and the guarantee from the third party in accordance with the international laws and practices, and (iii) the summary of the possibility and suitability of the use of the guarantee from the third party which is covered by the international laws and practices, i.e. ISP 98 and the Convention, in lieu of the use of the Third Party Guarantee which is governed by the principle of suretyship under CCC, as amended.

Hence, this thesis's scope of study is limited as follows:

(1) The size of the construction projects, studied under this thesis, is large construction projects. In order to define large construction projects, the following conditions shall be taken into consideration:

(i) Types of construction work

Under Building Control Act, B.E. 2522, an extra-large building is “a building which is constructed to be utilized in the area or any part of a building for dwelling, or for one type or several types of operation, with the total area on all floors from ten thousand square meters” and a high-rise building is “a building in which people may enter to reside or utilize, and which shall be at least twenty-three meters high.”<sup>27</sup>

In practice, if a construction project is a large scale construction work or a complex construction work, for instance, (a) a public building, for example, a dam, a port, an airport, a terminal, (b) the transportation work, for example, a

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<sup>27</sup> Section 4 of Building Control Act, B.E. 2535.



highway, an expressway, a tunnelling, a railroad, (c) an oil refinery or petrochemical plant, or (d) a large scale building, for example, an office building, a condominium, or a hotel. These projects may be considered as large construction projects.

(ii) Impact of construction work

If any construction project is requires a preparation and a submission of the Environmental Impact Assessment report under Enhancement and Conservation of National Environmental Quality Act, B.E. 2535, such construction project could cause a wide environmental impact to people and may be considered as a large construction project, for instance, an office building which is classified as an extra-large building or a high- rise building under Building Control Act, B.E. 2535, a petroleum development project, a petrochemical industry having chemical process project, an oil refinery project, a cement production project, a thermal power plant project, a mass transportation system by rail project, and an air transportation system project.<sup>28</sup>

(iii) Characteristic of the contractor to construction work

If any construction project requires a contractor, who has an advanced technology or expertise including international experience on construction work, for instances, an international contractor, a public company limited, or who is in the form of joint venture, or consortium, this construction project may be considered as a large construction project.

(iv) Project budget

If any construction project requires an amount of contract price, especially a project which is under a project finance program, this construction project may be considered as a large construction project.

(2) The construction contract forms studied under this thesis are (i) the FIDIC<sup>®</sup> Conditions of Contract for Construction for Building and Engineering Works designed by the Employer (“FIDIC Red Book”), and (ii) the FIDIC<sup>®</sup> Conditions of Contract for Plant and Design Build for Electrical and Mechanical Plant, and for

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<sup>28</sup> Attachment 3 of Notification of the Ministry of Natural Resources and Environment Subject: Type and Size of Project or Activity Required to Submit Environmental Impact Assessment Report; And Criteria, Procedure, Regulation and Guideline to Prepare Environmental Impact Assessment Report.

Building and Engineering Works designed by the Contractor (“FIDIC YELLOW BOOK”). Both of the construction contract forms are globally used in public and private construction business<sup>29</sup> including international construction business. The FIDIC Red Book is used for the construction of large buildings, where the designed work was prepared by the Owner, while the FIDIC Yellow Book is used for the construction of large buildings or electronic or mechanical Plants, where the designed work was composed by the Contractor.

(3) The principle of the following Third Party Guarantees: the advance payment guarantee, the performance guarantee, and the retention money guarantee, which are specified in (i) the FIDIC Red Book, and (ii) the FIDIC YELLOW BOOK.

(4) The effect on the Third Party Guarantee governed by the amendments of principle of suretyship under the CCC, as amended by the CCC Amendment No.20 and the CCC Amendment No.21.

(5) The key principles of standby letter of credit covered by the International Standby Practices (“ISP 98”) concerning the construction contract and the key principles of independent guarantee and stand-by letter of credit covered by the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit (“Convention”) concerning the construction contract. Due to the effect of the amended principle of suretyship on the Third Party Guarantees under the construction contract which may cause the question concerning the suitability of the use of the Third Party Guarantee governed by the principle of suretyship under the CCC, as amended, the use of the Third Party Guarantee covered by the international practices, as the provisions governing the Third Party Guarantee as agreed by the parties, shall be taken into consideration.

(6) The comparison among the use of the Third Party Guarantee governed by the principle of suretyship under CCC, as amended, the standby letter of credit covered by ISP 98, and the undertaking covered by the Convention will be made in order to understand the advantages and disadvantages from the use of either of them and the possibility and suitability to use the international practices of the Third Party

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<sup>29</sup> Ellos Baker, Ben Mellors, Scott Chalmers and Anthony Lavers, **FIDIC Contracts : Law and Practice**, (London: Informa, 2009), 14-15.

Guarantee in lieu of the use of the Third Party Guarantee governed by the principle of suretyship under CCC, as amended, under the construction contract.

### 1.5 Methodology of Study

The study of this thesis is a document research using the method of clarifying and analyzing the followings:

(1) The use of the advance guarantee, the performance guarantee, and the retention money guarantee, which are the common Third Party Guarantee forms used in most construction contracts, under the FIDIC Red Book and the FIDIC Yellow Book, which are both standard construction contracts used worldwide. The FIDIC® Conditions of Contract is also accepted, used and was published in Thai Language by the Engineering Institute of Thailand as the standard construction contract.<sup>30</sup>

(2) The guarantee from the third party which is governed by the principle of suretyship under the CCC, which was amended by the CCC Amendment No.20 and the CCC Amendment No.21;

(3) The key principles of standby letters of credit covered by the ISP 98 and the key principles of independent guarantees and stand-by letters of credit which are covered by the Convention.

Since the Convention is the only international law concerning both independent guarantees and stand-by letters of credit, the use of the international law is likely to be accepted by the Thai Court. Meanwhile a standby letter of credit covered by the ISP 98 is independent and documentary and, therefore, is considered as a separate agreement form the construction contract. Contrastingly, the principle of the independent guarantee under the Uniform Rules for Demand Guarantees (“URDG 758”) seems similar to the principle of Third Party Guarantee governed by the CCC. So, the parties’ agreement that the Third Party Guarantee shall be covered by it may be deemed that the parties try to avoid the use of the principle of suretyship under the CCC, as amended. In order to avoid this issue, the use of the standby letters of credit covered by the ISP 98 shall be considered.

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<sup>30</sup> EIT, **Standard Contract for Construction Work**, 1<sup>st</sup> Edition (Bangkok: EIT, 2540), Introduction.

(4) The related thesis, legal text books, legal publications, educational institution journals, and on-line information.

### **1.6 Anticipated Benefits**

(1) Understanding the use of the Third Party Guarantee under the construction contract. In this thesis, the construction contract forms, which are used to study, are the FIDIC Red Book and the FIDIC Yellow Book. Both construction contract forms are developed and used as standard construction contracts in the construction business of Thailand.<sup>31</sup> Thus, understanding the use of the Third Party Guarantee under such construction contract forms will help understanding the same of the other construction contract form used in Thailand.

(2) Understanding the Third Party Guarantee is governed by the principle of suretyship under the CCC and the effects of the amendments to the principle of suretyship under the CCC, as amended by the CCC Amendment No.20 and the CCC Amendment No.21, to the Third Party Guarantees under the construction contract.

(3) Understanding the use of the Third Party Guarantees under construction contracts governed by internal laws and practices.

(4) Possibility of the use of the Third Party Guarantees under construction contracts governed by the Convention or ISP 98 in lieu of the Third Party Guarantee governed by the amendment of principle of suretyship under the CCC, as amended by the CCC Amendment No.20 and the CCC Amendment No.21.

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<sup>31</sup> *Id.*

## **CHAPTER 2**

### **THE THIRD PARTY GUARANTEE UNDER THE CONSTRUCTION CONTRACT**

This Chapter consists of two parts. The first part will focus on the obligations and liabilities of the Contractor under the construction contract. The other will focus on the various types of the Third Party Guarantee under the construction contract and the principle thereof

#### **2.1 Construction Contract**

##### **2.1.1 Definition of Construction Contract**

A construction contract is an agreement under which the Contractor undertakes to carry out works of a building, an industrial plant or construction project for the Owner for remuneration.<sup>32</sup> However, the obligations and responsibilities of the Owner or the Contractor under the construction contract vary with types of the construction contract, which shall be described in 2.1.2.

##### **2.1.2 Types of Construction Contract**

The construction processes of the construction work consist of three major parts; (i) design, (ii) construction, and (iii) service which include a work test, a work maintenance and a work assessment. The construction work such as a building or a mechanical plant consists of many parts. Each part of the construction work consists of three foregoing processes and each construction process consists of many sub construction processes. For instance, before construction of the foundation, the design of the foundation is finished and the strength testing of such foundation is executed after the construction of the foundation. During the construction of such foundation, the following work is executed: soil investigation, steel work, concrete work, and etc.<sup>33</sup>

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<sup>32</sup> I.N. Duncan Wallace Q.C., **Hudson's Building and Engineering Contracts**, 11<sup>th</sup> Edition, Volume 1 (London: Sweet&Maxwell, 1995), 3.

<sup>33</sup> Joseph A. Huse, **Understanding and Negotiating Turnkey and EPC Contracts**, 2<sup>nd</sup> Edition (London: Sweet&Maxwell, 2002), 1.

So, in order to understand the construction process, some technical backgrounds are required. However, because construction processes of the construction work are based on the types of the construction contract, we can also understand the construction process by studying the types of construction contracts.

In order to choose the type of construction contracts to apply with the construction work, the Owner has to investigate himself on their particular institutional and technical strengths and weaknesses, including their finance. Each type of construction contracts is a vehicle of the Owner to allocate the responsibility and risk to the Contractor.

The construction contract can be classified by the following methods used in relation to the construction work: (i) Contracting Methods, (ii) Pricing Method, and (iii) Payment Method.

#### 2.1.2.1 Contracting Methods

Although the construction contract can be divided into various works, for instance, civil engineering work, electrical/mechanical engineering work, and finishing work, the two main aspects of the construction work that to considered by the Owner in order to choose the appropriate contracting method are the design function, and the co-ordination of the construction work.<sup>34</sup>

The method of contracting available to the Owner can be separated into two types: (i) design-bid-build, which separates the design work and construction work, and (ii) design-build, or turnkey, which places the entire project, including design and construction, to the Contractor.

##### (i) Design-bid-build

Under the design-bid-build method, the Owner provides the design of the construction work and co-ordination of the construction work and the Contractor provides the construction work.

The followings are the disadvantages associated with the design-bid-build: (1) the construction work tends to delay the overall completion date due to the use of distinct design and construction phase, which can be commenced only after

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<sup>34</sup> *Id.* at 1-2.

the design work is completed, (2) the design, which is provided by the Owner, does not necessarily correspond with the technical capacities of the Contractor.<sup>35</sup>

(ii) Design-build (Turnkey, EPC)

Under the design-build method, the Owner places the duty to design and construct solely on the Contractor while provides only the supervision of the construction work.

The followings are the advantages associated with the design-build: (1) as the design-build method places the responsibility for the entire construction work to the Contractor, there is no need to identify whether a defect has been caused by defective design or defective construction of the works, (2) the problem concerning the inconsistency between the design and the technical capacities of the Contractor should be reduced, resulting in a more efficient and cost effective application of the design of the construction work, and (3) the combination of the design and construction responsibilities should reduce the overall time for completion of the construction work.

However, because the Contractor under the design-build method is responsible for the entire construction work, the construction cost under this design-build method will be higher that the design-bid-build method.<sup>36</sup> .

#### 2.1.2.2 Pricing Methods

Some of the most common methods of pricing of the construction work are (i) lump-sum, (ii) cost-plus, and (iii) unit price. The Owner can choose only one pricing method or combine each of them under the construction contract.<sup>37</sup>

(i) Lump-sum method

Under the lump-sum method, the contract price shall cover the whole construction contract, irrespective of the actual cost of the Contractor. The difference between the lump-sum price of the construction contract and the actual cost of the Contractor will constitute the Contractor's profit or loss. The substantial risk that would adjust the contract price, including the risk of change in the price of

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<sup>35</sup> *Id.* at 2-3.

<sup>36</sup> *Id.* at 5-7.

<sup>37</sup> *Id.* at 9.

material and labor, shall be allocated to the Contractor under this method. In practice, if the Owner chooses to use the design-build method, the lump-sum price shall also be chosen as the pricing method.

The Contractor will usually be paid the lump-sum price in installments. The installments will be based on a schedule of payment or payable at specified stages of completion of the construction work.

The use of lump-sum price is generally easier and less expensive to administer than the other pricing method as the price is clearly specified. When the cost-plus method or the unit price method is used, the calculation of the pricing is based on the number of materials, equipment and services used or the amount of construction units required.<sup>38</sup>

(ii) Cost-plus (Cost-reimbursable) method

Under the cost-plus method, the Owner pays the Contractor for cost incurred plus a predetermined margin of profit. The margin can be fixed or fluctuating in a form of a percentage of actual cost. In the event that the cost-plus method is used, the construction contract may clearly specify that the Owner shall pay to the Contractor only for materials and services actually used by the Contractor in order to avoid any over-ordering by the Contractor and its subcontractor.

The use of cost-plus method may not incentivize the Contractor to work economically or rapidly as the greater cost makes the greater profit out of the Contract, notwithstanding the progress of construction work. In order to give incentives to the Contractor, the Owner may include an incentive mechanism to the construction contract. For instance, the Owner may specify the target cost, and to the extent that the construction cost exceeds a target cost, the Contractor shall not receive any profit and may, in addition, reduce the profit that the Contractor has already earned.

In practice, the cost-plus method is often used where it is impossible to calculate the construction cost.<sup>39</sup>

(iii) Unit price (Bill of quantities) method

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<sup>38</sup> *Id.* at 10-11.

<sup>39</sup> *Id.* at 11-12.



Under the unit price method, the price of the construction work is calculated in accordance with the amount of work done. The price is established per unit of quantity with reference to a bill of quantities or a schedule included in the construction contract which specifies the amount of materials and labor needed for particular task. This method allocates the risk from the number of units used to the Owner and allocates the risk of change in the cost or rate of each unit to the Contractor. For instance, to the extent that the foundation work of construction work consists of ten units of work at the total fixed price, (a) if such foundation work require more than ten units of work, Owner will be responsible for the addition cost, and (b) if the fixed price of such foundation work is increased due to the foreseeable cause, the Contractor will be responsible for the addition cost.

If the unit price method is used under the construction contract, the contract may provide a mechanism to adjust the unit price when the change of unit price which is beyond the parties' control or is an unforeseeable cause.<sup>40</sup>

#### 2.1.2.3 Payment Methods

In addition to consider the method of contracting and pricing, the Owner and the Contractor shall agree upon the methods of payment under the construction contract. The followings are the methods of payment generally used under the construction contract.<sup>41</sup>

##### (i) Payment after completion method

Under this method, the payment of the contract price shall be made only after the completion of the work.

This method is more common for smaller subcontractors or simple task-oriented contracts but this method is not usually used under large construction projects.<sup>42</sup>

##### (ii) Milestone payment method

Under this method, the parties shall set up a schedule of tasks for the construction work to be completed, which is called milestones. For each milestone achieved, the Owner shall pay a portion of the lump-sum price or an amount in

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<sup>40</sup> *Id.* at 12-13.

<sup>41</sup> *Id.* at 14.

<sup>42</sup> *Id.* at 14-15.

accordance with rate schedules against the completed unit or cost-plus pricing. Milestone payments can occur either upon the completion of each given milestone, or periodically, i.e. payment for all milestones completed within the period involved.

Milestone payments at specified stage of construction work may provide an incentive for rapid construction progress. However, the Contractor may try to complete the more expensive tasks at the early stage of construction work, resulting in less incentive to progress at later stages of the construction work. To this extent the Owner may use the combination of this milestone payment method and the lump-sum price; the Contract shall receive the price in proportion to the percentage of completed work, to mitigate the foregoing situation.<sup>43</sup>

(iii) Progress or scheduled payment method

Under this method, the Owner shall pay the price for work completed during given period of time, calculating the value of the completed work during such period, or simply setting a percentage of the contract price to be paid at the end of each period.<sup>44</sup>

### **2.1.3 FIDIC<sup>®</sup> Conditions of Contract**

FIDIC<sup>®</sup> Conditions of Contracts are the forms of construction contracts which are globally used in public and private construction business<sup>45</sup> and is accepted, used and was published in Thai language by the Engineering Institute of Thailand as the standard of construction contracts.<sup>46</sup> FIDIC<sup>®</sup> Conditions of Contracts have been created and developed by the International Federation of Consulting Engineers or FIDIC. For the propose of providing flexibility and suitability for a wide range of construction project types and contents, FIDIC has created and developed a number of FIDIC<sup>®</sup> Conditions of Contracts, for instance, (i) FIDIC<sup>®</sup> Conditions of Contract for Construction for Building and Engineering Works designed by the Employer (FIDIC Red Book), (ii) FIDIC<sup>®</sup> Conditions of Contract for Plant and Design Build for Electrical and Mechanical Plant, and for Building and Engineering Works designed by the Contractor (FIDIC Yellow Book), (iii) FIDIC<sup>®</sup> Conditions of

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<sup>43</sup> *Id.* at 15.

<sup>44</sup> *Id.* at 15-16.

<sup>45</sup> Ellos Baker and others, *Supra* note 29.

<sup>46</sup> EIT, *Supra* note 30.

Contract for EPC/Turnkey Project (FIDIC Silver Book), or (iv) FIDIC<sup>®</sup> Conditions of Contract for Design, Build and Operate Projects (FIDIC Gold Book). However, the two fundamental construction contract forms of FIDIC, which are widely used, are the FIDIC Red Book and FIDIC Yellow Book.

This thesis focuses on the construction for large projects, which, in general, the contractor who has the capability to provide the construction works and services at this scale is a public company limited, an international firm, or a group of contractors that may be established in the form of the joint venture or the consortium. Due to the international characteristics of the contractor, the forms of the construction contract used under such a construction project shall also be globally accepted and used. Hence, the FIDIC<sup>®</sup> Conditions of Contracts is proper to be the construction contract forms that are used for the study in this thesis. As the fundamental and widely used construction contract forms, the following FIDIC<sup>®</sup> Conditions of Contract forms are the only construction contract forms to be focused under this thesis: (i) FIDIC Red Book, and (ii) FIDIC Yellow Book.

#### 2.1.3.1 FIDIC<sup>®</sup> Conditions of Contract for Construction for Building and Engineering Works designed by the Employer (FIDIC Red Book)

The FIDIC Red Book is the construction contract form created based on the design-bid-build method, where: (i) The Owner is responsible for executing the contract administration and providing the design of the construction work to the Contractor;<sup>47</sup> and (ii) The Contractor is responsible for (a) providing the design (only to the extent specified in the construction contract), executing and completing the construction work in accordance with the terms and conditions of the construction contract and the Owner's instructions, and remedying any defects in the construction work, and (b) providing the construction work and Contractor's document, Contractor's personnel, goods, consumables and other things and services, whether a temporary or permanent nature, required in and for the design, execution, completion and remedying of defects.<sup>48</sup>

The FIDIC Red Book is based on the unit price method, where the Owner pays a price based on each unit of construction work actually constructed

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<sup>47</sup> Ellos Baker and others, *Supra* note 29, at 59, 93.

<sup>48</sup> Ellos Baker and others, *Supra* note 29, at 60.

and performed. The price of each unit is fixed within set limits, and is valued by the quantity of each work item multiplied by the appropriate rate in the bill of quantities or other schedules.<sup>49</sup>

The FIDIC Red Book allows the Owner to choose whether (i) the progress payment method, which is based on an amount or percentage of the contract price payable for each month or period of payment, or, (ii) the milestone payment method, which is based on actual progress achieved in executing the construction work.<sup>50</sup>

2.1.3.2 FIDIC<sup>®</sup> Conditions of Contract for Plant and Design Build for Electrical and Mechanical Plant, and for Building and Engineering Works designed by the Contractor (FIDIC Yellow Book)

The FIDIC Yellow Book is the construction contract form created based on the design-build method, where: (i) the Owner is responsible for executing the contract administration;<sup>51</sup> and (ii) The Contractor is responsible for (a) designing, executing and completing the construction work, and remedying any defects in the construction work, and (b) any work necessary to satisfy the Owner's requirements, the Contractor's proposal, and all work necessary for the stability, completion, or safe and proper operation of the construction work.<sup>52</sup>

The FIDIC Yellow Book is based on the lump-sum method, where the Owner pays a price based on a fixed amount which is predetermined sum for completing the fixed scope of the construction work contained in the construction contract. The sum is paid irrespective of the actual cost to the Contractor of performing such work.<sup>53</sup>

The FIDIC Yellow Book allows the Owner to choose between (i) the progress payment method, which is based on an amount or percentage of the contract price payable for each month or period of payment, and, (ii) the milestone

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<sup>49</sup> Ellos Baker and others, *Supra* note 29, at 161.

<sup>50</sup> Ellos Baker and others, *Supra* note 29, at 187-188.

<sup>51</sup> Ellos Baker and others, *Supra* note 29, at 59.

<sup>52</sup> Ellos Baker and others, *Supra* note 29, at 60.

<sup>53</sup> Ellos Baker and others, *Supra* note 29, at 163.

payment method, which is based on actual progress achieved in executing the construction work.<sup>54</sup>

## **2.2 Obligations and Liabilities of the Contractor to the Construction Contract**

### **2.2.1 Obligation of the Contractor**

In this topic, a number of obligations of the Contractor under the construction contract will be discussed. In order to simplify the obligations of the Contractor, the Contractor's obligations under the construction contract shall be separated into the following topics:

#### **2.2.1.1 Obligation to Complete<sup>55</sup>**

This obligation is a general obligation of the Contractor under the construction contract. Most of the construction contract forms, such as, FIDIC Red Book,<sup>56</sup> FIDIC Yellow Book<sup>57</sup> and ICC Model Turnkey Contract for Major Projects,<sup>58</sup> express this obligation in similar term as follows: “the Contractor shall execute and complete the construction work in accordance with the contract”. The forgoing term shows that the obligation to complete contains two parts of the obligation, first is the obligation to execute the construction work and second is the obligation to complete the construction work.

#### **2.2.1.2 Obligation upon the Design and Quality of Materials and Work**

In addition to the obligation to complete, which provides that the Contractor shall execute and complete the construction work, the Contractor will also have the following obligations:

- (1) The design obligation

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<sup>54</sup> Ellos Baker and others, *Supra* note 29, at 187-188.

<sup>55</sup> I.N. Duncan Wallace Q.C., *Supra* note 32, at 472.

<sup>56</sup> FIDIC, **FIDIC® Condition of Contract for Construction**, 1<sup>st</sup> Edition (Switzerland: FIDIC, 1999), 12.

<sup>57</sup> FIDIC, **FIDIC® Condition of Contract for Plant and Design Build**, 1<sup>st</sup> Edition (Switzerland: FIDIC, 1999), 11.

<sup>58</sup> International Chamber of Commerce [ICC], **ICC Model Turnkey Contract for Major Projects** (France: ICC SERVICE Publications Department, 2007), 24.

This obligation is not only scoped to structural calculations, the dimensions, shape and location of the construction work, but also includes the obligation to choose the suitable materials for specified function of the construction work and the obligation to choose the suitable work process for the construction work.

(2) The obligation to supply good material and qualified staffs

The Contractor shall execute the construction work with care and workmanlike staffs and use good quality materials.<sup>59</sup>

### **2.2.1.3 Obligation upon the Progress**

One of the principle obligations of the Contractor is the obligation to complete the construction work in accordance with the schedules without delay.<sup>60</sup>

Prior to the commencement of the construction work, the Contractor has a duty to submit a detailed time program or a breakdown schedule of the construction work to the Owner within specified time, such breakdown schedule of the construction work will include the detail of the order that the Contractor intends to carry out in the construction work, including the estimated timing of each stage of the construction work, which is sometimes, called milestones,<sup>61</sup> to the Owner for approval. To the extent that the Owner approves such breakdown schedule of the construction work, the Contractor shall complete each stage of the construction work in accordance with the breakdown schedule of work.

To control the construction work to be completed within milestones, the Owner usually links each milestone with portion of contract price. If the Contractor fails to achieve the work as specified in the milestone within the specified time, the Owner shall be entitled to suspend the payment of such portion of contract price until the contractor has achieved such construction work, as specified in the milestone.<sup>62</sup>

In addition to the right to suspend the payment, the delay by the Contractor shall give the right to demand for liquidated damages for delay to the

<sup>59</sup> I.N. Duncan Wallace Q.C., *Supra* note 32, at 517-519.

<sup>60</sup> Ellos Baker and others, *Supra* note 29, at 230-231.

<sup>61</sup> FIDIC, *Supra* note 57, at 28.

<sup>62</sup> I.N. Duncan Wallace Q.C., *Supra* note 32, at 563-564.

Owner, in order to force the Contractor to speed up such delayed work to be achieved as fast as possible. However, in practice, the Contractor will propose to the Owner that if the Contractor can complete the delayed work within the specified period of time, the Owner will agree to make a waiver for the liquidated damages for the delay occurred from such delayed work. In order to encourage the Contractor, the Owner sometimes accepts such offer.

#### **2.2.1.4 Obligation as to Cost**

Normally the obligation to pay the contract price is the obligation of the Owner against the portion of construction work to be done by the Contractor. However, in many cases, the Contractor shall be entitled to request the Owner to pay him some of the contract price before the commencement of the construction work; this portion of the contract price is usually called the Advance Payment. If the Owner agrees to pay the Advance Payment to the Contractor, the Contractor shall have the obligation to return the Advance Payment to the Owner by mutually agreed mean. In practice, the Contractor shall pay the Advance Payment back to the Owner by giving the right to the Owner to deduct the portion of Advance Payment from the payment of contract price proportionally. For instance, if the Contractor requests the Advance Payment which is equal to ten per cent of the contract price, any payment of the contract price made by the Owner shall be deducted by ten per cent of such payment as the returned Advance Payment. However, in order to protect the Owner from the event that the Contractor does not perform any construction work or abandons the construction work at any time during the construction period after the Contractor has received the full amount of Advance Payment, the Contractor shall be requested to provide the Advance Payment Guarantee against the Advance Payment to the Owner, as security of such Advance Payment.<sup>63</sup>

#### **2.2.2 Liabilities of Contractor**

To the extent that the Contractor breaches any of his obligations under the construction contract, the Contractor shall be liable for any and all damages occurred to the Owner. After the breach of the Contractor's obligations, the dispute

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<sup>63</sup> I.N. Duncan Wallace Q.C., *Supra* note 32, at 564-565.

concerning the calculation of the actual cost of damages often occurred. Thus, in order to mitigate this dispute of the parties, which may affect the performance of the construction work, including the schedule of work, the parties may agree upon the cost of damage occurred from either breach of the Contractor's obligations in advance. The advance agreed cost concerning the said damages is called as "liquidated damages"<sup>64</sup>. Even though, the liquidated damages has been agreed by the

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<sup>64</sup> Although the use of liquidated damages clauses is widespread in the modern construction industry, the position in law differs between different jurisdictions. For example, in some civil law countries, a judge could intervene to increase or decrease the amount of liquidated damages in a contract. In France, the law of 9 July 1975, No 75-598 as reformed by the law of 11 October 1985, No 85-1097, provides that 'the judge may even on his own motion moderate or increase the agreed penalty, if it is obviously excessive or ridiculously low. Any stipulation to the contrary shall be deemed unwritten'. In the common law jurisdictions, by contrast, it will not be open to a judge to change the amount of a liquidated damages provision; it will either be enforced or it will not. English Law distinguishes between penalty clauses and liquidated damages clauses in much more fundamental way. It is the difference between the unenforceable and the enforceable. In principle, a clause which imposes a penalty has always been unenforceable. The classic case, almost invariably cited whenever the liquidated damages/penalty issue was raised, was *Dunlop Pneumatic Tyre Co Ltd v New Garage Motors Co Ltd*. The manufacturer, Dunlop, supplied motor types and its contracts prohibited purchasers such as New Garage from a number of interferences with Dunlop's intellectual property (including trademarks) and also from selling the products at below Dunlop's current list price. The purchaser would be liable to have to pay £5 for each sale in breach of these contractual prohibitions. Lord Dunedin, giving the principal speech, provided the key distinctions between penalties and liquidated damages: 'the essence of a penalty is a payment of money stipulated as *in terrorem* of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of loss'. In other words, a contractual provision would be a penalty if its purpose is to put a party in fear of the consequences of breach of its primary obligation, whereas a liquidated damages provision is intended to compensate the innocent party for the loss suffered as a result of the breach. see David Thomas QC, *Penalties and liquidated damages in English law: a centenary review by the Supreme Court*, 11 *Construction Law International*, 37-38 (March 1, 2016); Thai Law does not distinguish between penalty clauses and liquidated damages clauses, so, there are no significant differences between penalty and liquidated damages. The Supreme Court Judgment number 1078/2496, the judge has handed down that an agreement called penalty is liquidated damages. However, from the remark of the Supreme Court Judgment number 2654/2519 which was given by Professor Chitti Thingsabadh, in some case, liquidated damages may differ from penalty, there are not always similar, liquidated damages may be included in penalty but the meaning of penalty is greater than liquidated damages. Hence, even the liquidated damages was specified in the contract, if its characteristic is penalty, it shall



parties, many construction contract forms shall not release the Contractor from any other liabilities occurred from such breach and also address the right to the Owner to claim such other liabilities from the Contractor.

Types of the liquidated damages under the construction contract, which the parties to the construction contract often agreed upon, are (i) liquidated damages for performance and (ii) liquidated damages for delay.

The liquidated damages for performance shall be claimed when the Contractor breaches his obligation concerning the performance under the construction contract, for instances, the obligation to execute and complete the construction work, the design obligation, the obligation to supply good material and qualified staffs and any other related obligation. For instance, if the performances of the completed construction work do not meet the guarantee figures specified in the construction contract, the Owner shall be entitled to demand for the liquidated damages for performance, which can be calculated as agreed by both parties.

In the event that the Contractor fails to complete any portion of construction work within any specific time, set as milestone, for reasons attributable to the Contractor, the Owner shall be entitled to claim from the Contractor the liquidated damages for delay from the date of prescribed time, to the date which such delay work is completed. A common method to calculate and impose liquidated damages for delay is the usage of daily rate. However, the Owner and the Contractor may agree upon the maximum amount of the liquidated damages for delay.

After the Contractor is in breach of any of his obligation as specified in the terms of the construction contract, some as described in the Topic 2.2.1, and the Owner is entitled to demand for the damages whether as actual damages or liquidated damages, the Owner may exercise his right to claim either directly from the

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be considered as penalty and may be reduced by the Court in case the amount thereof is disproportionately high. Penalty is specified for the following proposes: (i) as *in terrorem*, if the debtor does not perform his obligation, the debtor shall pay a sum of money which is much higher than the actual damages, such penalty may be reduced by the Court; (ii) as liquidated damages, if a sum of money is approximately equal to the expected actual damages, in order to avoid the proving of actual damages which is hard to find; (iii) as limitation of liability, in order to prohibit the creditor from claiming the penalty in exceed of the specified amount. *see* Chaiyos Hemarajata, Law of Contract, 356-357 (3<sup>rd</sup> ed. 2004).

Contractor or deduct such damages from the payment of the contract price due to the Contractor in accordance with the construction contract.

However, if the Owner demands for the payment of the damages from the Contractor by either of forgoing means, such demand will affect the cash flow of the Contractor and the Contractor sometimes may not have enough cash flow to pay such damages to the Owner or, even, to execute the existing construction work then. Thus, in order to mitigate such effect, an additional security form the Contractor may be requested by the Owner. One of the widely used additional securities in the construction business is the Third Party Guarantee.

### **2.3 Third Party Guarantees under the Construction Contract**

The Third Party Guarantees were widely used as an additional security for various purposes under the construction contract. Each of construction contract forms used in the construction business, for instance, the FIDIC Red Book, the FIDIC Yellow Book, and the ICC Model Turnkey Contract for Major Projects, has provisions related to the use of the Third Party Guarantee. The followings are the types of Third Party Guarantee which are usually used in the construction business and in the foregoing forms of the construction contracts: (i) a Performance Guarantee, (ii) an Advance Payment Guarantee, (iii) a Retention Money Guarantee (where actual retention money is not used), and (iv) a Parent Company Guarantee.<sup>65</sup>

In this topic the foregoing types of the Third Party Guarantees under the construction contract and their principle will be discussed.

#### **2.3.1 Types of the Third Party Guarantee under the Construction Contract**

##### **2.3.1.1 Performance Guarantee**

Most of the construction contract forms, for instances, FIDIC Red Book,<sup>66</sup> FIDIC Yellow<sup>67</sup> and ICC Model Turnkey Contract for Major Projects<sup>68</sup>

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<sup>65</sup> Joseph A. Huse, *Supra* note 33, at 64.

<sup>66</sup> FIDIC, *Supra* note 56, at 12-13.

<sup>67</sup> FIDIC, *Supra* note 57, at 12.

<sup>68</sup> International Chamber of Commerce [ICC], *Supra* note 58, at 21, 109-110.

provide the Owner with the right to require the Contractor to provide a Performance Guarantee to the Owner.

The purpose of a Performance Guarantee is to secure that the Contractor shall duly and timely perform his obligations under the construction contract.

The Performance Guarantee shall be usually issued by a commercial bank or a financial institution, which has their place of business in the country, and in the form approved by the Owner.<sup>69</sup>

The amount of the Performance Guarantee varies from project to project, anywhere from five per cent to fifty per cent of the overall contract price depending on the type of the project and financial standing of the Contractor. However, ten per cent of the contract price is average amount for a Performance Guarantee.<sup>70</sup>

The Performance Guarantee comes into force on the date of issuance and shall remain valid and enforceable until the Contractor has executed and completed the construction works without any defects. Hence, in practice, the period of the Performance Guarantee will cover through the Construction Stage and the Post Construction Stage until the Warranty Period expires.

### **2.3.1.2 Advance Payment Guarantee**

At the initial stage of a construction project, the Contractor is not entitled to any payment from the Owner; they, however, already have the duties concerning the construction work, such as, the design work, the mobilization and the procurement of materials. Thus, under the construction contract form, either FIDIC or ICC, the Contractor may have the right to require an advance payment from the Owner to assist the Contractor with cash flow at this initial stage.

Even though the Advance Payment shall be paid back to the Owner by proportional deduction from their payment, the Owner still has the risk from non-repayment of the Advance Payment. The non-repayment may occur from the early termination of the construction contract, the Contractor's cash-flow, the Contractor's failure to perform his obligations or complete the construction work, or

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<sup>69</sup> Ellos Baker and others, *Supra* note 29, at 389.

<sup>70</sup> Joseph A. Huse, *Supra* note 33, at 64.

whatsoever reasons that will abolish the Contractor's right to have the payment of the contract price. In order to protect the Owner from the risk of non-repayment of the Advance Payment, the Owner shall be entitled to require the Advance Payment Guarantee from the Contractor.

The Advance Payment Guarantee is usually issued by a commercial bank, which has their place of business in the country and in the form approved by the Owner.

The amount of the Advance Payment Guarantee shall be equal to or cover the Advance Payment that the Contractor received from the Owner.

The Advance Payment Guarantee is effective upon the Contractor's receipt of the Advance Payment and shall remain valid until the Advance Payment has been fully repaid to the Owner. Hence, in practice, the period of the Advance Payment Guarantee may cover through the Construction Stage and the Post Construction Stage when the last payment of the contract price is due after the expiration of Warranty Period.

### **2.3.1.3 Retention Money Guarantee**

Even though, the Owner is entitled to require the Contractor to provide a Performance Guarantee, as an additional security, the Owner shall also be entitled to retain a fixed percentage from any progress payment made as per the execution of the construction work by the Contractor. The money retained is called "Retention Money". The purposes of Retention Money are to provide another additional security, in the form of a fund, against the Contractor's failure to complete any construction work in accordance with the terms of the construction contract and to remedy any defects or damages and problems in respect of any other liabilities of the Contractor to the Owner. The practice of holding a percentage of the sums already payable as security for completion of the construction works is widespread, not only in common law countries, but in Continental Europe as well. A recent paper at the European Society of Construction Law (ESCL) conference demonstrated that the concept is familiar in all the countries surveyed in the ESCL research project (Austria,

England and Wales, France, Germany, Greece, Netherlands, Sweden and Switzerland).<sup>71</sup>

Although the Contractor agrees with the Owner about the Retention Money, many Contractors propose to provide the Retention Money Guarantee to the Owner instead of the Retention Money itself, in order to protect the Contractor's cash flow. One of the difference between the Performance Guarantee and the Retention Money Guarantee is the issued amount thereof, the issued amount of the Performance Guarantee is equal to the agreed percentage of the contract price, but the issued amount of the Retention Money Guarantee is to zero if the Owner requires the Contractor to provide before making the first progress payment, or to the agreed percentage of the progress payment. The amount of the Retention Money Guarantee is increased proportionally in relation to the contract price paid by the Owner.

The Retention Money Guarantee shall be issued by a commercial bank or a financial institution, whose place of business is in the country and in the form approved by the Owner.

The amount of the Retention Money Guarantee depends on the agreement between the Contractor and the Owner. However, the ESCL proposes an amount of five per cent of each progress payment in France, Greece and Netherlands and an amount of five to ten per cent of the progress payment in Germany and Switzerland.<sup>72</sup>

The Retention Money Guarantee comes into force upon the agreed point of time or the receipt of the first progress payment and shall remain valid and enforceable until the Contractor has executed and completed the construction works and remedied any defects. Hence, in practice, the period of the Retention Money Guarantee will cover through the Construction Stage and the Post Construction Stage until the Warranty Period expires.

#### **2.3.1.4 Parent Company Guarantee or Corporate Guarantee**

To the extent that the Contractor is a subsidiary or affiliate of another larger company, a group of companies, a joint venture or a consortium, the Owner may require the Contractor to provide a Parent Company Guarantee or

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<sup>71</sup> Ellos Baker and others, *Supra* note 29, at 393.

<sup>72</sup> Ellos Baker and others, *Supra* note 29, at 393.

Corporate Guarantee. In the Parent Company Guarantee or Corporate Guarantee, the Contractor's parent company, including the Contractor's shareholder or ultimate holding company, guarantees the due performance of all of the Contractor's obligations under the construction contract and agrees to indemnify the Owner in the case of the Contractor's non-performance. However, as the requirement of the Parent Company Guarantee or Corporate Guarantee is a special requirement, it should be expressly specified in the invitation to bid.<sup>73</sup>

The Parent Company Guarantee or the Corporate Guarantee shall be issued by a parent company or a corporate company and in the form approved by the Owner.

The amount of the Parent Company Guarantee or Corporate Guarantee depends on the agreement between the Contractor and the Owner.

The Parent Company Guarantee or the Corporate Guarantee comes into force upon the agreed timeframe and shall remain valid and enforceable until the Contractor has executed and completed the construction works and remedied any defects. Hence, in practice, the period of the Parent Company Guarantee or Corporate Guarantee will cover through the Construction Stage and the Post Construction Stage until the Warranty Period is expires.

### **2.3.2 Principles of Guarantee under the Construction Contract**

There are various forms of the Third Party Guarantees under the construction contract, each form is used for specified propose. However, the principle of each form is not different. In order to study and summarize the principles of the various forms of the Third Party Guarantee, this study chooses the form of letter of guarantee (Performance Security), the form of letter of guarantee (Advance Payment) and the form of letter of guarantee (Retention Money) as attached to the Bid Documents for Civil Works, which are issued by the Office of the Prime Minister<sup>74</sup> which are widely used and accepted in construction business in Thailand and the form of Parent Company Guarantee issued by FIDIC.<sup>75</sup> After consideration of the foregoing

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<sup>73</sup> Ellos Baker and others, *Supra* note 29, at 393.

<sup>74</sup> The Office of Prime Minister, *Supra* note 4, at 4-47 – 4-51.

<sup>75</sup> FIDIC, *Supra* note 56, at 23.

forms of the Third Party Guarantee, the followings are the summary of the principles behind those forms of the Third Party Guarantee under the construction contract.

### **2.3.2.1 Parties to the Third Party Guarantee**

The parties to the Third Party Guarantee shall consist of a guarantor, a principal and a beneficiary. The guarantor is the person who agrees to guarantee to pay to the Owner, as a beneficiary, if the Contractor, as a principal, fails to perform his obligation and to act in accordance with the construction contract.<sup>76</sup> Apart from the Parent Company Guarantee, in which the guarantor is the parent company, the shareholder of the Contractor or the corporate company related to the Contractor,<sup>77</sup> most of the guarantees are issued by a commercial bank or a financial institution approved by the Owner.

### **2.3.2.2 The Statue of Guarantor**

The form of letter of guarantee (Performance Security)<sup>78</sup> and the form of Parent Company Guarantee<sup>79</sup> expressly and clearly specify that the guarantor under the both forms guarantees to the Owner as a primary obligator. However, the guarantor under the Retention Money Guarantee and Advance Payment Guarantee does not agree in the same way, such guarantor merely agrees to waive some of his right as a surety under the CCC, since to the form of letter of guarantee (Retention Money)<sup>80</sup> specifies that “the guarantor agrees to pay to the owner immediately without delay ... and without it being necessary to prove to the guarantor the defects or shortcomings of the contractor” and the form of letter of guarantee (Advance Payment)<sup>81</sup> addresses that “the guarantor shall pay to the owner without the necessity of previous request to the contractor for repayment of the same without whatsoever right of objection on our part”.

### **2.3.2.3 Payment Condition**

The guarantor to all Third Party Guarantee forms agrees unconditionally to guarantee to pay to the Owner on their first demand or after the

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<sup>76</sup> The Office of Prime Minister, *Supra* note 4.

<sup>77</sup> FIDIC, *Supra* note 56, at 23.

<sup>78</sup> The Office of Prime Minister, *Supra* note 4, at 4-47.

<sup>79</sup> FIDIC, *Supra* note 56, at 23.

<sup>80</sup> The Office of Prime Minister, *Supra* note 4, at 4-51.

<sup>81</sup> The Office of Prime Minister, *Supra* note 4, at 4-49.

receipt of a written request from the Owner. Moreover, under the form of letter of guarantee (Retention Money),<sup>82</sup> “the guarantor agrees to pay to the Owner immediately without delay and without necessity of previous notice or of judicial or administrative procedures and without it being necessary to prove to the guarantor the defects or shortcomings of the contractor”. All Third Party Guarantee forms with these payment conditions can be called on demand guarantees.<sup>83</sup>

#### **2.3.2.4 Extension of Time**

Under the all forms of the Third Party Guarantee, the guarantor agrees to give the advance consent to grant a time extension of the guarantee to the Owner, as beneficiary. The all forms of letter of guarantee issued by the Office of the Prime Minister<sup>84</sup> are specified that “If, at any time in the course of the execution of the construction contract, the Owner grants a time extension, or allows the Contractor to deviate from any conditions of the construction contract without our (bank) knowledge, it shall be deemed that such grants shall have been made with our consent.” while the form of the Parent Guarantee issued by FIDIC<sup>85</sup> specifies that “Our obligations and liabilities under this guarantee shall not be discharged by any allowance of time or other indulgence whatsoever by the owner to the contract, or by any variation or suspension of the Construction works to be executed under the construction contract, or by any amendments to the construction contract or to the constitution of the Contractor or the Owner, or by any other matters, whether with or without our knowledge or consent”.

Hence, almost all guarantors under the construction contract agree to give the advance consent of the time extension under the Third Party Guarantee.

#### **2.3.2.5 Withdrawal of the Third Party Guarantee**

The all forms of letter of guarantee issued by the Office of the Prime Minister<sup>86</sup> have the clause which specifies that “We (bank) shall in no event withdraw this Letter of Guarantee for any reason so far as the Contractor is still liable

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<sup>82</sup> The Office of Prime Minister, *Supra* note 4, at 4-51.

<sup>83</sup> Ellos Baker and others, *Supra* note 29, at 380.

<sup>84</sup> The Office of Prime Minister, *Supra* note 4, at 4-47 – 4-51.

<sup>85</sup> FIDIC, *Supra* note 56, at 23.

<sup>86</sup> The Office of Prime Minister, *Supra* note 4, at 4-47 – 4-51.



under the construction contract”. Moreover, under the terms of the forms of letter of guarantee (Performance Security)<sup>87</sup> and the Parent Guarantee issued by FIDIC,<sup>88</sup> the guarantor agrees to irrevocably guarantee to the Owner.

Thus, most of the guarantors under the construction contract agree not to withdraw the Third Party Guarantee if the Contractor is still liable to the Owner and some of guarantor also agrees to irrevocably guarantee to the Owner.

### **2.3.2.6 Expiration of the Third Party Guarantee**

Under the form of letter of guarantee (Performance Security),<sup>89</sup> the guarantor agrees that “This Letter of Guarantee shall be valid and in full force and effect from the date of execution of the construction contract until all obligations on the part of the Contractor has been fulfilled”.

Under the form of the Parent Guarantee issued by FIDIC,<sup>90</sup> the guarantor agrees that “This guarantee shall continue in full force and effect until all the Contractor’s obligations and liabilities under the construction contract have been discharged, when this guarantee shall expire and shall be returned to us (the parent company), and our liability hereunder shall be discharged absolutely”.

Under the form of letter of guarantee (Advance Payment)<sup>91</sup> and the form of letter of guarantee (Retention Money),<sup>92</sup> there are no specific terms about the expiration of the Third Party Guarantee. However, we may imply that both forms will expire when the Contractor is not liable under the construction contract from the following term “We (bank) shall in no event withdraw this Letter of Guarantee for any reason so far as the contractor is still liable under the construction contract”.

So, all form of the Third Party Guarantee shall expire when all the Contractor’s obligations and liabilities under the construction contract have been discharged and there is no specific expiration date of the Third Party Guarantee.

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<sup>87</sup> The Office of Prime Minister, *Supra* note 4, at 4-47.

<sup>88</sup> FIDIC, *Supra* note 56, at 23.

<sup>89</sup> The Office of Prime Minister, *Supra* note 4, at 4-47.

<sup>90</sup> FIDIC, *Supra* note 56, at 23.

<sup>91</sup> The Office of Prime Minister, *Supra* note 4, at 4-49 – 4-50.

<sup>92</sup> The Office of Prime Minister, *Supra* note 4, at 4-51.

## CHAPTER 3

### THE INTERNATIONAL PRACTICES OF THE THIRD PARTY GUARANTEE

The international law and practice concerning the guarantee from the third party which are decided to be studied under this research are (i) the standby letter of credit covered by International Standby Practices (“ISP 98”) due to the widespread and accepted use as an independent undertaking and, today, the standby letter of credit is a permanent and important fixture in international banking and commerce<sup>93</sup> and (ii) the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit (“Convention”) due to the Convention is the only international law covering the both of the independent guarantee and the stand-by letter of credit. This Chapter will consist of three parts. The first and second parts will focus upon the significant principles of the standby letters of credit covered by ISP 98 and the Undertaking covered by the Convention. The other will be the comparison of the Third Party Guarantee under the CCC, as amended, the ISP 98, and the Convention and the summarization of the comparison result.

#### **3.1 The Standby Letters of Credit covered by the International Standby Practices (“ISP 98”)**

##### **3.1.1 Purpose of the Standby Letters of Credit covered by the ISP 98**

The standby letters of credit are issued to support payment, when due or after default, of the obligations based on money loaned or advanced, or upon the occurrence or non-occurrence of another contingency.<sup>94</sup> The standby letters of credit are commonly classified based on their function in the underlying transaction or other factors not necessarily related to the terms and conditions of the standby letter of credit itself, for instance, A “Performance Standby” which is used to support an

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<sup>93</sup> Byrne, James E., “*New rules for standby letters of credit: the International Standby Practices/ISP98*” **Business credit** 100, 5 (May 1998): 32.

<sup>94</sup> Preface paragraph 3 of the ISP 98.

obligation to perform other than to pay money including the purpose of covering losses arising from a default of the applicant, referred to in the construction contract as the Contractor, in completion of the construction contract, An “Advance Payment Standby” which is used to support an obligation to account for an advance payment made by the beneficiary, referred to in the construction contract as the Owner, to the Contractor, and a “Bid Bond/Tender Bond Standby” which is used to support an obligation of the applicant, as the Contractor, to execute a contract if the applicant is awarded a bid.<sup>95</sup>

The ISP 98 reflects generally accepted practice, custom, and usage of standby letters of credit by way of simplifying, standardizing, and streamlining the drafting of standby letters of credit, and providing clear and widely accepted answers to common problems.<sup>96</sup>

### **3.1.2 Significant principles of Standby Letters of Credit covered by the ISP 98**

The significant principles of the standby letters of credit covered by ISP 98 concerning the construction contract can be summarized as follows:

#### (1) Scope and application of the ISP 98 to standby letters of credit

The ISP 98 is intended to be applied to the standby letters of credit, including performance, financial and direct pay standby letters of credit, for either domestic or international use.<sup>97</sup>

#### (2) Nature of standby letters of credit covered by the ISP 98

Standby letters of credit are an irrevocable, independent, documentary, and binding undertaking when issued, whether or not it has stated the foregoing nature in a standby letters of credit.<sup>98</sup>

As a standby letter of credit is irrevocable, an issuer’s obligations thereunder cannot be amended or cancelled solely by the issuer, except provided

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<sup>95</sup> Preface paragraph 4 of the ISP 98.

<sup>96</sup> Preface paragraph 1 and 9 of the ISP 98.

<sup>97</sup> Rule 1.01 (a) and (c) of the ISP 98.

<sup>98</sup> Rule 1.06 (a) of the ISP 98.

therein such letter or as consented by the person against whom the amendment or cancellation is asserted.<sup>99</sup>

As a standby letter of credit is independent, the enforceability of an issuer's obligations thereunder does not depend on the followings: (i) the issuer's right or ability to obtain reimbursement from the Contractor; (ii) the Owner's right to obtain payment from the Contractor; (iii) any reference therein to reimbursement agreement, underlying transaction, or the construction contract; or (iv) the issuer's knowledge of performance or breach of any reimbursement agreement, underlying transaction,<sup>100</sup> or the construction contract.

As a standby letter of credit is a documentary, issuer's obligations depend only on the presentation of such documents and the examination of required documents on their face.<sup>101</sup>

Additionally, as a standby letter of credit is binding when it has been issued, the standby letter of credit will be enforceable against an issuer, whether the Contractor has authorized its issuance, the issuer has received a fee, or the Owner has received or relied on such standby letter of credit.<sup>102</sup>

(3) Duty of the issuer to the standby letter of credit covered by the ISP 98

(3.1) Duty to honor: When the document is presented to an issuer, which appears on its face that the terms and conditions in relation to time, place, location within the place, person or medium that the presentation must be made, shall be followed, an issuer will honor such letter by paying the amount demanded at sight and in a timely manner, unless otherwise specified in such standby letter of credit.<sup>103</sup>

(3.2) Duty to examine: The receipt of a document, which required by and presented under a standby letter of credit, constitutes a presentation where a compliance of terms and conditions is required, even not all of the required

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<sup>99</sup> Rule 1.06 (b) of the ISP 98.

<sup>100</sup> Rule 1.06 (c) of the ISP 98.

<sup>101</sup> Rule 1.06 (d) of the ISP 98.

<sup>102</sup> Rule 1.06 (e) of the ISP 98.

<sup>103</sup> Rule 2.01 (a), (b) and (c) and Rule 3.01 of the ISP 98.

documents have been presented.<sup>104</sup> On the contrary, there will be no duty to examine and such duty shall be disregarded for purposes of determining the compliance of the presentation if the presentation of documents is not required under the terms and conditions of the standby letter of credit.<sup>105</sup>

Additionally, examination is a determination that whether the face of the presented document comply with the terms and conditions stated in the standby letter of credit.<sup>106</sup> Furthermore, an issuer is required to examine documents for inconsistency only to the extent as provided in the standby letter of credit.<sup>107</sup>

(4) Expiry date of standby letters of credit covered by the ISP 98

A standby letter of credit shall contain an expiry date or permit an issuer to terminate the standby letter of credit upon reasonable prior notice period payment.<sup>108</sup> To the extent that no time of expiry day is stated for expiration, the expiration shall occur at the close of business at the place of presentation.<sup>109</sup>

A presentation is timely when such presentation made at any time after issuance and before expiry on the expiration date of such standby letter of credit.<sup>110</sup> A presentation made after the close of business at the place of presentation is deemed to be made on the next business day.<sup>111</sup> If the last day for presentation that stated in a standby letter of credit (whether stated to be the expiration date or the date by which documents must be received) is not a business day of the issuer or nominated person where presentation is to be made to, the presentation made there on the following business day shall be deemed timely.<sup>112</sup>

(5) Exception to the payment obligation

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<sup>104</sup> Rule 3.02 of the ISP 98.

<sup>105</sup> Rule 4.02 of the ISP 98.

<sup>106</sup> Rule 4.01(b) of the ISP 98.

<sup>107</sup> Rule 4.03 of the ISP 98.

<sup>108</sup> Rule 9.01 (a) and (b) of the ISP 98.

<sup>109</sup> Rule 9.04 of the ISP 98.

<sup>110</sup> Rule 3.05 (a) of the ISP 98.

<sup>111</sup> Rule 3.05 (b) of the ISP 98.

<sup>112</sup> Rule 3.13 (a) of the ISP 98.

The ISP 98 does not define or provide for defenses to honor based on fraud, abuse, or any similar matter. These matters will be covered by the applicable law.<sup>113</sup>

(6) The application of standby letters of credit covered by the ISP 98 under the Thai Law

The rules of the ISP 98 will apply to a standby letter of credit if it is stated in such standby letter of credit that it is subject to the ISP98.

As the ISP 98 is the only international rule or practice, the question concerning the application of the ISP 98 under the Thai Law shall be taken into consideration.

As stated in Article 1 and Article 4 of the Uniform Customs and Practice for Documentary Credits, 2007 Revision, ICC Publication No. 600 (“UCP 600”), that “The UCP 600 are rules that apply to any documentary credit (“credit”), including, to the extent that it is applicable, any standby letter of credit, when such credit expressly indicates that it is subject to the rules. They are binding on all parties thereto unless expressly modified or excluded by the credit”<sup>114</sup> and “a credit by its nature is a separate transaction from the sale and other contract on which it may be based. Banks are in no way concerned with or bounded by such contract, even there is any reference whatsoever specified in the credit. Consequently, the undertaking of a bank to honor, negotiate or fulfil any other obligation under the credit is not subject to claims or defenses by the application resulting from its relationships with the issuing bank or the beneficiary”,<sup>115</sup> together with the Supreme Court Judgement No. 12709/2555, where the Supreme Court of Thailand rules that “Article 3 and Article 4 of UCP 500 provided that the feature of the letter of credit is a separate transaction from the sale contract and other contract which create the obligation to pay under the credit. The banks of the letter of credit are in no way concerned with or bounded by such contract; however, such bank shall perform its duties as specified in the letter of credit”. The foregoing information supports that the Supreme Court of Thailand accept the independent feature of a letter of credit under the UCP 600.

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<sup>113</sup> Rule 1.05 (c) of the ISP 98.

<sup>114</sup> Article 1 of the UCP 600.

<sup>115</sup> Article 4 of the UCP 600.

As the standby letter of credit covered by the ISP 98 is independent, Rule 1.06 (c), analogy with the Supreme Court Judgment No. 12709/2555, it seems that the Supreme Court may accept the independent feature of the standby letter of credit, as described in Topic 3.1.2 (2), of the standby letter of credit covered by the ISP 98.

Furthermore, pursuant to the Supreme Court Judgment No. 3974/2532 a letter of guarantee issued by the defendant no.3 to the plaintiff, which specified that if the defendant no.1 has acted in breach of the contract, the defendant no.3 shall promptly pay the plaintiff for the defendant no.1, is considered valid and enforceable and defendant no.3 will not be considered as the surety under the suretyship. As from this judgment, it seems that the Supreme Court of Thailand considers that the letter of guarantee as an independent document which is valid and enforceable under Thai Law.

Hence, as mentioned above, it may be considered that the standby letter of credit covered by the ISP 98, with an independent feature, is valid and enforceable under Thai Law.

## **3.2 The Independent Guarantees or Stand-by Letters of Credit covered by the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit (“Convention”)**

### **3.2.1 Purpose of the Convention**

The Convention is drafted to facilitate the use of undertaking, for both independent guarantees and stand-by letter of credit, by way of summary and creation of the common rules which is used for the undertaking.<sup>116</sup>

### **3.2.2 Significant Principles of Undertaking covered by the Convention**

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<sup>116</sup> UNCITRAL, Explanatory note by the UNCITRAL secretariat on the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit, para.2, pp.16-17, from <http://www.uncitral.org/pdf/english/texts/payments/guarantees/guarantees.pdf> (accessed June 1, 2015).

The significant principles of the undertaking covered by the Convention concerning the construction contract can be summarized as follows:

(1) Scope and application of Convention to the Undertaking

The Convention applies only to the undertaking and only to the extent that (1) the place of business of the guarantor/issuer, who issues the undertaking respectively, is in a contracting state, or (2) the rules of private international law lead to the application of the law of a contracting state.<sup>117</sup>

Additionally, the Convention also applies to an international letter of credit, which is not falling under Article 2 of this Convention and such international letter of credit expressly specifies that it is subject to this Convention.<sup>118</sup>

(2) Undertaking under the Convention

Under this Convention, an independent guarantees and stand-by letter of credit shall be referred to as “Undertaking”. The Undertaking under this Convention is an undertaking which is issued by a bank, or other institution, or person (referred to as “guarantor” for an independent guarantee or “issuer” for a stand-by letter of credit) to pay to the beneficiary (referred to in the construction contract as “Owner”) a certain amount upon simple demand or upon demand accompanied by other documents, in accordance with the terms and conditions of the undertaking, indicating that payment is due because of a default in the performance of an obligation, or because of another contingency, of money borrowed or advanced, or on account of any mature indebtedness undertaken by the principal/applicant (referred to the construction contract as “Contractor”) or another person.<sup>119</sup>

(3) Nature of the Undertaking covered by the Convention

The nature of the Undertaking covered by the Convention can be summarized as follows:

a. The Undertaking is independent. Thus, the obligations of the guarantor or issuer of the Undertaking to the Owner is neither (i) dependent upon the existence or validity of any underlying transaction, nor (ii) subject to any other terms and conditions that are not specified in the Undertaking, or any future, uncertain act or

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<sup>117</sup> Article 1 (1)(a) and (1)(b) of the Convention.

<sup>118</sup> Article 1 (2) of the Convention.

<sup>119</sup> Article 2 (1) of the Convention.



event except presentation of documents or other act or event within a sphere of operations of a guarantor or issuer.<sup>120</sup>

b. As the Convention applies to the international Undertaking, so, the Undertaking shall be international. The Undertaking is international if places of business, as specified therein, of any two of guarantor/issuer, beneficiary, principal/applicant, instructing party, or confirmer are in different States.<sup>121</sup>

c. Except as otherwise specified in the Undertaking, the Undertaking is irrevocable when issued,<sup>122</sup> unless the Undertaking is expressly specified that it is revocable, then the Undertaking shall be revocable.

d. When a demand for payment is made, it shall be made in a form referred to this Convention and in accordance with the terms and conditions of the Undertaking, and any certification or other document required by the Undertaking shall be presented to the guarantor or issuer, Hence, the undertaking covered by the Convention is documentary.<sup>123</sup>

(4) Duty of Guarantor or Issuer of the Undertaking covered by the Convention

Subject to the exception to payment obligation, as expressly specified in the Convention, to the extent that a demand for payment has been made correctly, in accordance with the terms and conditions of the Undertaking, and has been made to the guarantor or issuer, the guarantor or issuer shall pay such demanded amount. After an examination of the demand and any accompanying documents, if the guarantor or issuer decides to pay the demanded amount to the Owner, such payment shall be made promptly, unless otherwise stipulated in the Undertaking.<sup>124</sup>

In order to examine the demand and accompanying document, the guarantor or issuer shall act in good faith and with reasonable care regard to generally accepted standards of international practice of the Undertaking. In addition, the guarantor or issuer shall finish the examination and decide, whether or not pay the demanded amount, within reasonable time, but shall not more than seven business

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<sup>120</sup> Article 3 (a) and (b) of the Convention.

<sup>121</sup> Article 4 (1) of the Convention.

<sup>122</sup> Article 7 (4) of the Convention.

<sup>123</sup> Article 15 (1) and (2) of the Convention.

<sup>124</sup> Article 17 (1) of the Convention.

days following the day of receipt of the demand, unless otherwise stipulated in the Undertaking or elsewhere agreed between the guarantor/ issuer and the Owner.<sup>125</sup>

(5) Cessation of right to the demand payment

The right of the Owner to demand payment shall be ceased when (i) the guarantor or issuer has received a statement of release from its liability by the Owner, (ii) the guarantor/issuer and the Owner have agreed to terminate the Undertaking, (iii) the amount available under the Undertaking has been paid in full, unless otherwise stipulated in the Undertaking, or (iv) the Undertaking is expired.<sup>126</sup>

The Undertaking shall be expired (i) at the expiry date, which may be a specified calendar date or the last day of a fixed period of time, and (ii) when six years have elapsed from the date of issuance of the Undertaking, if the Undertaking does not state an expiry date.<sup>127</sup>

(6) Exception to payment obligation

To the extent it is manifest and clear that (i) any presented document is not real or has been falsified, (ii) no payment is due on the basis asserted in the demand and accompanying documents, or (iii) judging by the type and purpose of the Undertaking, the demand has an impossible basis, the guarantor or issuer, which acts in good faith, has a right to withhold demanded payment.<sup>128</sup> In addition, in the foregoing events, the principal or applicant (referred to in the construction contract as “Contractor”) shall have the right to request the relevant court the provisional court measures.<sup>129</sup>

To the extent that the Contractor exercises its right to request the provisional court measures, and the court has strong, manifest or clear evidence, the court may (i) issue a provisional order to the effect that the Owner does not receive payment, including an order that the guarantor or issuer hold the demanded amount, or (ii) issue a provisional order to the effect that the proceeds of the Undertaking paid

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<sup>125</sup> Article 14 (1) and Article 16 (1) and (2) of the Convention.

<sup>126</sup> Article 11 (1) (a), (1) (b), (1) (c) and (1) (d) of the Convention.

<sup>127</sup> Article 12 (a) and (c) of the Convention.

<sup>128</sup> Article 19 (1)(a), (1)(b) and (1)(c) of the Convention.

<sup>129</sup> Article 19 (3) of the Convention.

to the Owner are blocked. Together with the aforesaid court order, the court may require the Contractor to furnish the appropriated security with the court.<sup>130</sup>

(7) The application of the Undertaking under the Convention in Thai Law

Even the Convention is an international law; however, Thailand has not signed or ratified this Convention. Therefore, Thailand is not the Contracting State under this Convention and do not have a duty under the Convention to have the domestic law as in compliance with the Convention.

The countries which have already made the ratification or accession of the Convention are Belarus, Ecuador, El Salvador, Gabon, Kuwait, Liberia, Panama and Tunisia. Additionally, the United States of America has also signed this Convention but not yet ratified.<sup>131</sup>

To the extent that the Contractor and the Owner agree to use the Undertaking, as the Third Party Guarantee, under the construction contract to be covered by the Convention, the guarantor or issuer shall be a bank or other institution with the place of business situated in the Contracting State.

### **3.3 The Third Party Guarantee under the CCC and International Practices**

#### **3.3.1 Comparison of the Third Party Guarantee under the CCC, the ISP 98 and the Convention**

In order to summarize the advantages and disadvantages of Third Party Guarantee under the CCC, the ISP 98 and the Convention, the comparison of each function or characteristic of the Third Party Guarantee was selected under this thesis, and described (in reference with the construction contract). In addition, the brief summary from this comparison is shown in the Appendix C Table: Comparison of the use of the Third Party Guarantee governed by the Amendment Principle of

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<sup>130</sup> Article 20 (1)(a), (1)(b) and (2) of the Convention.

<sup>131</sup> United Nations Treaty Collection, **United Nations Convention on Independent Guarantees and Stand-by Letters of Credit**, from: [https://treaties.un.org/Pages/ViewDetails.aspx?src=IND&mtdsg\\_no=X-15&chapter=10&lang=en](https://treaties.un.org/Pages/ViewDetails.aspx?src=IND&mtdsg_no=X-15&chapter=10&lang=en) (accessed December 7, 2015).

Suretyship under the CCC, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention.

### **3.3.1.1 Scope and Application of the Rule to the Third Party Guarantee**

#### (1) The Third Party Guarantee governed by the CCC

The principal (referred to in the construction contract as the “Contractor”) and the beneficiary (referred to in the construction contract as the “Owner”) can agree to apply the CCC to the third party guarantee without any prohibition by the CCC.

#### (2) Standby letter of credit covered by the ISP 98

The Contractor and the Owner can agree to apply the ISP 98 to the standby letter of credit without any prohibition by the ISP 98

#### (3) The Undertaking covered by the Convention

The Contractor and the Owner can agree to apply the Convention to the Undertaking only when (i) the guarantor/issuer’s place of business is situated in the Contracting State. In addition, the Convention will be automatically applied to the Undertaking if the rules of private international law lead to the application of the law of the Contracting State.

Thus, the Contractor and the Owner can freely agree to apply either the CCC or the ISP 98 to the Third Party Guarantee or the standby letter of credit without considering on the guarantor/issuer’s place of business while the consideration on the guarantor/issuer’s place of business is required for the application of the Convention.

### **3.3.1.2 Independent feature of the Third Party Guarantee**

#### (1) The Third Party Guarantee governed by the CCC

As the suretyship under the CCC is a secondary obligation and can be given only for a valid obligation and to the extent that a future obligation of the suretyship can be given only for the event which it would have effect and shall be specified the purpose and characteristic of underlying obligation, the Third Party Guarantee governed by the CCC is not independent from the construction contract.

#### (2) Standby letter of credit covered by the ISP 98

As the ISP 98 has expressly specified that a standby letter of credit is independent and that the enforceability of an issuer's obligation does not depend on (i) the issuer's right or ability to obtain reimbursement from the Contractor, (ii) Owner's right to obtain payment from the Contractor, (iii) any reference in a standby letter of credit to any reimbursement agreement or the construction contract, or (iv) the issuer's knowledge of performance or a breach of any reimbursement agreement or the construction contract.

(3) The Undertaking covered by the Convention

As the Convention has expressly specified that the Undertaking is independent and that the obligation of the guarantor or issuer to Owner is not (i) dependent upon the existence or validity of the construction contract, or (ii) subject to any other terms and conditions that are not specified in undertaking, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention is independent from the construction contract while the third party guarantee under the CCC is dependent on the construction contract.

**3.3.1.3 Internationality of the Third Party Guarantee**

(1) The Third Party Guarantee governed by CCC

As the CCC does not expressly prohibit the use of suretyship internationally, the Owner, the Contractor and the guarantor who concern with the Third Party Guarantee can either be in the same or in different countries.

(2) Standby letter of credit covered by the ISP 98

As the ISP 98 has expressly specified that it is intended to be applied for either domestic or international use, the Owner, the Contractor and the issuer who concern with standby letter of credit can be either in the same or in different countries.

(3) The Undertaking covered by the Convention

As the Convention has expressly specified that the Convention will be applied only to the international undertaking, any two of guarantor/issuer, the Owner and the Contractor can be in the different countries.

Thus, the CCC and the ISP 98 can apply for both domestic and international use while the Convention can only apply for international use.

#### **3.3.1.4 The Documentary Characteristic**

##### **(1) The Third Party Guarantee governed by the CCC**

The suretyship under the CCC does not specify about documentary mechanism which the Owner can demand for payment by the presentation of documents in accordance with the terms and conditions of the Third Party Guarantee to guarantor. However, in accordance with the amendment principle of suretyship under the CCC, if the Contractor is in default, the Owner shall notify such default to the guarantor within sixty days as from the date of default. Prior to such notification received by guarantor, the Owner will not be entitled to claim against the guarantor.<sup>132</sup>

##### **(2) Standby letter of credit covered by the ISP 98**

As the ISP 98 has expressly specified that a standby letter of credit is documentary, an issuer's obligations depend only on the presentation of documents.

##### **(3) The Undertaking covered by the Convention**

As the Convention specified that to the extent that the Owner demands for payment to guarantor or issuer, the Owner shall present the demand and any certification to guarantor or issuer, the Undertaking under the Convention is documentary.

Thus, standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention are documentary while the Third Party Guarantee governed by the CCC is not documentary.

#### **3.3.1.5 Responsibility of Guarantor or Issuer as Joint Debtor**

##### **(1) The Third Party Guarantee governed by the CCC**

The suretyship under the CCC specifies that any agreement which binds guarantor to be jointly liable with contractor or as joint debtor shall be void. However, if guarantor is the juristic person and agrees to be jointly liable with the Contractor or as joint debtor, such agreement is enforceable.

##### **(2) Standby letter of credit covered by the ISP 98**

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<sup>132</sup> Section 686 paragraph 1 of the CCC that was amended by the CCC Amendment No.20.

Even though standby letter of credit is independent from the construction contract, however, the ISP 98 does not expressly prohibit an agreement which binds issuer to be jointly liable with contractor or as joint debtor; therefore, such agreement is enforceable.

(3) The Undertaking covered by the Convention

Even though the Undertaking covered by the Convention is independent from the construction contract, however, the Convention does not expressly prohibit an agreement which binds guarantor or issuer to be jointly liable with contractor or as joint debtor; therefore, such agreement is enforceable.

Thus, an agreement, which binds guarantor or issuer to be jointly liable with contractor or as joint debtor, that is specified in standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention is enforceable, while such agreement is enforceable under the Third Party Guarantee governed by the CCC only to the extent that guarantor is juristic person.

**3.3.1.6 Duty of Beneficiary when Principal/Applicant is in Default**

(1) The Third Party Guarantee governed by the CCC

When the Contractor is in default under the construction contract, the Owner shall notify the guarantor who issued the Third Party Guarantee within sixty days since the date of default. In addition, since the debt is due, the guarantor is entitled to pay the debt without the request from the Owner.

(2) Standby letter of credit covered by the ISP 98

As standby letter of credit is independent from the construction contract, in the event that the Contractor is in default, the Owner to the standby letter of credit shall not be requested to notify such default to the issuer.

(3) The Undertaking covered by the Convention

As the Undertaking covered by the Convention is independent from the construction contract, in the event that the Contractor is in default, the Owner to the Undertaking will not be requested to notify such default to the guarantor or issuer.

Thus, to the extent that the Contractor is in default under the construction contract, the Owner to the Third Party Guarantee shall notify the guarantor within sixty day from the date of default, while the Owner to the standby

letter of credit or the Undertaking shall not be requested to notify such default to the issuer to the standby letter of credit or the guarantor or issuer to the Undertaking and shall not subject to the consequential effect, as specified in suretyship under the CCC.

### **3.3.1.7 Duty of Beneficiary when Reduction of the Amount of Secured Debt**

#### (1) The Third Party Guarantee governed by the CCC

To the extent that the Owner and the Contractor have an agreement which cause the reduction of the amount of secured debt, the Owner shall notify such agreement to the guarantor within sixty days from the agreement date. In addition, the responsibility of the guarantor shall be reduced in equal to a reduced amount under such agreement.

#### (2) Standby letter of credit covered by the ISP 98

As the standby letter of credit is independent from the construction contract, in the event that the Owner and the Contractor have an agreement to reduce the amount of secured debt, the Owner to the standby letter of credit shall not be requested to notify such agreement to the issuer.

#### (3) The Undertaking covered by the Convention

As the Undertaking under the Convention is independent from the construction contract, if the Owner and the Contractor have agreed to reduce the amount of secured debt, the Owner to the Undertaking shall not be requested to notify such agreement to the guarantor or issuer.

Thus, to the extent that the Owner and the Contractor have agreed to reduce the amount of secured debt under the construction contract, the Owner to the Third Party Guarantee governed by the CCC shall notify such agreement to the guarantor within sixty day, while the Owner to the standby letter of credit or the Undertaking shall not be requested to notify such agreement to the issuer to the standby letter of credit or the guarantor or issuer to the Undertaking and shall not be subject to the consequential effect which cause the reduction of the responsibility of the issuer or the guarantor/issuer proportionally, as specified in suretyship under the CCC.

### **3.3.1.8 Extension of time**

#### (1) The Third Party Guarantee governed by the CCC



To the extent that the Third Party Guarantee is issued for the secured obligation which is to be performed in a definite time, if the Owner grants the Contractor an extension of time for the secured obligation, the guarantor will be discharged, unless the guarantor agrees with such extension of time. In addition, if the guarantor is not a financial institution or a person who undertakes suretyship business for remuneration, such guarantor shall not enter into an agreement which allow the Owner to grant an extension of time to the Contractor, in advance.

(2) Standby letter of credit covered by the ISP 98

As the standby letter of credit is independent from the construction contract, so, if the Owner and the Contractor have an agreement to extend the time for any performance under the construction contract, the issuer will not be discharged from the standby letter of credit.

(3) The Undertaking covered by the Convention

As the Undertaking under the Convention is independent from the construction contract, if the Owner and the Contractor have an agreement to extend the time for any performance under the construction contract, the guarantor/issuer will not be discharged for the Undertaking.

Thus, to the extent that the Owner grants an extension of time for the secured obligation, the guarantor to the Third Party Guarantee governed by the CCC will be discharged, unless the guarantor agrees with such extension of time on time to time basis, while the issuer to the standby letter of credit or the guarantor or issuer to the Undertaking will not be discharged whether such person agrees with such extension of time.

### **3.3.1.9 Exception to the Payment Obligation**

(1) The Third Party Guarantee governed by the CCC

The suretyship under the CCC does not specify the right of the guarantor to withhold the payment of secured amount under the Third Party Guarantee based on fraud, abuse, or similar matter to the Owner. However, in the event that such matter occurs, a person who is affected from the matter shall be entitled to execute the concerning right as specified in the CCC or other applicable laws.

(2) Standby letter of credit covered by the ISP 98

The ISP 98 does not provide for defenses to honor based on fraud, abuse, or any similar matter. These matters will be governed by the applicable laws.

(3) The Undertaking covered by the Convention

To the extent that it is manifest and clear that (i) any presented document is not real, (ii) no payment is due on the basis asserted in the demand, or (iii) judging by the type and purpose of the Undertaking, the demand has an impossible basis, the guarantor or the issuer, which acts in good faith, has a right to withhold demanded payment. In addition, the Contractor shall also have the right to request the relevant court for the provisional court measures.

Thus, to the extent that the fraud on the demand of payment occurs, the guarantor or the issuer to the Undertaking shall have a right to withhold demented payment, while the guarantor to the Third Party Guarantee governed by the CCC and the issuer to the standby letter of credit covered by the ISP 98 shall not have such right and such matter will be governed by the applicable law.

## **CHAPTER 4**

### **THE AMENDMENT OF SURETYSHIP AND EFFECTS**

This Chapter consists of three parts. The first part focuses on the principle of suretyship under the CCC and the amendment of the principle of suretyship in accordance with the CCC which was amended by the CCC Amendment No.20 and the CCC Amendment No.21. The second addresses the effects of the amendment of the principle of suretyship under the construction contract for large projects. The last part highlights the use of the international laws or practices to mitigate the effect of the amended principle of suretyship on the Third Party Guarantee under the construction contract.

#### **4.1 Principle of Suretyship under the CCC**

##### **4.1.1 Relationship between Suretyship and the Third Party Guarantee under the Construction Contract.**

Because Thailand does not have specific law concerning Third Party Guarantee, the closest principle that can be applicable is the principle of suretyship under the CCC. Therefore, it is important to study the principle of suretyship in order to understand how Third Party Guarantee applies in the context of Thai laws.

##### **4.1.2 Principle of Suretyship**

The principle of suretyship under the CCC is one of the principles that had not been amended since Book 3 of the CCC was firstly promulgated in B.E. 2471. However, in B.E. 2557, the first amendment to the principle of suretyship was introduced by the Civil and Commercial Code Amendment Act, (No.20), B.E. 2557 (“CCC Amendment No.20”) which was announced in the Royal Gazette on 13 November B.E. 2557 and became effective on 11 February B.E. 2558. The rationale of this amendment is the inadequate protection of the surety who is not the primary debtor. In practice, the creditor, who mostly has more bargaining power, often

requests the surety to be liable as the primary obligor. Such surety cannot be protected by the existing principle of suretyship.<sup>133</sup>

However, after the CCC Amendment No.20 was proclaimed, there were many requests for a re-amendment from concerning parties to the Third Party Guarantee, such as financial institutions, as guarantor, creditors, and the debtor itself. The requests were based on the prohibition that the guarantors were not allowed to bind themselves to be jointly liable with the debtor, which is the core function of the Third Party Guarantee. Thus, in this situation, the Third Party Guarantee seems useless to the construction contract.

On 14 July B.E. 2558, the Civil and Commercial Code Amendment Act, (No.21), B.E. 2558 (“CCC Amendment No.21”) was proclaimed in the Royal Gazette and became effective on 15 July B.E. 2558. The main rationale behind the change was to improve the amended principle of suretyship to be more suitable for current business. The surety, who is a juristic person, may agree to bind himself as the primary obligor to the suretyship, while, a financial institution or a person who undertakes suretyship business for remuneration, as the surety, can agree to give the advance consent for an extension of time grant by the creditor.<sup>134</sup>

As the Third Party Guarantee under the construction contract is governed by the principle of suretyship, the amendment of the principle of suretyship therefore directly affects the Third Party Guarantee.

#### **4.1.2.1 The Primary Principle of Suretyship**

Prior to the amendment under the CCC Amendment No.20, the principle of suretyship can be summarized as follows:

(1) The suretyship is the contract which a third party, called a surety, agrees to binds himself to a creditor in order to satisfy an obligation when the debtor fails to perform such obligation.<sup>135</sup>

(2) Only to the valid obligation can a suretyship be given for. However, if such obligation is a future obligation or a conditional obligation, such obligation may be secured only in the event in which it would be enforceable.<sup>136</sup>

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<sup>133</sup> Remark of the CCC Amendment No.20.

<sup>134</sup> Remark of the CCC Amendment No.21.

<sup>135</sup> Section 680 paragraph 1 of the CCC.

(3) The creditor shall have the right to demand the surety to perform the secured obligation when the debtor is in default.<sup>137</sup>

(4) The surety may agree to be jointly liable with the debtor as the primary obligor. In this event, the surety shall not have the following refusal rights:<sup>138</sup>

a. The right to request the creditor to demand the debtor to perform first.<sup>139</sup>

b. The right to request the creditor to first make an execution against the property of the debtor.<sup>140</sup>

c. The right to request the creditor to first make an execution against the real security of the debtor which the creditor has already held.<sup>141</sup>

(5) To the extent that the surety has performed its obligation to the creditor, the surety shall be entitled to recourse against the debtor for the principal, including the interest and other benefits.<sup>142</sup>

(6) If the secured obligation of the debtor is extinguished by whatsoever cause, the surety shall be discharged.<sup>143</sup>

(7) To the extent that the obligation under the underlying transaction is to be performed at a definite time, if the creditor grants a time extension of such obligation to the debtor, the surety shall be discharged, unless the surety has agreed to such extension of time.<sup>144</sup>

#### **4.1.2.2 The Amended Principle of Suretyship**

The principle of suretyship under the CCC is first amended by the CCC Amendment No.20, then, re-amended by the CCC Amendment No.21. The followings are the summary of the amendments to the principles of suretyship under

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<sup>136</sup> Section 681 paragraph 1 and 2 of the CCC.

<sup>137</sup> Section 686 of the CCC.

<sup>138</sup> Section 691 of the CCC.

<sup>139</sup> Section 688 of the CCC.

<sup>140</sup> Section 689 of the CCC.

<sup>141</sup> Section 690 of the CCC.

<sup>142</sup> Section 693 of the CCC.

<sup>143</sup> Section 698 of the CCC.

<sup>144</sup> Section 700 of the CCC.

the CCC, as amended by the CCC Amendment No.20 and the CCC Amendment No.21:

(1) Since the principle of suretyship allows a future or conditional obligation to be secured, most of the creditors generally request the surety to bind himself to any future or conditional obligations between the creditor and the debtor, even such obligation may not occur under the underlying transaction.<sup>145</sup>

In order to protect the surety from such uncertain agreement, the CCC Amendment No.20 states that some specific information of such future or condition obligation must be specified in the provision of suretyship to limit the liability of the surety.

To the extent that the suretyship is given to secure the future of conditional obligation, the followings information shall be specified:

- a. The purpose of the obligation that is secured;
- b. The characteristics of the secured obligation;
- c. The maximum secured amount under such suretyship; and
- d. The period of the secured obligation, however, to the extent that the suretyship is given for a series of transactions, such period does not have to specified.<sup>146</sup>

In addition, if the creditor requests the surety to waive the specification of the foregoing information, as required by Section 681 paragraph 2 of the CCC which was amended by the CCC Amendment No.20, such agreement shall be void.<sup>147</sup>

(2) As the principle of suretyship allows the surety to be jointly liable with the debtor or liable as primary obligor, most of the creditors, who have more bargaining power, generally request the surety to be jointly liable with the debtor.<sup>148</sup>

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<sup>145</sup> Suda Visrutpich. “*Explanation of Laws of Suretyship and Mortgage Amended by the Civil and Commercial Code Amendment Act, No. 20, B.E. 2557*” **Memory Book of Khun Chumpol Juntratip** (December 19, 2014): 285-286.

<sup>146</sup> Section 681 paragraph 2 of the CCC that was amendment by the CCC Amendment No.20.

<sup>147</sup> Section 685/1 of the CCC that was amended by the Amendment CCC No.21.

<sup>148</sup> Suda Visrutpich, *Supra note* 145, at 289-290.

In order to protect the surety from such agreement, the CCC Amendment No.20 prohibits an agreement which the surety agrees to be jointly liable with the debtor.

To the extent that the provision of the suretyship specifies that the surety agree to be jointly liable with the debtor, such agreement shall be void.<sup>149</sup>

After such amendment of the principle of suretyship was declared, there were heavy demands for the re-amendment to allow the guarantor under the Third Party Guarantee to be jointly liable, especially from the parties relating to Third Party Guarantee such as commercial banks, creditors and debtors.

Finally, the CCC Amendment No.21 was issued and allowed juristic persons to be jointly liable with the debtor. Therefore, to the extent that the surety is the juristic person, even the provision of the suretyship which specified that the surety agree to be jointly liable with the debtor is void, such provision shall be enforceable.<sup>150</sup>

However, there is the problem concerning the effect of the suretyship agreement where the surety, who is the juristic person, agreed to be jointly liable with the debtor and such agreement was made during the period from the effective date of the CCC Amendment No.20 to the date prior to the effective date of CCC Amendment No.21. Even if the transitional provision (Section 8) of the CCC Amendment No.21 specifies that any suretyship agreement, which is made during such transitional period, shall be enforceable if such agreement does not conflict over the CCC Amendment No.21,<sup>151</sup> some provision of the suretyship agreement is already void under the CCC Amendment No.20, for instance, the provision which the surety agrees to be jointly liable with the debtor or give advance consent to grant time extension. This generates questions as to how the voided provision,<sup>152</sup> become re-enforceable. There will not be an answer to this question until the Supreme Court of Thailand has the decision concerning this issue.

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<sup>149</sup> Section 681/1 of the CCC that was amended by the CCC Amendment No.20.

<sup>150</sup> Section 681/1 paragraph 1 and 2 of the CCC that was amended by the CCC Amendment No.20 and the CCC Amendment No.21.

<sup>151</sup> Section 8 of the CCC Amendment No.21.

<sup>152</sup> Section 172 of CCC.

(3) Under the principle of suretyship, the creditor shall be entitled to claim against the surety whenever the debtor is in default.<sup>153</sup> In practice, some creditors intend not to notify the surety and execute their right to claim against the surety, even if the surety is ready to satisfy the creditor. This will cause the interest, compensation, or charge (if any) to grow. If the surety had known that the debtor is in default, the surety may have performed the secured obligation to the creditor. This practice of the creditor is an unfair practice to the surety.<sup>154</sup>

Hence, in order to protect the surety from this unfair practice of the creditor, the CCC Amendment No.20 and No.21 added the mechanism concerning the notification by the creditor in such event. Such mechanism can be summarized as follows:

a. To the extent that the debtor is in default, the creditor shall notify such default to the surety within sixty days from the default date, while the surety shall be entitled to perform the secured obligation to the creditor whether he has received such notification. In addition, until such notification has been received by the surety, the creditor shall not be entitled to claim against the surety.<sup>155</sup>

However, this amended principle of suretyship does not describe the details required to be specified in such notification.

b. To the extent that the creditor fails to notify the surety within sixty days from the default date, the surety shall be released from an interest, any compensations, or charges which are occurred after such period of time.<sup>156</sup>

c. To the extent that (i) the creditor is entitled to claim against the surety after the surety has received the notification or (ii) the surety is entitle to perform the due secured obligation, the surety shall be entitled to perform

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<sup>153</sup> Section 686 of the CCC.

<sup>154</sup> Suda Visrutpich, *Supra note* 145, at 292-293.

<sup>155</sup> Section 686 paragraph 1 of the CCC that was amended by the CCC Amendment No.20.

<sup>156</sup> Section 686 paragraph 2 of the CCC that was amended by the CCC Amendment No.20.



the secured obligation in whole or under the conditions and means that the debtor and the creditor have mutually agreed prior to the default.<sup>157</sup>

For instance, after the debtor is in default, the creditor and the debtor have agreed upon the debt restructuring agreement, where the creditor agrees to reduce the amount of debt or to extend the period of the secured obligation. If the debtor is in breach of any obligations under such debt restructuring agreement, the surety shall be entitled to perform the secured obligation, as amended by such debt restructuring agreement.<sup>158</sup>

d. During the period that the surety is performing the secured obligation, whether under the original suretyship agreement or under the debt restructuring agreement, if the debtor is in default, the creditor cannot increase the rate of interest, such as the default interest rate.<sup>159</sup>

e. An agreement which is different from the foregoing mechanisms and conditions shall be void.<sup>160</sup>

f. Under the transitional provision of the CCC Amendment No.20, the obligation of the creditor to notify the surety shall apply any suretyship agreement, whether such agreement has been executed before or after the effective date of the CCC Amendment No.20. That is to say if, after the effective date of the CCC Amendment No.20, the debtor is in default of the secured obligation, which is executed prior to the effective date of the CCC Amendment No.20, the creditor also has to notify such default to the surety.<sup>161</sup>

(4) The underlying transaction and the suretyship are separate transactions. Therefore, if the creditor agrees to reduce a secured amount under the underlying transaction to the debtor, and the creditor or the debtor does not inform the surety, the surety shall not be aware of such information and shall not enter into a

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<sup>157</sup> Section 686 paragraph 3 of the CCC that was amended by the CCC Amendment No.20.

<sup>158</sup> Suda Visrutpich, *Supra* note 145, at 293.

<sup>159</sup> Section 686 paragraph 4 of the CCC that was amended by the CCC Amendment No.20.

<sup>160</sup> Section 685/1 of the CCC that was amended by the CCC Amendment No.21.

<sup>161</sup> Section 19 of the CCC Amendment No.21.

negotiation with the creditor to lower the debt amount.<sup>162</sup> Hence, the surety, who is a secondary debtor, shall be liable to the creditor in the full amount of the secured obligation, while the debtor shall be liable to the creditor only in the reduced amount. This creates an unfair practice to the surety.

In order to protect the surety from such unfair practice, the CCC Amendment No.20 and No.21 added the mechanism concerning the notification by the creditor to the surety in such event. Such mechanism can be summarized as follows<sup>163</sup>:

a. To the extent that the creditor and the debtor have an agreement to reduce the secured amount, the creditor shall notify such agreement to the surety within sixty days from the date of agreement. However, this amended principle of suretyship does not describe the details required to be specified in such notification.

In practice, an agreement between the creditor and debtor to reduce the secured amount shall be made in the form of the debt restructuring agreement where the provision to reduce the secured amount shall be cancelled if the debtor breaches any provision of the debt restructuring agreement. Hence, without this amended principle, the surety cannot surrogate the privilege of the debtor under the debt restructuring agreement.<sup>164</sup>

b. If (i) the debtor pays the remained secured amount in whole, or (ii) the debtor pays the reduced secured amount in part and the surety has paid for the remaining, or (iii) the surety has paid the reduced secured amount in whole, the surety shall be discharged.

c. To the extent that the creditor and the debtor have an agreement to reduce the secured amount with the condition that the debtor shall pay such reduced secured amount within the specific period of time, if the surety receives

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<sup>162</sup> Suda Visrutpich, *Supra* note 145, at 296-297.

<sup>163</sup> Section 691 paragraph 1 of the CCC that was amended by the CCC Amendment No.21.

<sup>164</sup> Office of Judicial and Legal Affairs, Office of the Judiciary. **Consideration of the Law of Suretyship and Mortgage, as amended under the Civil and Commercial Code Amendment No.20 and No.21**, 7, from [http://www.jla.coj.go.th/doc/data/jla/jla\\_1456302939.pdf](http://www.jla.coj.go.th/doc/data/jla/jla_1456302939.pdf) (accessed March 1, 2016).

a notification concerning the reduced secured amount after the foregoing period of time has expired, the surety shall be entitled to pay such reduced secured amount within sixty days from the receiving date.

d. An agreement which creates more burdens to the surety than as specified in the foregoing mechanisms and conditions shall be void.<sup>165</sup>

e. Under the transitional provision of the CCC Amendment No.21, if the creditor and the debtor have an agreement to reduce the secured amount or the debt restructuring agreement during the period from the effective date of the CCC Amendment No.20 to the date prior to the effective date of CCC Amendment No.21, the creditor shall notify such agreement to the surety within sixty days from the effective date of CCC Amendment No.21.<sup>166</sup>

(5) Under the principle of suretyship, to the extent that the secured obligation is to be performed at a definite time, if the creditor grants a time extension of such obligation without the consent of the surety, the surety shall be discharged. However, the surety is allowed to give advance consent to the creditor.

In practice, most of the creditors will require the surety to give advance consent on such extension of time by the creditor, which results in the extension of period of suretyship and the surety shall also be liable for any interest, compensation and charges, which are occurred during such extension period. This is an unfair practice to the surety.<sup>167</sup>

In order to protect the surety from such unfair practice, the CCC Amendment No. 20 prohibits the creditor from requesting advance consent on such extension of time. If the surety gives such advance consent to the creditor, such advance consent shall not be enforceable.<sup>168</sup>

This amendment was also a subject of a protest for the re-amendment by concerning parties of the Third Party Guarantee. The CCC Amendment No.21 was finally proclaimed and provides certain exceptions for

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<sup>165</sup> Section 691 paragraph 2 to the CCC that was amended by the CCC Amendment No.20.

<sup>166</sup> Section 9 of the CCC Amendment No.21.

<sup>167</sup> Suda Visrutpich, *Supra* note 145, at 298-299.

<sup>168</sup> Section 700 paragraph 2 to the CCC that was amended by the CCC Amendment No.20.

financial institutions and a person who undertakes suretyship business for remuneration. To the extent that the surety is a financial institution or person who undertakes suretyship business for remuneration, such advance consent on time extension shall be enforceable.

Nevertheless, there is an issue concerning the effect of the suretyship agreement in accordance with this re-amendment during transitional period. The transitional provision (Section 8) of the CCC Amendment No.21 specifies that any suretyship agreement, which is made during the period from the effective date of the CCC Amendment No.20 to the date prior to the effective date of CCC Amendment No.21, shall be enforceable if such agreement does not conflict over the CCC Amendment No.21.<sup>169</sup> Therefore, even if this agreement is unenforceable under the CCC Amendment No.20, it does not conflict over the CCC Amendment No.21. As a result, this agreement shall become enforceable from the effective date of the CCC Amendment No.21.

(6) Under the principle of suretyship, the surety is protected from unfair practices by the following principles: (i) in addition to the defense of the surety against the creditor, the surety can also use the defense of the debtor against the creditor,<sup>170</sup> (ii) to the extent that the secured obligation is extinguished, the surety shall be discharged,<sup>171</sup> and (iii) the suretyship for a series of transaction without limit of time can be terminated for any future transaction if the surety notify such termination to the creditor.<sup>172</sup>

However, the creditor usually requires the surety to waive such protections under the principle of suretyship, which is unfair to the surety.<sup>173</sup>

In order to protect the surety from such unfair practice, the CCC Amendment No.21 rules that an agreement concerning the waiver of the foregoing rights of the surety shall be void.<sup>174</sup>

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<sup>169</sup> Section 8 of the CCC Amendment No.21.

<sup>170</sup> Section 694 of the CCC.

<sup>171</sup> Section 698 of the CCC.

<sup>172</sup> Section 699 of the CCC.

<sup>173</sup> Suda Visrutpich, *Supra note* 145, at 291.

<sup>174</sup> Section 685/1 of the CCC Amendment No.21.

## **4.2 The Effect of the Amended Principle of Suretyship under the CCC to the Third Party Guarantees under the Construction Contract.**

Because the terms of the Third Party Guarantee under the construction contract, in which the construction work is executed in Thailand, are mostly governed by the principles of suretyship under CCC, hence, the amendments of the principles of suretyship cause significant effects to the provisions of the Third Party Guarantee under the construction contract, including the duty and liability of all concerning parties. In this topic, such significant impacts will be discussed.

### **4.2.1 Details of the Third Party Guarantee**

The amended principle of suretyship under the CCC Amendment No.20 specifies that if the secured obligation is a future obligation, the suretyship contract shall state the following information: (i) the purpose; (ii) the characteristics; (iii) the maximum amount; and (iv) the period of the secured obligation<sup>175</sup>.

As the Third Party Guarantee under to the construction contract is a guarantee for a future obligation, it must also comply with the amended principle. The Third Party Guarantee shall specify the following information:

- (1) The purpose of the secured obligation;
- (2) The characteristics of the secured obligation;
- (3) The maximum amount of the secured obligation; and
- (4) The period of the secured obligation.

As it is a Third Party Guarantee for construction contract, the purpose and characteristics of the secured obligation are clear. However, it is problematic to identify maximum secured amount and the period of the secured obligation.

In practice, the secured amount of the Third Party Guarantee under the construction contract is calculated in percentage to the contract price, such as, ten (10) per cent of the contract price. However, it is known that, during the construction period, the contract price is subject to changes due to the variation of the construction work to be performed. Thus, some of the Third Party Guarantee will specify the

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<sup>175</sup> Section 681 paragraph 2 to the CCC that was amended by the CCC Amendment No.20.

conditions concerning the change of the contract price. For instance, if the contract price adjusts, whether to higher or lower amount, the secured amount shall be adjusted accordingly. Under the amended principle, this type of condition might not be valid. In order to avoid this issue, both parties to the construction contract may agree upon the proper secured amount which may be higher than the foregoing amount or, prior to execute the amendment agreement to the construction contract concerning the variation of the contraction work, the Contractor shall submit the amended Third Party Guarantee which the secured amount has changed according to the amended contract price.

Another important issue is the period of the Third Party Guarantee which is required to be clearly expressed under the amended principle of suretyship. As described in Topic 2.3.2.6, the Third Party Guarantee under the construction contract often specifies that the Third Party Guarantee will expire when all of the Contractor's obligations and liabilities have been discharged, instead of stating specific date, due to uncontrolled events which may affect the completion schedule of the construction work. To the extent that the Third Party Guarantee indicates a specific period, if such period expires before the completion of the construction work, the Contractor shall re-submit a new Third Party Guarantee to the Owner. However, the foregoing procedure may create risk where the Contractor fails to make a re-submission to the Owner. To eliminate such risk, a certain period, which is specified in the Third Party Guarantee, may be longer than the proposed completion schedule of the construction work, for instance, the proposed completion term plus two months.

Both of the above mechanisms can, however, cause additional burden, not only to the Contractor to provide the amended Third Party Guarantee, but also to the Owner. As a result, expenses relating to the amended Third Party Guarantee may increase.

#### **4.2.2 Joint Liability of Guarantor**

The amended principle of suretyship under the CCC Amendment No.20 prohibits the surety from agreeing to be jointly liable with the debtor as the primary obligor.<sup>176</sup>

However, the amended principle of suretyship under the CCC Amendment No.21 specifies that if the guarantor is a juristic person, such guarantor shall be allowed to be jointly liable with the debtor.<sup>177</sup>

Most of the Third Party Guarantee forms under the construction contract are issued by financial institutions or juristic persons, which are not subject to this prohibition under the amended principle of suretyship. However, one of the Third Party Guarantee forms, which is the Parent/Corporate Guarantee, may be affected. To the extent that Parent/Corporate Guarantee is given by shareholders of the Contractor, if the shareholder is not a juristic person, such shareholder is then prohibited from being jointly liable with the Contractor. Thus, such shareholder, as guarantor, will have the following refusal rights: (1) the right to demand the Owner that the Contractor shall be first called upon to perform when the Owner demands from the Third Party Guarantor, (2) the right to require the Owner to first make execution against the property of the Contractor if the guarantor can prove that the Contractor has the means to perform and that execution would not be difficult and (3) the right to require the Owner to first have the obligation performed out of the real security if the Owner holds real security belonging to the Contractor. The foregoing refusal rights of individual shareholder, as guarantor, will change the unconditional guarantee, which most of guarantees under the construction contract are, to the conditional guarantee which significantly reduces the benefit of Owner and causes more burdens of proof to the Owner in order to calm this Third Party Guarantee from the guarantor.

#### **4.2.3 Extension of Time**

During the execution of the construction work, if the Contractor fails to complete any part thereof within the specified time, the Owner shall be entitled to

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<sup>176</sup> Section 681/1 paragraph 1 to the CCC that was amended by the CCC Amendment No.20.

<sup>177</sup> Section 681/1 paragraph 2 to the CCC that was amended by the CCC Amendment No.21.

claim liquidated damages, as specified in the construction contract. However, the Owner sometimes agrees to extend such specified time for the Contractor due to various reasons. For instance, the Owner agrees to extend such specified time in exchange with (i) the commitment of the Contractor to speed up the construction work by increasing manpower or working hours, or (ii) other expenses or costs which the Owner has to pay to the Contractor. The extension of the specified time may affect the responsibility of the guarantor under the Third Party Guarantee. Normally, the guarantor shall be discharged if the guarantor does not give the consent to grant such time extension to the Owner. Thus, in order to ensure that the guarantor shall not be discharged, advance consent from the guarantor must be obtained.

Under the amended principle of suretyship under the CCC Amendment No.20, an agreement that the guarantor has made in advance as regards his consent to the extension of time before the Owner grants a time extension to the Contractor is not enforceable.<sup>178</sup>

However, the amended principle of suretyship under the CCC Amendment No.21 specifies that if the guarantor is a financial institution or a person undertaking suretyship business for remuneration, such guarantor shall be allowed to grant an extension of time in advance.<sup>179</sup>

Most of the Third Party Guarantee forms under construction contract specify that, to the extent that the Owner grants a time extension, or allows the Contractor to deviate from any conditions of the construction contract without the guarantor knowledge, it shall be deemed that such grants have been made with the guarantor's consent. The foregoing provision of the Third Party Guarantee means if the guarantor is not a financial institution or a person undertaking suretyship business for remuneration, the guarantor shall be prohibited to give such prior consent under the amended principle. Even though, most of the Third Party Guarantee forms under the construction contract are issued by financial institution, one of the Third Party Guarantee forms, which is the Parent/Corporate Guarantee, shall be affected as a

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<sup>178</sup> Section 700 paragraph 2 to the CCC that was amended by the CCC Amendment No.20.

<sup>179</sup> Section 700 paragraph 3 to the CCC that was amended by the CCC Amendment No.21.



person who issues this Third Party Guarantee, is mostly not a financial institution or a person in suretyship business. Hence, to the extent that the Owner requires the Contractor to provide a Parent/Corporate Guarantee, the Owner must remember that he must request consent from the guarantor of the Parent/Corporate Guarantee before granting the Contractor time extension. The foregoing, however, may cause some Owners to deny time extension to protect his benefit.

#### **4.2.4 Default of the Contractor**

According to the amended principle of suretyship under the CCC Amendment No.20, when the Contractor is in default, the Owner has a duty to notify all guarantors under any Third Party Guarantees of the contractor contract within sixty days from the default date. If the Owner fails to notify any guarantor within the said period, such guarantor shall be discharged from the interest and reimbursement including any charges which occurred after the said period. In addition, until such notification is received by the guarantor, the Owner shall not be entitled to claim against the guarantor. Nonetheless, the guarantor shall be entitled to perform the secured obligation whether he has received a notification from the Owner or not.<sup>180</sup>

In addition, the amended principle of suretyship under the CCC Amendment No.21 imposes that any agreement between the guarantor and the Owner in relation to the Third Party Guarantee which is different from this principle shall be void.<sup>181</sup>

The foregoing is a new principle which is added under the amendment of the principle of suretyship. This new principle generates more burdens to the Owner who receives a Third Party Guarantee from the Contractor, which may be summarized as follows:

(1) It is rather difficult to consider whether there is any event of default by the Contractor under the construction contract for large projects. Sometimes, this task is too complex for non-lawyer or anyone who lacks legal background, especially for the Owner and its personnel who have mainly engineering background. Even though the Owner or its personnel are aware that the Contractor

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<sup>180</sup> Section 686 to the CCC that was amended by the CCC Amendment No.20.

<sup>181</sup> Section 685/1 paragraph 2 to the CCC that was amended by the CCC Amendment No.21.

may be in default, most of them must consult their lawyer before notifying the Contractor and the guarantor of such default.

(2) If the Contractor is in default, the Owner shall notify such default to the guarantor within sixty days from the default date. However, the amended principle of suretyship does not provide any detail on the commencement of such period of sixty day.

For example, in the event that the Owner considers and notifies the Contractor that he is in default, if the Contractor denies such default, there must be dispute settlement. After the completion of the settlement of dispute, if the period of dispute settlement consumes more than sixty days, which results in the Owner failing to notify the guarantor within sixty days from the actual default date, whether the right of the Owner to claim interest, compensation, or charges occurred after the period of sixty day will be nullified.

Whether when the period of sixty days starts, either on actual default date or on default date, as agreed by the Owner and the Contractor, is still an issue which requires further clarification.

(3) As described in Chapter 2, in some construction contracts, the Contractor has to provide four types of the Third Party Guarantee, which are Advance Payment Guarantee, Performance Guarantee, Retention Money Guarantee and Parent/Corporate Guarantee, to the Owner. When the Contractor is in default, the Owner has to send at least four notifications to all guarantors. Hence, additional monitoring procedure in order to notify the default to the guarantors is required and the Owner needs more manpower to observe and comply with the procedures.<sup>182</sup> In addition, because the Third Party Guarantee under the construction contract is a guarantee to the future obligation within the period of the construction, if the Contractor is in default during the period of construction more than one time, the Owner has to notify any and all default to all guarantors under the construction contract, whether the Owner wishes to claim from such Third Party Guarantees or not. This notifying duty put more burden and costs to the Owner.

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<sup>182</sup> Panita Nguansiri, "Problems with the Suretyship Provisions in the Civil and Commercial Code of Thailand Amendment Act (No.20) B.E. 2557 (2015)" (Master's Individual Research Paper, Faculty of Law, Chulalongkorn University, 2014), 38.

(4) After the Contractor is in default and after the guarantor has received the notification of the default from the Owner, the guarantor shall be entitled to perform the secured obligation to the Owner under the amended principle of suretyship. In some construction contracts, the Contractor has to provide four types of the Third Party Guarantee. If any or all guarantor(s) makes this payment to the Owner, the payment may cause the cash flow problem to the Contractor and subsequently causes the Contractor to be unable to perform the construction work. In practice, even though the Owner has the right to claim the liquidated damages from the Contractor during the construction period, some of the Owners will not exercise such right at that time and chooses to exercise such right when most of the construction work are complete to avoid the interruption of the Contractor's performance due to the cash flow problem.

(5) In the event of delay in performance of the Contractor resulting in default by the Contractor, the Owner shall be entitled to claim the liquidated damages for delay. In such case, the Owner shall notify the default to the guarantor. However, at the time of notification, which is the default date, the Owner has not known the exact amount of these liquidated damages. The amount of liquidated damages for delay increases daily and the exact amount will be finalized only when the delayed work is completed.<sup>183</sup> Hence, the Owner can only specify in the notification to the guarantor that the Contractor is in default without giving the exact amount of liquidated damages for delay. In this situation, even the guarantor is liable to pay liquidated damages for delay under the amended principle, the guarantor cannot perform as he also does not know the exact amount thereof. Furthermore, the amended principle does not expressly specify whether or not the Owner has to notify the guarantor the exact amount of liquidated damages for delay again once the work is completed. If the Owner does not re-notify the guarantor such exact amount, whether or not, the guarantor will not be able to execute his right under this amended principle. In order to mitigate the effect to the guarantor, the Owner shall notify the following information to the guarantor: (i) information specifying that the Contractor is in default under the construction contract, (ii) the mean of calculation of the

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<sup>183</sup> Joseph A. Huse, *Supra note 33*, at 63.

liquidated damages for delay including the default interest on daily rate, and (iii) the maximum amount of this liquidated damages for delay under the construction contract.

#### **4.2.5 Reduction of the Debt for the Contractor**

Under the amended principle of suretyship, in the event that the Owner has an agreement to reduce the amount of secured debt with the Contractor, the Owner shall notify such agreement to the guarantor within sixty days from the agreement date. If the Contractor repays the reduced debt or the Contractor partially repays the reduced debt and the guarantor repays the rest of the debt or the Contractor fails to repay the reduced debt but the guarantor repays the full amount of reduced debt, the guarantor shall be discharged.<sup>184</sup> Any agreement which causes more burdens to the guarantor than as specified in the foregoing clauses shall be void.

The foregoing provision is a new principle which was added under the amendment of the principle of suretyship. After the promulgation of this new principle, if the Owner agrees to waive any right to make any claims, such as the liquidated damages, to the Contractor, the Owner shall be subject to the followings:

(1) To the extent that the Owner agrees to waive or reduce the liquidated damages which the Owner has under the construction contract to the Contractor, any and all guarantors under the construction contract shall be subject to the reduced amount under such agreement; and

(2) The Owner shall notify such agreement to any and all guarantors under any Third Party Guarantee of the contractor contract within sixty days from the agreement date.

As described in Topic 4.2.4, in some construction contracts, the Contractor has to provide four types of the Third Party Guarantees. Consequently, if the Owner and the Contractor make an agreement concerning the waiver or reduction of the liquidated damages, which is part of the secured obligation, the Owner must then notify such agreement to all guarantors. This seems to be onerous to the Owner.

In addition, an arrangement on the waiver or reduction of the liquidated damages is not made due to mere kindness of the Owner. Instead, it is

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<sup>184</sup> Section 691 paragraph 1 to the CCC that was amended by the CCC Amendment No.21.

initiated because it is more beneficial to the Owner and the Contractor, or because it is easier for the Owner to manage the construction project, or because the Owner has actually contributed in causing the default by the Contractor. The examples of such incident are (i) the Owner requests the Contractor to perform additional works and exchange additional contract price with the liquidated damages in order to avoid the amendment to the construction contract, especially when the additional contract price is not high, or (ii) the Owner requests the Contractor to put additional effort to speed up the delay part of construction work by increasing manpower or working hours and the Contractor, in exchange, requests the Owner to waive or reduce the liquidated damages.<sup>185</sup> As a result, the Owner and the Contractor may not wish to notify this agreement to any third party. Furthermore, because of additional duty to notify all guarantors, the Owner and the Contractor are even more prone to not make any debt reduction, but instead make a side arrangement between each other.

(3) If the Contractor repays the reduced debt or the Contractor partially repays the reduced debt but the guarantor repays the rest of the debt or the Contractor fails to repay the reduced debt but the guarantor repays the full amount of reduced debt, the guarantor shall be discharged from such debt. If any guarantor exercises his right under this provision by repaying the reduced debt, which the guarantor will be entitled to recourse such amount from the Contractor, such recourse shall cause the cash flow problem to the contract. Consequently, it will affect the performance of the Contractor under the construction contract, while such guarantor shall already be discharged.

#### **4.2.6 The enforceability of the Third Party Guarantee made during the period after the effective date of CCC Amendment NO.20 to the date before the effective date of CCC Amendment No.21**

Under the transitional provision of the CCC Amendment No.21, any agreement made during the period from the effective date of the CCC Amendment No.20 to the date prior to the effective date of CCC Amendment No.21 shall be

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<sup>185</sup> See Joseph A. Huse, *Supra* note 33, at 9-16.

enforceable if such agreement does not conflict with the provision of the CCC Amendment No.21.<sup>186</sup>

Hence, any Third Party Guarantee governed by the CCC made during the period from the effective date of the CCC Amendment No.20 to the date prior to the effective date of CCC Amendment No.21 (“Transitional Third Party Guarantee”) shall be subject to the transitional provision of the CCC Amendment No.21. The core of the transitional provision can be digested as follows:

(1) The provision of the Transitional Third Party Guarantee, which was unenforceable during the period of the CCC amendment No.20 and became enforceable during the period of the CCC Amendment No.21.

The provision where the guarantor, who is a financial institution, agrees to give advance consent on time extension time to the Owner, shall not be enforceable under the period of CCC Amendment No.20.<sup>187</sup> However, under the CCC Amendment No.21, the foregoing agreement shall be enforceable.<sup>188</sup>

Thus, in accordance with the transitional provision under the CCC Amendment No.21, if the foregoing provision has been made during the period from the effective date of the CCC Amendment No.20 to the date prior to the effective date of CCC Amendment No.21, this provision shall be enforceable as it does not conflict with the CCC Amendment No.21.

(2) The provision of the Transitional Third Party Guarantee which is void during the period of the CCC amendment No.20 but is enforceable under the CCC Amendment No.21.

In the event that the guarantor, who is a juristic person, agrees to bind itself as the primary obligor to the Owner, this agreement is void under the CCC Amendment No.20,<sup>189</sup> but enforceable under the CCC Amendment No.21.<sup>190</sup>

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<sup>186</sup> Section 8 of the CCC Amendment No.21

<sup>187</sup> Section 700 paragraph 2 to the CCC that was amended by the CCC Amendment No.20.

<sup>188</sup> Section 700 paragraph 3 to the CCC that was amended by the CCC Amendment No.21.

<sup>189</sup> Section 681/1 paragraph 1 to the CCC that was amended by the CCC Amendment No.20.

<sup>190</sup> Section 681/1 paragraph 2 to the CCC that was amended by the CCC Amendment No.21.

Under the transitional provision of the CCC Amendment No.21, this agreement does not conflict with the relevant principle under the CCC Amendment No.21. However, it is questionable how a nullified agreement can become enforceable again. This question may not be answered until the Supreme Court has decided on this issue. In the meantime, in order to avoid this issue, the Owner can request the Contractor to replace the Third Party Guarantee made during the transitional period with a new Third Party Guarantee which is made after the effective date of the CCC Amendment No.21.

#### **4.3. Mitigation of the Effect of the Amendment of Principle of Suretyship under the CCC to the Third Party Guarantee by Using the Third Party Guarantee under the ISP 98, and the Convention**

After considering the effect of the amendment of principle of suretyship under the CCC to the Third Party Guarantee under the construction contract for large projects, as described in Topic 4.2, together with the comparison of the Third Party Guarantee governed by the CCC, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention, as described in Topic 3.3.1, it can be seen that the use of the standby letter of credit and the Undertaking can mitigate the significant effects on the Third Party Guarantee governed by the CCC, as amended, as follows:

##### **(1) Joint Liability of Guarantor**

Even if the amended principle of suretyship allows the guarantor to be jointly liable with the Contractor, such guarantor must be a juristic person. To the extent that the guarantor to the Third Party Guarantee is an individual person, such guarantor cannot agree to be jointly liable with the Contractor.

However, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention do not prohibit the guarantor or issuer to be jointly liable with the Contractor. Therefore, such guarantor or issuer can agree to be jointly liable with the Contractor without any conditions.

##### **(2) Extension of Time**

The amended principle of suretyship prohibits a guarantor the Third Party Guarantee from giving advance consent on the extension of time of secured obligation to the Owner, unless such guarantor is a financial institution or a person who undertakes the suretyship business for the remuneration.

However, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention do not bar the guarantor or issuer from giving such advance consent concerning to the Owner. Under the standby letter of credit and the Undertaking, the guarantor or issuer can agree to give advance consent to the Contractor without any conditions, even if the guarantor is not a financial institution or a person who undertake the suretyship business with remuneration as usual.

Hence, the use of standby letter of credit and the Undertaking can mitigate this consequence from the amended principle of suretyship under the CCC.

### (3) Default of the Contractor

Under the amended principle of suretyship, when the Contractor is in default, the Owner shall notify such default to all guarantors to the Third Party Guarantees within sixty days from the default date. If the Owner fails to notify such default, the guarantor shall be discharged from the interest and reimbursement which is incurred after said period, together with the other effects as described in Topic 4.2.4. This is one of the significant impacts which undermines to the suitability of the use of Third Party Guarantee governed by the amended principle of suretyship, under the construction contract for large projects.

However, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention do not require the Owner to notify such default. Hence, the use of such both of Third Party Guarantees covered by the ISP 98 and the Convention does not create more onerous duty concerning the notification of the Contractor's default nor cause the guarantor or issuer discharged by such duty.

Thus, the use of standby letter of credit and the undertaking can lessen this substantial effect from the amended principle of suretyship under the CCC.

### (4) Reduction of the Debt for the Contractor

Under the amended principle of suretyship, when the Owner agrees to reduce the secured amount to the Contractor, the Owner shall notify such reduction to all guarantors to the Third Party Guarantees, and such guarantors shall be subject



the newly agreed amount between the Owner and the Contractor, together with the other effect as described in Topic 4.2.5.

However, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention do not impose duty on the Owner to notify such reduction. Consequently, the use of such both of Third Party Guarantees covered by the ISP 98 and the Convention does not create any duty concerning the notification of the reduction of secured amount nor allow the guarantor or issuer to benefit from such reduction.

By using the standby letter of credit and the Undertaking, it can help reducing the undesirable outcome created by the amended principle of suretyship under the CCC.

In sum, the use of the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention can mitigate most of the effects stemmed from the amended principle of suretyship under the CCC relating to the Third Party Guarantee under the construction contract. However, the use of the standby letter of credit covered the ISP 98 and the Undertaking covered by the Convention under Thai laws may cause issues concerning the application of the both Third Party Guarantees by Thai Court, as described in Topic 3.1.2(6) and Topic 3.2.2(7). This problem is yet to be unraveled by the decision from the Supreme Court of Thailand.

## **CHAPTER 5**

### **CONCLUSIONS AND RECOMMENDATIONS**

#### **5.1 Conclusions**

Construction work for large projects requires progressive technology and skilled workmanship. The Contractor who can provide construction service for project of such scale is usually a large construction company equipped with high technology, trained personnel and available cash flow. Most of them are in fact international companies, or public companies, including Joint Ventures or Consortiums. In the course of business, they are well familiar with a guarantee from any third party (“Third Party Guarantee”) under international laws and practices, for instance, the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention.

The comparison between the Third Party Guarantee which is governed by ordinary principle of suretyship under the CCC and the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention reveals that there is hardly any material difference between using Third Party Guarantee under ordinary principle of suretyship of the CCC and independent guarantee and standby letter of credit under the international laws and practices.

In addition, the essential impacts caused by the amendments of CCC can be mitigated by the use of the standby letter of credit covered by the ISP 98 and the undertaking covered by the Convention. Nevertheless, the use of the standby letter of credit covered by the ISP 98 and the undertaking covered by the Convention itself also causes some issues as there have been no precedent decisions from the Supreme Court.

To summarize, the significant effects from the amendment of principle of suretyship to the construction contract for large projects are:

(1) The Owner has a duty to notify the guarantor to the Third Party Guarantee in the event that the Contractor is in the breach of the construction contract within sixty days from the default date. This is troublesome for the Owner because

(i) the period of sixty days from the default date, sometimes, may not enough. As it is rather difficult to consider whether there is any event of default by the Contractor under the construction contract for large projects, which require both engineering and legal knowledge to consider this issue, (ii) the amended principle of suretyship does not provide any detail on the commencement of the period of sixty day. Whether, when, the period of sixty days starts, either on actual default date or on default date, as agreed by the Owner and the Contractor, and (iii) the exact amount of the liquidated damages for delay. The amended principle of suretyship does not expressly specify whether or not the Owner has to notify the guarantor the exact amount of liquidated damages for delay again once the delayed work is completed; and

(2) To the extent that the Owner agrees to reduce or waive the underlying amount to the Contractor, the Owner must notify arrangement to all guarantors within sixty days from the date of the agreement. An arrangement on the waiver or reduction of the liquidated damages is not made due to mere kindness of the Owner. Instead, it is initiated because it is more beneficial to the Owner and the Contractor, or because it is easier for the Owner to manage the construction project, or because the Owner has actually contributed in causing the default by the Contractor. As a result, the Owner and the Contractor may not wish to notify this agreement to any third party.

Nevertheless, both effects can be mitigated by the use of the standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention as they do not give the foregoing rights to the guarantor or issuer or create the foregoing duty to the Owner. However, the application mechanism is still uncertain.

The standby letter of credit covered by the ISP 98 is only an international rule of practice, not international law. The ISP 98 therefore binds the party to the standby letter of credit as the provision of contract, not as binding international law. Thus, if Thai Court considers that some provision of the ISP 98 is contrary to the public order or good morals, such provision shall be void.<sup>191</sup>

Meanwhile, the application of the Undertaking under the Convention shall be allowed only when the place of business of the guarantor or issuer of the Underlying is in the Contracting State and the Undertaking shall be used solely in

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<sup>191</sup> Section 150 of the CCC.

international transactions where any two of the guarantor/issuer, the Contractor or the Owner are in different states.

The brief summary of the comparison of the Third Party Guarantee under the amended principle of suretyship, the ISP98 and the Convention is shown in the Appendix C Table: Comparison of the use of the Third Party Guarantee governed by the Amendment Principle of Suretyship under the CCC, the standby letter of credit covered by the ISP98 and the undertaking covered by the Convention.

Hence, if the Owner and the Contractor wish to use the standby letters of credit cover by the ISP 98 or the independent guarantees or the stand-by letters of credit covered by the Convention to mitigate the effect from the amendment of the principle of guarantee to the Third Party Guarantee under the construction contract for large projects, the Owner and the Contractor shall take the foregoing issues into account and apply suitable Third Party Guarantee covered by the ISP 98 or the Convention for their situation.

## **5.2 Recommendations**

The amendment of the principle of suretyship is intended to protect the surety, who is an ordinary person and has less bargaining power than the creditor. Meanwhile, the purpose of the Third Party Guarantee is to be an additional security to the Contractor, as debtor. However, most of the time, the guarantor to the Third Party Guarantee is a commercial bank or the financial institution, who has as much the bargaining power as the Owner, as creditor. Therefore, the application of the amendment to the principle of suretyship under the CCC to the Third Party Guarantee under the construction contract for large projects may be inappropriate.

Third Party Guarantee is widely used in the construction business. Because there are many ongoing problems relating to the Third Party Guarantee, it is quite common to use standby letter of credit covered by the ISP 98 and the Undertaking covered by the Convention to mitigate the effects from the amendment of principle of suretyship under the CCC. This however is an indirect solution. It is advisable that Thailand should enact the law concerning independent guarantee and standby letter of credit to address this issue.

The draft new law concerning independent guarantee and standby letter of credit should consist of the legal principles which are accepted internationally and should be designed to avoid the same consequence occurred from the amended principle of suretyship under the Thai Civil and Commercial Code. In this regard, the following principles of the standby letter of credit covered by the ISP 98 and the independent guarantee and stand-by letter of credit covered by the Convention shall be taken into consideration:

1. The draft new law shall be applied to both domestic and international use of independent guarantee and standby letter of credit.

2. The independent guarantee and standby letter of credit under the draft new law shall be an irrevocable, independent, documentary, and binding the secured transaction when issued.

3. The guarantor under the independent guarantee and the issuer under the standby letter of credit can agree to be joint liable with the principal or the applicant without any prohibitions.

4. The guarantor under the independent guarantee and the issuer under the standby letter of credit can give advance consent concerning the time extension of secured transaction to the beneficiary without any prohibitions.

5. The beneficiary shall not be requested to notify any defaults of the principal under the independent guarantee or the applicant under the standby letter of credit to the guarantor or the issuer.

6. The beneficiary shall not be requested to notify the agreement concerning the reduction of the amount of secured transaction with the principal under the independent guarantee or the applicant under the standby letter of credit to the guarantor or the issuer.

However, due to this thesis merely focuses on the impact of the amended principle of suretyship under the Civil and Commercial Code on the guarantee from any third party under the Construction Contract, the new law must take the impacts of the amended principle of suretyship on others businesses, such as, financial business and transactions, for instance, project finance, syndicated loans, or loan agreements, into consideration.

For the future study, the in-depth study relating to the application of the independent guarantee or stand-by letter of credit covered by the Convention, the ISP 98 and/or the URDG 758 under the Thai Law and by the Thai Court are recommended, together with the analysis of the impacts of the amended principle of suretyship under the Civil and Commercial Code on others businesses or transactions.



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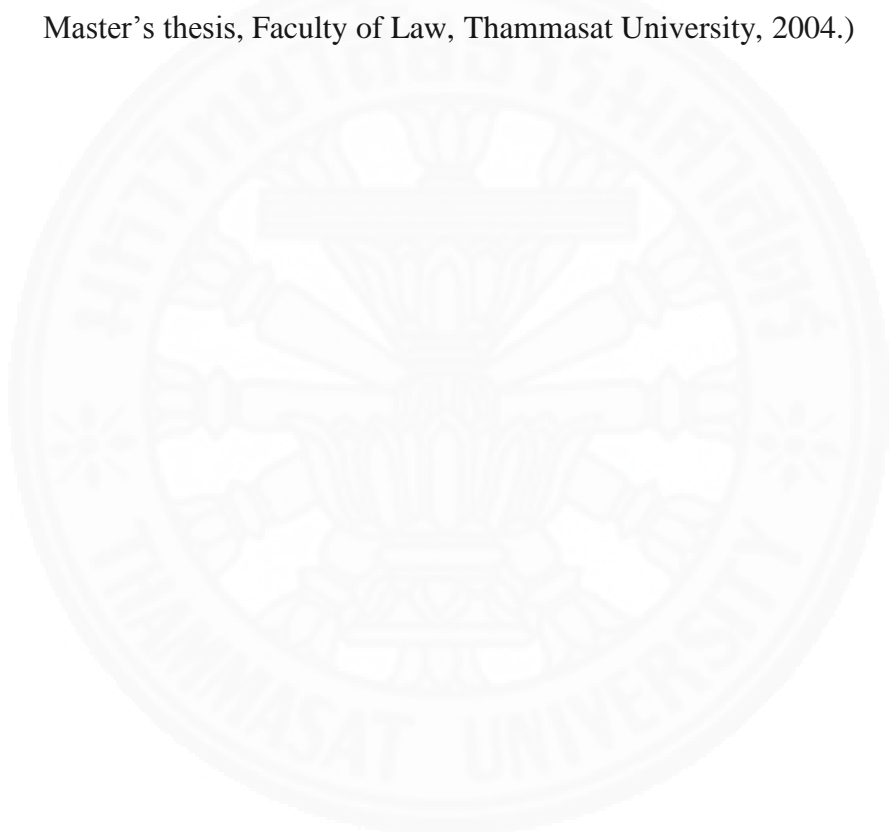
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**APPENDICES**

**APPENDIX A**  
**FORM OF SECURITY UNDER THE FIDIC RED BOOK**



## Annex A      **EXAMPLE FORM OF PARENT COMPANY GUARANTEE**

Brief description of Contract \_\_\_\_\_

Name and address of Employer \_\_\_\_\_

\_\_\_\_\_ (together with successors and assigns).

We have been informed that \_\_\_\_\_ (hereinafter called the "Contractor") is submitting an offer for such Contract in response to your invitation, and that the conditions of your invitation require his offer to be supported by a parent company guarantee.

In consideration of you, the Employer, awarding the Contract to the Contractor, we (*name of parent company*) \_\_\_\_\_ irrevocably and unconditionally guarantee to you, as a primary obligation, the due performance of all the Contractor's obligations and liabilities under the Contract, including the Contractor's compliance with all its terms and conditions according to their true intent and meaning.

If the Contractor fails to so perform his obligations and liabilities and comply with the Contract, we will indemnify the Employer against and from all damages, losses and expenses (including legal fees and expenses) which arise from any such failure for which the Contractor is liable to the Employer under the Contract.

This guarantee shall come into full force and effect when the Contract comes into full force and effect. If the Contract does not come into full force and effect within a year of the date of this guarantee, or if you demonstrate that you do not intend to enter into the Contract with the Contractor, this guarantee shall be void and ineffective. This guarantee shall continue in full force and effect until all the Contractor's obligations and liabilities under the Contract have been discharged, when this guarantee shall expire and shall be returned to us, and our liability hereunder shall be discharged absolutely.

This guarantee shall apply and be supplemental to the Contract as amended or varied by the Employer and the Contractor from time to time. We hereby authorise them to agree any such amendment or variation, the due performance of which and compliance with which by the Contractor are likewise guaranteed hereunder. Our obligations and liabilities under this guarantee shall not be discharged by any allowance of time or other indulgence whatsoever by the Employer to the Contractor, or by any variation or suspension of the works to be executed under the Contract, or by any amendments to the Contract or to the constitution of the Contractor or the Employer, or by any other matters, whether with or without our knowledge or consent.

This guarantee shall be governed by the law of the same country (or other jurisdiction) as that which governs the Contract and any dispute under this guarantee shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with such Rules. We confirm that the benefit of this guarantee may be assigned subject only to the provisions for assignment of the Contract.

Date \_\_\_\_\_ Signature(s) \_\_\_\_\_

## Annex D EXAMPLE FORM OF PERFORMANCE SECURITY - SURETY BOND

Brief description of Contract \_\_\_\_\_

Name and address of Beneficiary \_\_\_\_\_

\_\_\_\_\_ (together with successors and assigns, all as defined in the Contract as the Employer).

By this Bond, (*name and address of contractor*) \_\_\_\_\_  
(who is the contractor under such Contract) as Principal and (*name and address of guarantor*) \_\_\_\_\_  
as Guarantor are irrevocably held and firmly bound to the Beneficiary in the total amount of \_\_\_\_\_ (the "Bond Amount", say: \_\_\_\_\_ ) for the due performance of all such Principal's obligations and liabilities under the Contract. [Such Bond Amount shall be reduced by \_\_\_\_\_ % upon the issue of the taking-over certificate for the whole of the works under clause 10 of the conditions of the Contract.](<sup>1</sup>)

This Bond shall become effective on the Commencement Date defined in the Contract.

Upon Default by the Principal to perform any Contractual Obligation, or upon the occurrence of any of the events and circumstances listed in sub-clause 15.2 of the conditions of the Contract, the Guarantor shall satisfy and discharge the damages sustained by the Beneficiary due to such Default, event or circumstances.<sup>(2)</sup> However, the total liability of the Guarantor shall not exceed the Bond Amount.

The obligations and liabilities of the Guarantor shall not be discharged by any allowance of time or other indulgence whatsoever by the Beneficiary to the Principal, or by any variation or suspension of the works to be executed under the Contract, or by any amendments to the Contract or to the constitution of the Principal or the Beneficiary, or by any other matters, whether with or without the knowledge or consent of the Guarantor.

Any claim under this Bond must be received by the Guarantor on or before (*the date six months after the expected expiry of the Defects Notification Period for the Works*) \_\_\_\_\_ (the "Expiry Date"), when this Bond shall expire and shall be returned to the Guarantor.

The benefit of this Bond may be assigned subject to the provisions for assignment of the Contract, and subject to the receipt by the Guarantor of evidence of full compliance with such provisions.

This Bond shall be governed by the law of the same country (or other jurisdiction) as that which governs the Contract. This Bond incorporates and shall be subject to the Uniform Rules for Contract Bonds, published as number 524 by the International Chamber of Commerce, and words used in this Bond shall bear the meanings set out in such Rules.

Wherefore this Bond has been issued by the Principal and the Guarantor on (*date*) \_\_\_\_\_

Signature(s) for and on behalf of the Principal \_\_\_\_\_

Signature(s) for and on behalf of the Guarantor \_\_\_\_\_

<sup>(1)</sup> *When writing the tender documents, the writer should ascertain whether to include the optional text, shown in parentheses [ ]*

<sup>(2)</sup> *Insert:* [and shall not be entitled to perform the Principal's obligations under the Contract.]

*Or:* [or at the option of the Guarantor (to be exercised in writing within 42 days of receiving the claim specifying such Default) perform the Principal's obligations under the Contract.]

## Annex E      EXAMPLE FORM OF ADVANCE PAYMENT GUARANTEE

Brief description of Contract \_\_\_\_\_

Name and address of Beneficiary \_\_\_\_\_

\_\_\_\_\_ (whom the Contract defines as the Employer).

We have been informed that \_\_\_\_\_ (hereinafter called the "Principal") is your contractor under such Contract and wishes to receive an advance payment, for which the Contract requires him to obtain a guarantee.

At the request of the Principal, we (*name of bank*) \_\_\_\_\_ hereby irrevocably undertake to pay you, the Beneficiary/Employer, any sum or sums not exceeding in total the amount of \_\_\_\_\_ (the "guaranteed amount", say: \_\_\_\_\_ ) upon receipt by us of your demand in writing and your written statement stating:

- (a) that the Principal has failed to repay the advance payment in accordance with the conditions of the Contract, and
- (b) the amount which the Principal has failed to repay.

This guarantee shall become effective upon receipt [of the first instalment] of the advance payment by the Principal. Such guaranteed amount shall be reduced by the amounts of the advance payment repaid to you, as evidenced by your notices issued under sub-clause 14.6 of the conditions of the Contract. Following receipt (from the Principal) of a copy of each purported notice, we shall promptly notify you of the revised guaranteed amount accordingly.

Any demand for payment must contain your signature(s) which must be authenticated by your bankers or by a notary public. The authenticated demand and statement must be received by us at this office on or before (*the date 70 days after the expected expiry of the Time for Completion*) \_\_\_\_\_ (the "expiry date"), when this guarantee shall expire and shall be returned to us.

We have been informed that the Beneficiary may require the Principal to extend this guarantee if the advance payment has not been repaid by the date 28 days prior to such expiry date. We undertake to pay you such guaranteed amount upon receipt by us, within such period of 28 days, of your demand in writing and your written statement that the advance payment has not been repaid and that this guarantee has not been extended.

This guarantee shall be governed by the laws of \_\_\_\_\_ and shall be subject to the Uniform Rules for Demand Guarantees, published as number 458 by the International Chamber of Commerce, except as stated above.

Date \_\_\_\_\_ Signature(s) \_\_\_\_\_



## Annex F      EXAMPLE FORM OF RETENTION MONEY GUARANTEE

Brief description of Contract \_\_\_\_\_

Name and address of Beneficiary \_\_\_\_\_

\_\_\_\_\_ (whom the Contract defines as the Employer).

We have been informed that \_\_\_\_\_ (hereinafter called the "Principal") is your contractor under such Contract and wishes to receive early payment of [part of] the retention money, for which the Contract requires him to obtain a guarantee.

At the request of the Principal, we (*name of bank*) \_\_\_\_\_ hereby irrevocably undertake to pay you, the Beneficiary/Employer, any sum or sums not exceeding in total the amount of \_\_\_\_\_ (the "guaranteed amount", say: \_\_\_\_\_ ) upon receipt by us of your demand in writing and your written statement stating:

- (a) that the Principal has failed to carry out his obligation(s) to rectify certain defect(s) for which he is responsible under the Contract, and
- (b) the nature of such defect(s).

At any time, our liability under this guarantee shall not exceed the total amount of retention money released to the Principal by you, as evidenced by your notices issued under sub-clause 14.6 of the conditions of the Contract with a copy being passed to us.

Any demand for payment must contain your signature(s) which must be authenticated by your bankers or by a notary public. The authenticated demand and statement must be received by us at this office on or before (*the date 70 days after the expected expiry of the Defects Notification Period for the Works*) \_\_\_\_\_ (the "expiry date"), when this guarantee shall expire and shall be returned to us.

We have been informed that the Beneficiary may require the Principal to extend this guarantee if the performance certificate under the Contract has not been issued by the date 28 days prior to such expiry date. We undertake to pay you such guaranteed amount upon receipt by us, within such period of 28 days, of your demand in writing and your written statement that the performance certificate has not been issued, for reasons attributable to the Principal, and that this guarantee has not been extended.

This guarantee shall be governed by the laws of \_\_\_\_\_ and shall be subject to the Uniform Rules for Demand Guarantees, published as number 458 by the International Chamber of Commerce, except as stated above.

Date \_\_\_\_\_ Signature(s) \_\_\_\_\_

**APPENDIX B**  
**FORM OF SECURITY UNDER THE FIDIC YELLOW BOOK**



## Annex A      EXAMPLE FORM OF PARENT COMPANY GUARANTEE

Brief description of Contract \_\_\_\_\_

Name and address of Employer \_\_\_\_\_

\_\_\_\_\_ (together with successors and assigns).

We have been informed that \_\_\_\_\_ (hereinafter called the "Contractor") is submitting an offer for such Contract in response to your invitation, and that the conditions of your invitation require his offer to be supported by a parent company guarantee.

In consideration of you, the Employer, awarding the Contract to the Contractor, we (name of parent company) \_\_\_\_\_ irrevocably and unconditionally guarantee to you, as a primary obligation, the due performance of all the Contractor's obligations and liabilities under the Contract, including the Contractor's compliance with all its terms and conditions according to their true intent and meaning.

If the Contractor fails to so perform his obligations and liabilities and comply with the Contract, we will indemnify the Employer against and from all damages, losses and expenses (including legal fees and expenses) which arise from any such failure for which the Contractor is liable to the Employer under the Contract.

This guarantee shall come into full force and effect when the Contract comes into full force and effect. If the Contract does not come into full force and effect within a year of the date of this guarantee, or if you demonstrate that you do not intend to enter into the Contract with the Contractor, this guarantee shall be void and ineffective. This guarantee shall continue in full force and effect until all the Contractor's obligations and liabilities under the Contract have been discharged, when this guarantee shall expire and shall be returned to us, and our liability hereunder shall be discharged absolutely.

This guarantee shall apply and be supplemental to the Contract as amended or varied by the Employer and the Contractor from time to time. We hereby authorise them to agree any such amendment or variation, the due performance of which and compliance with which by the Contractor are likewise guaranteed hereunder. Our obligations and liabilities under this guarantee shall not be discharged by any allowance of time or other indulgence whatsoever by the Employer to the Contractor, or by any variation or suspension of the works to be executed under the Contract, or by any amendments to the Contract or to the constitution of the Contractor or the Employer, or by any other matters, whether with or without our knowledge or consent.

This guarantee shall be governed by the law of the same country (or other jurisdiction) as that which governs the Contract and any dispute under this guarantee shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with such Rules. We confirm that the benefit of this guarantee may be assigned subject only to the provisions for assignment of the Contract.

Date \_\_\_\_\_ Signature(s) \_\_\_\_\_

## Annex D EXAMPLE FORM OF PERFORMANCE SECURITY - SURETY BOND

Brief description of Contract \_\_\_\_\_

Name and address of Beneficiary \_\_\_\_\_

\_\_\_\_\_ (together with successors and assigns, all as defined in the Contract as the Employer).

By this Bond, (*name and address of contractor*) \_\_\_\_\_ (who is the contractor under such Contract) as Principal and (*name and address of guarantor*) \_\_\_\_\_ as Guarantor are irrevocably held and firmly bound to the Beneficiary in the total amount of \_\_\_\_\_ (the "Bond Amount", say: \_\_\_\_\_) for the due performance of all such Principal's obligations and liabilities under the Contract. [Such Bond Amount shall be reduced by \_\_\_\_\_ % upon the issue of the taking-over certificate for the whole of the works under clause 10 of the conditions of the Contract.](<sup>1</sup>)

This Bond shall become effective on the Commencement Date defined in the Contract.

Upon Default by the Principal to perform any Contractual Obligation, or upon the occurrence of any of the events and circumstances listed in sub-clause 15.2 of the conditions of the Contract, the Guarantor shall satisfy and discharge the damages sustained by the Beneficiary due to such Default, event or circumstances.<sup>(2)</sup> However, the total liability of the Guarantor shall not exceed the Bond Amount.

The obligations and liabilities of the Guarantor shall not be discharged by any allowance of time or other indulgence whatsoever by the Beneficiary to the Principal, or by any variation or suspension of the works to be executed under the Contract, or by any amendments to the Contract or to the constitution of the Principal or the Beneficiary, or by any other matters, whether with or without the knowledge or consent of the Guarantor.

Any claim under this Bond must be received by the Guarantor on or before (*the date six months after the expected expiry of the Defects Notification Period for the Works*) \_\_\_\_\_ (the "Expiry Date"), when this Bond shall expire and shall be returned to the Guarantor.

The benefit of this Bond may be assigned subject to the provisions for assignment of the Contract, and subject to the receipt by the Guarantor of evidence of full compliance with such provisions.

This Bond shall be governed by the law of the same country (or other jurisdiction) as that which governs the Contract. This Bond incorporates and shall be subject to the Uniform Rules for Contract Bonds, published as number 524 by the International Chamber of Commerce, and words used in this Bond shall bear the meanings set out in such Rules.

Wherefore this Bond has been issued by the Principal and the Guarantor on (*date*) \_\_\_\_\_

Signature(s) for and on behalf of the Principal \_\_\_\_\_

Signature(s) for and on behalf of the Guarantor \_\_\_\_\_

<sup>(1)</sup> *When writing the tender documents, the writer should ascertain whether to include the optional text, shown in parentheses [ ]*

<sup>(2)</sup> *Insert: [and shall not be entitled to perform the Principal's obligations under the Contract.]*

*Or: [or at the option of the Guarantor (to be exercised in writing within 42 days of receiving the claim specifying such Default) perform the Principal's obligations under the Contract.]*

## Annex E      EXAMPLE FORM OF ADVANCE PAYMENT GUARANTEE

Brief description of Contract \_\_\_\_\_

Name and address of Beneficiary \_\_\_\_\_

\_\_\_\_\_ (whom the Contract defines as the Employer).

We have been informed that \_\_\_\_\_ (hereinafter called the "Principal") is your contractor under such Contract and wishes to receive an advance payment, for which the Contract requires him to obtain a guarantee.

At the request of the Principal, we (*name of bank*) \_\_\_\_\_ hereby irrevocably undertake to pay you, the Beneficiary/Employer, any sum or sums not exceeding in total the amount of \_\_\_\_\_ (the "guaranteed amount", say: \_\_\_\_\_) upon receipt by us of your demand in writing and your written statement stating:

- (a) that the Principal has failed to repay the advance payment in accordance with the conditions of the Contract, and
- (b) the amount which the Principal has failed to repay.

This guarantee shall become effective upon receipt [of the first instalment] of the advance payment by the Principal. Such guaranteed amount shall be reduced by the amounts of the advance payment repaid to you, as evidenced by your notices issued under sub-clause 14.6 of the conditions of the Contract. Following receipt (from the Principal) of a copy of each purported notice, we shall promptly notify you of the revised guaranteed amount accordingly.

Any demand for payment must contain your signature(s) which must be authenticated by your bankers or by a notary public. The authenticated demand and statement must be received by us at this office on or before (*the date 70 days after the expected expiry of the Time for Completion*) \_\_\_\_\_ (the "expiry date"), when this guarantee shall expire and shall be returned to us.

We have been informed that the Beneficiary may require the Principal to extend this guarantee if the advance payment has not been repaid by the date 28 days prior to such expiry date. We undertake to pay you such guaranteed amount upon receipt by us, within such period of 28 days, of your demand in writing and your written statement that the advance payment has not been repaid and that this guarantee has not been extended.

This guarantee shall be governed by the laws of \_\_\_\_\_ and shall be subject to the Uniform Rules for Demand Guarantees, published as number 458 by the International Chamber of Commerce, except as stated above.

Date \_\_\_\_\_ Signature(s) \_\_\_\_\_

## Annex F EXAMPLE FORM OF RETENTION MONEY GUARANTEE

Brief description of Contract \_\_\_\_\_

Name and address of Beneficiary \_\_\_\_\_

\_\_\_\_\_ (whom the Contract defines as the Employer).

We have been informed that \_\_\_\_\_ (hereinafter called the "Principal") is your contractor under such Contract and wishes to receive early payment of [part of] the retention money, for which the Contract requires him to obtain a guarantee.

At the request of the Principal, we (*name of bank*) \_\_\_\_\_ hereby irrevocably undertake to pay you, the Beneficiary/Employer, any sum or sums not exceeding in total the amount of \_\_\_\_\_ (the "guaranteed amount", say: \_\_\_\_\_) upon receipt by us of your demand in writing and your written statement stating:

- (a) that the Principal has failed to carry out his obligation(s) to rectify certain defect(s) for which he is responsible under the Contract, and
- (b) the nature of such defect(s).

At any time, our liability under this guarantee shall not exceed the total amount of retention money released to the Principal by you, as evidenced by your notices issued under sub-clause 14.6 of the conditions of the Contract with a copy being passed to us.

Any demand for payment must contain your signature(s) which must be authenticated by your bankers or by a notary public. The authenticated demand and statement must be received by us at this office on or before (*the date 70 days after the expected expiry of the Defects Notification Period for the Works*) \_\_\_\_\_, (the "expiry date"), when this guarantee shall expire and shall be returned to us.

We have been informed that the Beneficiary may require the Principal to extend this guarantee if the performance certificate under the Contract has not been issued by the date 28 days prior to such expiry date. We undertake to pay you such guaranteed amount upon receipt by us, within such period of 28 days, of your demand in writing and your written statement that the performance certificate has not been issued, for reasons attributable to the Principal, and that this guarantee has not been extended.

This guarantee shall be governed by the laws of \_\_\_\_\_ and shall be subject to the Uniform Rules for Demand Guarantees, published as number 458 by the International Chamber of Commerce, except as stated above.

Date \_\_\_\_\_ Signature(s) \_\_\_\_\_

**APPENDIX C**

**TABLE: COMPARISON OF THE USE OF THE THIRD PARTY  
GUARANTEE GOVERNED BY THE AMENDMENT PRINCIPLE  
OF SURETYSHIP UNDER THE CCC, THE STANDBY LETTER  
OF CREDIT COVERED BY THE ISP 98 AND THE  
UNDERTAKING COVERED BY THE CONVENTION**



**Table:** Comparison of the use of the Third Party Guarantee governed by the amendment principle of suretyship under the CCC, the standby letter of credit covered by the ISP 98 and the undertaking covered by the Convention

<b>Issues</b>	<b>The amended principle of suretyship</b>	<b>ISP 98</b>	<b>Convention</b>
Joint Liability of Guarantor	The guarantor, who is a juristic person, can be jointly liable with the Contractor.	The standby letter of credit is not prohibited the issuer to be jointly liable with the Contractor.	The undertaking is not prohibited the guarantor/issuer to be jointly liable with the Contractor.
Extension of Time	The guarantor, who is a financial institution or a person who undertake the suretyship business with the remuneration as usual, can give the advance consent concerning the extension of time.	The standby letter of credit is not prohibited the issuer to give the advance consent concerning the extension of time.	The undertaking is not prohibited the guarantor/issuer to give the advance consent concerning the extension of time.
Default of the Contractor	To the extent that the Contractor is in default, the Owner shall notify such default to all guarantors within sixty days from the default date.	The standby letter of credit is independent, so, the Owner is not required to notify such default to the issuer.	The undertaking is independent, so, the Owner is not required to notify such default to the guarantor/issuer.



<b>Issues</b>	<b>The amended principle of suretyship</b>	<b>ISP 98</b>	<b>Convention</b>
Reduction of the Debt for the Contractor	To the extent that the Owner agrees to reduce the secured amount with the Contractor, the Owner shall notify such agreement to all guarantors within sixty days from the date of this agreement.	The standby letter of credit is independent, so, the Owner is not required to notify such agreement to the issuer and the liability of issuer shall be remain unchanged by this agreement.	Due to the undertaking is independent, so, the Owner, is not required to notify such agreement to the issuer and the liability of guarantor/ issuer shall be remain unchanged by this agreement.
Application under the Thai Laws	No issue concerning the application of the amended principle under Thai Laws,	As refer to the previous Supreme Court Judgement, the application of ISP 98 is valid and enforceable under Thai Laws.	If the undertaking is international and the place of business of the guarantor/issuer is in the Contracting Stage, the Convention is enforceable.

## **BIOGRAPHY**

Name	Mr. Pakorn Sirinanthanon
Date of Birth	July 5, 1977
Educational Attainment	2015: LL.M. (Thammasat) 2007: Barrister-at-Law 2002: LL.B. (Thammasat) 1998: B.Eng. (Civil Engineering) (Mahanakorn Technology University)
Work Position	Senior Lawyer TOC Glycol Company Limited
Work Experiences	September 2006 – Present: Senior Lawyer TOC Glycol Company Limited December 2003 – September 2006: Legal Officer The Secretarial of the Senate September 2003 - December 2003: Civil Engineer Thai Nishimatsu Construction Company Limited