RESEARCH ARTICLE

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ISSUANCE OF INDEPENDENT GUARANTEES BY INSURANCE COMPANIES

SUMMARY

Independent, or demand, guarantees are strong security instruments. They are designed to secure the proper performance of contractual obligations in commercial transactions. In South Africa, independent guarantees are a common feature of construction projects where the interests of any of the main parties (that is, the contractor or the employer) may conceivably be secured. Essentially, independent guarantees constitute an undertaking by the issuer of the guarantee to pay a stipulated sum of money to the beneficiary of the guarantee upon the presentation of conforming documents. The question of payment is, therefore, to be determined with reference only to the documents, and not to facts outside of the documents. Consequently, payment under an independent guarantee is expected to be made expeditiously, provided conforming documents are tendered. It is clear, therefore, that the proper functioning of the independent guarantee requires the use of a strong and reliable financier. Internationally, banks can probably be regarded as the dominant issuers of independent guarantees. This much is apparent in international jurisprudence, specifically in case law and academic writing. In South Africa, however, banks do not enjoy that status, since the guarantee market is competitively shared between banks and insurance companies, the latter having recently emerged as equally coveted issuers of independent guarantees. This can be evidenced by the significant number of case law involving an insurance company as issuer, rather than a bank. This article focuses on this development in South African law. It seeks to analyse and ultimately provide a rationale for the increasing use of insurance companies in independent-guarantee transactions. The analysis reveals the following factors as the main contributors to this growing practice: the favourable security requirements of insurance companies, the significance of the premium attached to guarantee policies, and the increasing flexibility of insurance companies in the formulation of guarantees.

1. INTRODUCTION

Independent guarantees[1] are regularly encountered in commercial transactions such as construction contracts. These instruments are designed to secure the proper performance of contractual obligations.[2] Akin to letters of credit,[3] this security takes the form of an undertaking by the issuer of the guarantee[4] to pay a stipulated sum of money to the beneficiary of the guarantee upon the submission of conforming documents.[5] The proper functioning of the independent guarantee accordingly requires the use of a strong and reliable financier.

Internationally, banks can probably be regarded as the dominant issuers of independent guarantees.[6] This much is apparent in international jurisprudence[7] and is furthermore consistent with letter-of-credit practice.[8] In South Africa, however, banks do not enjoy that status, since the guarantee market is competitively shared between banks and insurance companies, the latter having recently emerged as equally coveted issuers of specifically independent guarantees. This can be demonstrated by the significant number

1 Also known as "demand guarantees", "unconditional guarantees", and "performance bonds". Independent guarantees are essentially the same as "standby letters of credit".

2 Kelly-Louw 2009:1; Hugo 2017:2-3.

3 The letter of credit, also known as a "documentary credit", is a mode of payment used in international sale transactions. Letters of credit and independent guarantees share a close relationship. See section 2 below.

4 Also referred to as the "guarantor".

5 Hewetson & Mitchell 2017:124, 164; Kelly-Louw 2017:111-112.

6 This statement should not be construed to mean that, internationally, banks are the only issuers of independent guarantees. Other financial institutions also issue these instruments – not to the extent that banks do.

7 See, in this regard, for example, the following case law emanating from England, Singapore and Australia. *Edward Owen Engineering Ltd v Barclays Bank International Ltd* 1978 QB 159 (CA); *GKN Contractors Ltd v Lloyds Bank Plc* 1985 30 Building LR 48; *Mahonia Ltd v JP Morgan Chase Bank* 2003 2 Lloyd's Rep 911; *Uzinterimpex JSC v Standard Bank Plc* 2007 EWHC 1151; *National Infrastructure Development Co Ltd v Banco Santander SA* 2016 EWHC 2990 (Comm); *National Infrastructure Development Co Ltd v PNB Paribas* 2016 2508 (Comm); *Lukoil Mid-East Ltd v Barclays Bank Plc* 2016 EWHC 166 (TCC); *Chartered Electronic Industries Pte Ltd v The Development Bank of Singapore Ltd* 1999 4 SLR 665; *CKR Contract Services Pte Ltd v Asplenium Land Pte Ltd* 2015 SGCA 24; *Bateman Project Engineering Pty Ltd v Resolute Ltd* 2000 23 WAR 493; *Cloud Engineering Ltd v Oil and Natural Gas Corporation Ltd* 2008 249 ALR 458. This also applies to academic writing where independent guarantees are sometimes referred to as "bank guarantees". See, for example, Mugasha 2003; Barru 2005; Kurkela 2007; Bertrams 2013.

8 Letters of credit are invariably issued by banks. To our knowledge, there have been no reported cases involving a letter of credit issued by a non-bank institution.

of case law involving an insurance company as issuer, rather than a bank.[9] This article focuses on this development in South African law. It seeks to analyse and ultimately provide a rationale for the increasing use of insurance companies in independent-guarantee transactions. Whereas scholars have investigated various aspects of independent guarantees over the years,[10] an analysis of this specific development has not, to our knowledge, been undertaken. It is, therefore, hoped that this article will prove useful to the guarantee community.

We begin with a discussion of the operation of independent guarantees. Thereafter, we explore the insurance legislative framework in South Africa, which contains provisions that are particularly relevant to independent guarantees in the context of this article. This sets the scene for an analysis of the abovementioned development in South African law, which is undertaken using primary and secondary documentary sources in an interpretative empirical methodology, including interviews with guarantee specialists and professionals.

2. OPERATION OF INDEPENDENT GUARANTEES

2.1 Preliminary remarks

Independent guarantees play an important role in commerce. In South Africa, as indicated earlier, these instruments are especially common in the construction industry where they are encountered in different forms and typically used by the employer to secure the proper performance of the contractor's obligations, or the contractor for the performance of the employer's payment obligations.[11] One would be hard-pressed to find any major construction transaction in which such a guarantee is not utilised. Likewise, letters of credit, as a payment method, play a crucial role in international contracts of sale. The necessity of having to invoke independent guarantees and letters of credit in

9 See, for example, *Lombard Insurance Co Ltd v Landmark Holdings (Pty) Ltd* 2010 2 SA 86 (SCA); *Compass Insurance Co Ltd v Hospitality Hotel Developments (Pty) Ltd* 2012 2 SA 537 (SCA); *Kristabel Developments (Pty) Ltd v Credit Guarantee Insurance Corporation of Africa Limited* [2015] ZAGPJHC 264 (20 October 2015); *University of the Western Cape v ABSA Insurance Company* [2015] ZAGPJHC 303 (28 October 2015); *Mutual and Federal Insurance Co Ltd v KNS Construction (Pty) Ltd* [2016] ZASCA 87 (31 May 2016); *Mattress House (Pty) Ltd t/a Mia Bella Interiors v Investec Property Fund Ltd* [2017] *ZAGPHC* 298 (13 October 2017); *Lombard Insurance Co Ltd v Schoeman* 2018 1 SA 240 (GJ); *Schoeman v Lombard Insurance Co Ltd* [2019] ZASCA 66 (29 May 2019); *Investec Bank Ltd v Lombard Insurance Co Ltd* [2019] ZAGPPHC 251 (26 June 2019); *Bombardier Africa Alliance Consortium v Lombard Insurance Company Limited & Another* [2020] *ZAGPPHC* 554 (7 October 2020); *SA National Roads Agency SOC Limited v Fountain Civil Engineering (Pty) Ltd* [2021] *ZASCA* 118 (20 September 2021).

10 Most notably, the defences to payment available to the issuer and/or applicant of the guarantee. There are several influential texts on this issue, including Kelly-Louw 2009; Horowitz 2010; Enonchong 2011; Marxen 2018. See further section 2.3 below.

11 See, generally, Hugo 2014.

commercial transactions has prompted the English judiciary to characterise these instruments as "the lifeblood of commerce".[12] Against this background, two points need to be made.

First, as indicated earlier, independent guarantees function similarly to letters of credit: the issuer must honour its payment undertaking upon the presentation of conforming documents. The fundamental legal principles of independent guarantees (namely, the independence principle and the doctrine of documentary compliance which are dealt with below) are also similar to those of letters of credit. Consequently, case law on the one instrument is generally used as authority for the other.

Secondly, South Africa has not enacted legislation to deal specifically with independent guarantees (or letters of credit). The absence of legislation means that the law of demand guarantees in South Africa is developed primarily through domestic case law, as supported by foreign, and especially English, case law and academic writing. It also paves the way for parties to contractually incorporate any of the available sets of rules to govern the guarantee, including the International Chamber of Commerce's (ICC) Uniform Rules for Demand Guarantees (URDG 758),[13] the ICC-endorsed International Standby Practices (ISP98),[14] and the United Nations Commission on International Trade Law's (UNCITRAL) United Nations Convention on Independent Guarantees and Stand-by Letters of Credit (UNCITRAL Convention).[15] Yet, none of these rules enjoy strong usage in South Africa.

In the South African construction industry, uniformity is achieved through the widespread use of the standardised guarantees of the Joint Building Contracts Committee (JBCC) suite of agreements[16] and the General Conditions of Contract for Construction Works (GCC) of the South African Institution of Civil Engineering.[17] The standardised guarantees of the New Engineering Contract and the *Fédération Internationale des Ingénieurs-Conseil*,[18] are also gaining momentum in South Africa.

12 *RD Harbottle (Mercantile) Ltd v National Westminster Bank Ltd* 1977 2 All ER 862 (QB) 870b. The phrase was repeated in *Edward Owen Engineering Ltd v Barclays Bank International Ltd* 1978 1 All ER 976 (CA) 983; *Intraco Ltd v Notis Shipping Corporation* (*the* Bhoja Trader) 1981 2 Lloyd's Rep 256 (CA) 257. In South Africa, the phrase was cited authoritatively in *Ex parte Sapan Trading (Pty) Ltd* 1995 1 SA 218 (W) 224H; *Loomcraft Fabrics CC v Landmark Holdings (Pty) Ltd* 1996 1 SA 812 (A) 817E-F.

13 ICC publication 758 (2010).

14 ICC publication 590 (1998).

15 This convention was adopted by the General Assembly in 1995 and became effective on 1 January 2000 in those countries that adopted the convention, namely Belarus, Ecuador, El Salvador, Gabon, Kuwait, Liberia, Panama, and Tunisia.

16 For a detailed treatise on JBCC contracts and guarantees, see Segal 2018.

17 See South African Institution of Civil Engineering 2015.

18 The English translation is "International Federation of Consulting Engineers".

2.2 The guarantee process in basic perspectives

The need for a guarantee will be apparent from the underlying contract (for example, a construction contract), as it will stipulate that a certain performance must be secured by way of a guarantee. The applicant (for example, the contractor in the construction contract) will procure the issuance of a guarantee in favour of the beneficiary (the employer in the construction contract). This entails an application form for the issuance of the guarantee at the issuer of its choice: typically, a bank or insurance company. The application form will contain all the main details of the guarantee, including the type of guarantee, the guarantee value, the dates of issuance and expiry of the guarantee, and any special instructions such as the circumstances under which the guarantee may be called up and the specific documents that must be presented for payment.[19] The issuer will, on the basis of the information provided in the application form, determine the creditworthiness of the applicant[20] and conduct any other relevant assessments.[21] Depending on the nature of the chosen issuer (*i.e.*, bank or insurance company), the outcome of the creditworthiness assessment and other important factors such as the guarantee amount, the issuer may require some form of security from the applicant before accepting the application. The type of security required may also differ depending on the issuer. Cash deposits, collateral in the form of pledge agreements for assets, indemnities, suretyships, and notarial bonds are the main types of security encountered in guarantee practice.

If the application is accepted, this will be communicated to the applicant and, in turn, the beneficiary. The beneficiary is afforded an opportunity to review the terms and conditions of the guarantee.[22] If the stipulations of the guarantee deviate from the requirements of the underlying contract, the beneficiary must reject the guarantee and notify the other parties accordingly.[23] If the beneficiary is satisfied with the guarantee, performance in terms of the underlying contract will commence (in other words, the contractor will perform the construction works). It is important to emphasise the three contractual relationships at play: the underlying (construction) contract between the applicant (contractor) and the beneficiary (employer), the guarantee contract between the issuer and the beneficiary, and the contract of mandate between the applicant and the issuer (by virtue of the guarantee application). These contracts are independent of one another. The implication is that circumstances emanating from the one do not, in principle, affect performance in terms of the other.[24]

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19 See, for example, the application form of Lombard Insurance “Lombard construction guarantee – guarantee application”, https://www.lombardins.com/guarantees/construction-guarantees/ (accessed on 27 January 2023).

20 Bertrams 2013:par. 2.3.7.

21 For example, an assessment of the risk of money laundering and terrorist financing. See, in this regard, Spruyt 2020.

22 In practice, however, beneficiaries sometimes insist on using their own in-house guarantees. See section 4.3 below.

23 Enonchong 2011:43.

24 See section 2.3 below.

Should the circumstances contemplated in the guarantee be triggered during the currency of the guarantee, the beneficiary may demand payment by presenting the stipulated documents to the issuer. If the requirements of the guarantee are met, that is, if the documents presented are in conformity with the requirements of the guarantee, the issuer must pay in accordance with the guarantee and seek reimbursement from the applicant.[25]

2.3 Legal principles: Documentary compliance and independence

As alluded to earlier, the requirements under independent guarantees are almost always documentary in nature.[26] This means that, for the beneficiary to be entitled to payment, it must present certain stipulated documents to the issuer who will, in turn, examine those documents to determine their conformity. This is known as the doctrine of documentary compliance. Case law on the standard of compliance in this regard, however, is unclear.[27] The essential point is that a strict standard of conformity will ensure the retention of independent guarantees' reputation as strong security instruments. Too strict a standard, however, will result in a high number of rejections of documents, thereby restricting the usefulness of these instruments.[28] The better approach, as suggested by Chivizhe, is to give effect to the purpose of the instrument in determining conformity.[29] A purposive approach is likely to ensure an outcome that promotes the utility of these instruments as well as legal certainty.

A further principle of demand guarantees in South African law is the independence or autonomy principle. In terms of this principle, the question of payment is to be determined with reference solely to the documents, and not to facts outside of the documents.[30] This means that disputes relating to the underlying contract are irrelevant for the purposes of the issuer's liability in terms of the guarantee. By virtue of the "pay-first-argue-later"[31] effect of this principle, the beneficiary can rest assured that it will receive payment shortly after presenting conforming documents.

The independence principle is the distinguishing factor between independent guarantees and accessory guarantees. Accessory guarantees[32] also provide a security function, whereby the issuer undertakes to pay a sum of money to the beneficiary of the guarantee. The difference, however, is that the liability of the issuer under an accessory guarantee is determined with reference to the debtor's default in law of its obligations towards the creditor

25 Enonchong 2011:294.

26 There is, however, a growing practice of including so-called sanctions clauses in independent guarantees and letters of credit. Sanctions clauses that refer to internal sanctions policies or a "discretion" of the issuer constitute non-documentary conditions. On this growing practice, see Lupton 2022.

27 A detailed discussion of this issue is beyond the scope of this article. For a comprehensive treatise, see Chivizhe 2021.

28 Chivizhe 2021:291.

29 Chivizhe 2021:291.

30 Kelly-Louw 2009:41-48; Hugo 2016:445-446; Mugasha 2003:24-25.

31 Bertrams 2013:73.

32 Also referred to as "conditional bonds (or guarantees)".

(beneficiary).[33] This means that the issuer may, as in the case of suretyship, raise any defence to the beneficiary's claim that would have been available to the debtor whose performance is secured by the guarantee.[34] Whereas, under an independent guarantee, the independence principle entitles the beneficiary to payment upon the mere submission of conforming documents, irrespective of disputes arising from the underlying contract. Consequently, accessory guarantees provide significantly less security to the beneficiary than independent guarantees.[35]

Bearing in mind that independent guarantees are susceptible to abuse by beneficiaries,[36] it is, on the basis of public policy, inappropriate for the independence principle to exist without exception. Against this background, fraud has been raised frequently in the South African courts as a basis to resist a claim for payment under an independent guarantee. In this context, fraud refers to forgery or falsification of the documents and to fraudulent conduct of the beneficiary relating to the underlying contract. In the latter regard, knowledge of the beneficiary to its lack of entitlement is central to the question of fraud.[37] Currently, fraud is the only clearly recognised exception to the independence principle in South African law,[38] although illegality has emerged tentatively in this regard.[39]

3. THE ROLE OF THE INSURANCE LEGISLATIVE FRAMEWORK IN THE ISSUANCE OF GUARANTEE POLICIES

3.1 An overview of the South African insurance legislative framework

As far as the regulation of the South African insurance industry is concerned, it is worth noting that there have been significant changes to the regulatory framework over the past five years. The "improved" regulatory framework under the Twin Peaks model was introduced to support broader objectives in the

33 See *Minister of Transport and Public Works, Western Cape v Zanbuild Construction (Pty) Ltd* 2011 5 SA 528 (SCA):par. 13.

34 See Forsyth & Pretorius 2010:28-29.

35 For a detailed discussion of the diverging nature of independent and accessory guarantees, see Kelly-Louw 2017.

36 Hugo 2016:449-450.

37 The Supreme Court of Appeal in *Guardrisk Insurance Company Ltd v Kentz (Pty) Ltd* 2014 1 All SA 307 (SCA):par. 17 put it thus: "It is trite that where a beneficiary who makes a call on a guarantee does so with knowledge that it is not entitled to payment, our courts will step in to protect the bank and decline enforcement of the guarantee in question."

38 For case law in which fraud was successfully relied upon, see *Group Five Construction (Pty) Ltd v Member of the Executive Council Public Transport Roads and Works Gauteng* 2015 5 SA 26 (GJ); *Phenix Construction Technology Ltd v Hollard Insurance Company Ltd* 2017 [2017] *ZAGPJHC* 174 (4 May 2017).

39 With reference to *Mattress House (Pty) Ltd t/a Mia Bella Interiors v Investec Property Fund Ltd*, see Lupton & Kelly-Louw 2020.

financial sector.[40] The Twin Peaks regulatory system was signed into law on 21 August 2017. The *Financial Sector Regulation Act* (*FSRA*)[41] introduced a new system of financial regulation in South Africa. In terms of the previous regulatory framework, a number of regulatory authorities were responsible for the financial sector's regulation, each with substantially different powers and functions.[42] Under the previous system, the Registrar of Banks, which is part of the Bank Supervision Department within the Reserve Bank, is responsible for the prudential supervision of banks and for performing functions assigned to them in terms of the *Banks Act*.[43] Other institutions that played a critical role in the regulation of the financial services industry included the Financial Services Board (FSB) and the National Credit Regulator.[44]

The non-banking sector was previously overseen by the FSB.[45] The FSB was responsible for the prudential and market conduct supervision of all non-bank financial institutions, including insurance companies.[46] The FSB was structured to have a Registrar for each type of industry.[47] It is clear that FSB regulated and controlled both the insurance industry and the insurance brokers.[48]

The Twin Peaks model provides for the establishment of two regulators: one to maintain control of the stability of the financial market – prudential regulation, and the other responsible for ensuring consumer protection and market conduct.[49] The promulgation of the *FSRA* established the prudential authority (PA) as well as the financial services conduct authority (FSCA). Notably the role of the FSCA is to supervise the market conduct of financial services providers (including banks and insurers).

The FSCA is tasked with ensuring the fair treatment of financial consumers; enhancing efficiency and integrity of the financial system; providing financial consumers with financial education programmes and promoting financial literacy.[50] As far as the role of the PA is concerned, this was previously undertaken by the Reserve Bank. Nowadays, the power to oversee the financial soundness of financial service providers lies with the PA. The PA ensures that all financial institutions meet their obligations to consumers and assist in maintaining financial stability.[51] The Twin Peaks system is designed to make the financial sector safer and to better protect financial customers.[52]

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40 Nagel 2019:346.
41 *Financial Sector Regulation Act* 9/2017.
42 Millard 2016:4-5; Millard & Maholo 2016:597-598.
43 *Banks Act* 94/1990.
44 Millard 2016:22; Millard & Maholo 2016:598.
45 FSB was an independent body established in terms of the *Financial Services Board Act* 97/1990.
46 Millard & Hattingh 2016:6.
47 Millard & Hattingh 2016:6.
48 Millard 2016:22; Millard & Maholo 2016:598.
49 Millard 2016:22.
50 Nagel 2019:347.
51 Nagel 2019:347.
52 Millard 2016:2.

As part of ensuring the protection of financial customers (in this specific instance, policyholders procuring guarantee policies), the financial soundness of insurers is a critical issue to consider in terms of ensuring that insurers comply with the relevant solvency requirements. Of relevance, in this instance, is the Solvency Assessment and Management (SAM) regime.

SAM was first introduced in 2009, when the FSB and the insurance industry embarked on an approach to establish a risk-based supervisory regime for the prudential regulation of insurers.[53] SAM is modelled on the Solvency II capital adequacy, risk governance, and risk disclosure regime employed in Europe.[54] The regime employs three pillars. Pillar I deals with capital adequacy; Pillar II deals with systems of governance, and Pillar III deals with reporting requirements. Of key importance to the SAM regime is the protection of policyholders. SAM attempts to align capital requirements with the underlying risks of insurers. It also aims for the development of a proportionate, risk-based approach to supervision, with appropriate treatment for both small insurers and large, cross-border groups. Ultimately, SAM hopes to ensure financial stability.[55] Based on the key objectives of SAM, it is apparent that the implementation of the system will have several consequences for South African insurers. Most noteworthy in this regard is that the solvency and capital requirements, as prescribed under the SAM framework, will require of insurers to assess and determine whether they have appropriate risk-management systems and policies in place to meet the SAM requirements. In this instance, it is expected that insurers carry out so-called own risk and solvency assessments in accordance with prudential standard GOI 3.1. Insurers have a concomitant obligation to implement reporting systems that are consistent with the reporting requirements under SAM.[56] In the context of this article, the solvency requirements mean that, in the issuing of guarantee policies, insurers must ensure that they remain solvent and adhere to the SAM regime at all times.

Lastly, the 2017 *Insurance Act*[57] will deal with the prudential aspect of insurance, while market conduct supervision will continue to be dealt with in terms of the *Long-term Insurance Act*[58] (*LTIA*) and the *Short-term Insurance Act*[59] (*STIA*) (and their relevant *Policyholder Protection Rules*), until such

53 Nagel 2019:348.

54 Nagel 2019:348.

55 Nagel 2019:348.

56 Nagel 2019:348.

57 *Insurance Act* 9/2017. The aim of this *Act* is "to provide for a legal framework for the prudential supervision of insurance business in the Republic that is consistent, where relevant, with international standards for insurance regulation and supervision; to introduce a legal framework for micro-insurance to promote financial inclusion; to replace certain parts of the *Long-term Insurance Act, 1998, and the Short-term Insurance Act,* 1998; and to provide for matters connected therewith."

58 *Long-term Insurance Act* 52/1998.

59 *Short-term Insurance Act* 53/1998.

time that the *Conduct of Financial Institutions* (*CoFI*) Bill is enacted.[60] In accordance with phase two of Twin Peaks, all market conduct requirements will be centralised in the planned *CoFI Act*.[61]

3.2 The regulation of guarantee policies

In South Africa, the definition of a guarantee policy is generally fairly wide,[62] because it encompasses as the risk, a third person's failure "to discharge an obligation", in general.[63] Different forms of guarantee policies are recognised, depending on the precise nature of the third party's obligation. These include fidelity guarantee insurance, credit (or debit) guarantee insurance, and independent guarantees. It is important to note that there is a distinct difference between suretyship and insurance. It is possible that, in the instance of an insurer contractually undertaking, for remuneration, to pay a sum of money to the other party on the failure of a third person to perform an obligation, it may amount to being a contract of insurance or one of suretyship.[64] It will come down to the intention of the parties. If the intention was that the insurer, by performance of its own, principal obligation, indemnifies the other party (the insured) on the third party's non-performance, it will be insurance.[65] Suretyship will be the case where the intention was that, on the third party's non-performance, the insurer renders to the other party (the creditor) an accessory performance in the third-party debtor's place.[66]

It is necessary to consider the initial roots of guarantee policies in the South African insurance legislation. This starts with considering the concept from the 1943 *Insurance Act*.[67]

3.2.1 The *Insurance Act* 24 of 1943

It is interesting to note that the initial 1943 *Insurance Act* made no specific reference to "guarantee policies" or "guarantee business". However, following two subsequent amendments to the *Act*, these terms were then incorporated. The phrase "guarantee business" was introduced by sec. 1*(h)* of the first amendment[68] and subsequently amended by sec. 1*(b)* of the second amendment,[69] and was defined as "the business of assuming obligations under guarantee policies".[70]

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60 Millard 2020:2-5.
61 Millard 2020:2-5.
62 Reinecke *et al*. 2013:537.
63 Reinecke *et al*. 2013:537.
64 Reinecke *et al*. 2013:536.
65 Reinecke *et al*. 2013:536.
66 Reinecke *et al*. 2013:536.
67 *Insurance Act* 27/1943.
68 *Insurance Amendment Act* 10/1965.
69 *Insurance Amendment Act* 103/1979:
70 Inserted by the *Insurance Amendment Act* 10/1965:sec. 1(h) and substituted by the *Insurance Amendment Act* 103/1979:sec. 1(b).

A definition of “guarantee policy” was similarly inserted by sec. 1*(h)* of the first amendment and subsequently amended by sec. 1*(c)* of the second amendment and was defined as

> any contract whereby any person assumes an obligation (in return for the payment or the promise of the payment of a sum or sums of money, and otherwise than incidentally to an insurance effected by means of some other class of policy) to discharge the debts or other obligations of any other person in the event of the failure of that person to do so, and includes any statutory form of bond, guarantee or undertaking issued by any person in return for payment.

Worth noting is that an insurer undertaking to carry on “guarantee business” in terms of the *Insurance Act* was required to register as such.[71]

In the case of *Johannesburg Livestock Auctioneers Association v President Insurance Co Ltd*,[72] the definition of a guarantee policy was brought under inspection. The facts, in brief, were as follows. The plaintiff was owed R100 000 by a company subsequently placed under liquidation. The defendant was a registered domestic insurer, which was also registered to do guarantee business. The insurer had bound itself as surety and co-principal debtor and guaranteed to the plaintiff that it would pay a sum not exceeding R150 000 in respect of money owing to the plaintiff in respect of purchases made by the company which was placed under liquidation.[73] Subsequently, the insurer attempted to avoid liability, by denying that the surety bond was incorporated in a guarantee policy or that the deed constituted a guarantee policy within the meaning of sec. 20(2)*(b)* of the 1943 *Insurance Act*.[74] The court held that, prior to the two amendments to the *Act* (in 1965 and 1979, respectively), such a guarantee was required to be incorporated in a valid insurance policy. However, following the amendments, the word or concept of a policy no longer applied.[75] The *Act* now specified that a guarantee policy was required to be “any contract …” and, therefore, it was no longer necessary to draw the difference between a contract of suretyship and insurance.[76] The court stated that, if the legislature had intended to limit the nature of the contract, it would have done so in unambiguous terms.[77]

This case made it clear that an undertaking to provide benefits upon the occurrence of an event “relating to the failure of a person to discharge an

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71 1943 *Insurance Act:*sec. 20(2)(b).

72 *Johannesburg Livestock Auctioneers Association v President Insurance Co Ltd* 1987 1 SA 539 (W).

73 *Johannesburg Livestock Auctioneers Association v President Insurance Co Ltd*:540.

74 See the previous judgment of Theron J in *Trans Africa Credit and Savings Bank Ltd v Union Guarantee and Insurance Co Ltd* 1963 2 SA 92 (C).

75 *Johannesburg Livestock Auctioneers Association v President Insurance Co Ltd*:541.

76 *Johannesburg Livestock Auctioneers Association v President Insurance Co Ltd*:543.

77 *Johannesburg Livestock Auctioneers Association v President Insurance Co Ltd*:543.

obligation" could include suretyship contracts.[78] This is a pertinent point to bear in mind when it comes to the wording and drafting of insurance policies and specifically guarantee policies, especially with regard to the obligation of the insurer under the policy itself.[79]

3.2.2 The *Short-term Insurance Act* 53 of 1998

In terms of the 1998 *STIA*, the definition of a short-term policy becomes the starting point and can be found in sec. 1, which states that a "short-term policy" means an engineering policy, guarantee policy, liability policy, miscellaneous policy, motor policy, accident and health policy, property policy, or transportation policy, or a contract comprising a combination of any of those policies; and includes a contract whereby any such contract is renewed or varied.[80] This definition clearly includes guarantee policies as being short-term policies and were accordingly governed under the *STIA*.

The definition of a "guarantee policy" under the *STIA*

> means a contract in terms of which a person, other than a bank, in return for a premium, undertakes to provide policy benefits if an event, contemplated in the policy as a risk relating to the failure of a person to discharge an obligation, occurs; and includes a reinsurance policy in respect of such a policy.[81]

Importantly, one must note that the concept of a premium plays an integral part of a guarantee policy and is considered one of the *essentialia* of any insurance contract.[82] This means that a contract will only constitute an insurance contract if a premium is payable, as well as an undertaking by the insurer to cover the insured and the risk.

In order to carry on guarantee insurance business, insurers must be authorised to do so.[83] Further to that, sec. 33(1) of the *STIA* states that a short-term insurer shall not encumber its assets or allow its assets to be held by another person on its behalf directly or indirectly borrow any asset; by means of suretyship or any other form of personal security, whether under a primary or accessory obligation, give security in relation to obligations between other persons, unless the short-term insurer is registered to provide policy benefits in terms of a guarantee policy and does so in terms of a guarantee policy, without the approval of the Registrar, given generally or in a particular case, and subject to such conditions as the Registrar may determine.[84] Reinecke *et al.* explain that this prohibition is not readily clear. The authors, however, believe that it should be read as meaning

78 For a further discussion on suretyship and insurance, see Reinecke *et al*. 2013:92-93.
79 See section 4.3 below.
80 *STIA*:sec.1(1).
81 *STIA*:sec.1(1).
82 Reinecke *et al.* 2013:86.
83 *STIA*:sec.7(1).
84 *STIA*:sec.33(1)(d).

that insurers not registered to carry on guarantee business insurance may conclude suretyships only with approval from the Registrar, while those that do have authority to carry on guarantee business insurance may conclude suretyships without the approval of the Registrar.[85] Sec. 33 has since been repealed by the 2017 *Insurance Act*.[86]

The nature of guarantee policies has come under scrutiny[87] on many occasions, due to the wording of the policies as being either demand guarantees[88] or accessory guarantees.[89] Either way, however, they both still are encompassed under a guarantee policy, but the insurers' obligation to perform will depend on the nature of the guarantee as either being principal or accessory.[90] In South African law, as in English law, the question whether a particular guarantee is the one or the other requires an interpretation of the terms of the guarantee. It is, accordingly, important for insurers to ascertain the precise nature of any construction guarantee they may issue.[91]

3.2.3 The *Insurance Act* 18 of 2017

The new *Insurance Act* was assented to by the President on 18 January 2018 and came into effect on 1 July 2018. The *Act* establishes a legal framework for the prudential regulation and supervision of insurers and insurance groups in terms of the Twin Peaks model.[92] The *Insurance Act* repealed various sections of both the *STIA* and the *LTIA*, including sec. 33. as mentioned earlier. Importantly, the *Insurance Act* now differentiates between life and non-life policies. Under the *Insurance Act*, a ''non-life insurance policy'' means any arrangement under which a person, in return for provision being made for the rendering of a premium to that person, undertakes to meet insurance obligations that fully or partially indemnify loss on the happening of an unplanned or uncertain event.[93]

In terms of Table 2 of the *Insurance Act*, there are classes and sub-classes of non-life insurance policies. The guarantee class states that such policies cover loss resulting from either insolvency, or the direct and indirect failure of

85 Reinecke *et al.* 2013:536.

86 *Insurance Act* 9/2017:schedule 1.

87 See *Dormell Properties 282 CC v Renasa Insurance Co Ltd and Others* 2011 1 SA 70 (SCA) where it was said that the guarantee was wholly independent of the underlying building contract and whatever disputes subsequently arose between the employer and the contractor were irrelevant to the guarantor's obligations under the guarantee.

88 *Lombard Insurance Co Ltd v Landmark Holdings (Pty) Ltd*; *Petric Construction CC t/a AB Construction v Toasty Trading t/a Furstenburg Property Development and Others* 2009 5 SA 550 (ECG).

89 Reinecke *et al.* 2013:538. For accessory guarantees, see *Basil Read (Pty) Ltd v Beta Hotels (Pty) Ltd and Others* 2001 2 SA 760 (C).

90 See section 2.3 above.

91 Van Niekerk 2009:680-683.

92 See discussion above.

93 The term "insurance obligations" includes a guarantee. See *Insurance Act* 9/2017:schedule 2.

a person to discharge an obligation, or suretyship offered as part of normal business activities, other than a guarantee issued by a Bank registered under the *Banks Act*. Therefore, when dealing with construction or building guarantees, it is clear that the *Insurance Act* covers the loss resulting from a failure to discharge an obligation under a guarantee policy, which may take the form of an independent guarantee or accessory guarantee.

4. ANALYSIS OF THE PREVALENCE OF INSURANCE COMPANIES ISSUING GUARANTEES

The decision as to which financial institution (*i.e.*, bank or insurance company) to approach for the issuance of an independent guarantee is generally not one that is taken lightly. Such a decision is informed by a variety of factors. As indicated earlier,[94] in South Africa, insurance companies are increasingly engaged as issuers of independent guarantees, while there appears to be a decline in bank-issued guarantees. Our research points to the following factors as the main contributors to this trend: (i) the favourable security requirements of insurance companies; (ii) the significance of the premium attached to guarantee policies, and (iii) the increasing flexibility of insurance companies in relation to the formulation of guarantees. While we concede that there may be other relevant factors,[95] these three factors appear to be the most important to the parties in ascertaining a suitable issuer.

4.1 Security requirements

Before a financial institution accepts a demand-guarantee application, it may, as indicated earlier,[96] wish to obtain security for reimbursement after it discharges its payment obligations. Banks and insurance companies diverge on the type of security they may require. Banks frequently require a cash deposit.[97] The cash deposit usually constitutes a high percentage of the guarantee amount. In fact, in many cases, a 100 per cent cash deposit is required. Banks also often require collateral in the form of a pledge agreement for assets. Such assets may, and usually do, include cash accounts. Collateral is typically equal to, or constitutes a high percentage of the guarantee amount. The practical implication of both types of securities is that the applicant would need to depart with, or set aside a significant amount of cash to secure the guarantee, thus before the commencement of the underlying (construction) project. In practice, the bank may, but not necessarily, require both types of security.

The approach of South African banks to security requirements is, *inter alia*, informed by the capital adequacy requirements imposed on them through the prudential regulatory framework,[98] a detailed discussion of which is beyond

94 Section 1. above.
95 Such as long-standing relationships with specific financial institutions.
96 Section 2.2 above.
97 Bertrams 2013:22-25.
98 Consisting of the *Banks Act* and the *FSRA*.

the scope of this article.[99] Essentially, for every transaction a bank wishes to enter into, it needs to hold, in its reserves, capital equivalent to the transaction amount. This ensures that the bank is able to meet its contractual obligations without fear that doing so would render it financially unstable. South Africa's prudential regulatory framework is influenced considerably by the standards issued by the Basel Committee on Banking Supervision.[100]

As discussed earlier,[101] insurance companies must comply with SAM, which, in turn, informs the security requirements of insurance companies. Insurers routinely use three different types of instruments such as indemnities, suretyships, and notarial bonds to secure reimbursement in demand-guarantee transactions.

An indemnity is a contract in which "one party undertakes to keep another harmless against loss; that is, to make good any loss suffered by that other".[102] It is noteworthy that the insurer under an indemnity can only recover the amount of the actual loss suffered or the liability it incurred and not the actual value of the indemnity itself.[103]

A suretyship is a contract between a creditor, a principal debtor, and a third party binding himself/herself in part or in whole on behalf of the principal debtor, usually as surety and co-principal debtor.[104] The surety undertakes, in his/her personal capacity, to take the place of the principal debtor and pay the creditor if the principal debtor cannot. When a guarantee is sought from an insurance company, the directors of the applicant may be required to stand surety. The recent case of *Schoeman v Lombard Insurance Co Ltd*[105] is a good example of a case, in which the directors of a company stood surety in respect of a demand guarantee and sought to resist liability under the suretyship. In guarantee practice, the security normally required from large, well-established companies is an indemnity,[106] while in the case of small to medium-sized companies, an indemnity is usually accompanied by personal suretyships in respect of the directors.[107]

Insurance companies also make use of notarial bonds. A notarial bond is a bond attested by a notary public, hypothecating all the movable assets or a specific asset of the debtor, and is registered in the Deeds Office by the registrar of deeds in a manner similar to mortgage bonds.[108] The security, which forms the subject matter under the notarial bond, must be movable, in the form of either corporeal or incorporeal movable property. In the construction

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99 For a comparative discussion in this regard, see Grizet 2020:95-109.
100 Grizet 2020:100-102.
101 See section 3.2 above.
102 Mugasha 2003:14; Bailey 2016:911.
103 Marxen 2018:95.
104 Forsyth & Pretorius 2010:27-28.
105 See the case discussion in section 4.3 below.
106 See, for example, *Group Five Construction (Pty) Ltd v Member of the Executive Council Public Transport Roads and Works Gauteng*; *Phenix Construction Technology Ltd v Hollard Insurance Company Ltd*.
107 See, for example, *Schoeman v Lombard Insurance Co Ltd*.
108 Ntsoane 2018:2.

industry, notarial bonds are usually registered over the prime equipment of the contractor.

It is clear from the above that the security requirements of banks are cash-oriented, while the security requirements of insurance companies are not. Over the past decade, the South African economy has not, to put it mildly, shown great promise. Year-on-year, the economy has either expanded minimally or contracted.[109] In recent times, the economy has come under immense pressure due to, *inter alia*, prolonged electricity shortages (known locally as “loadshedding”) and more persistent inflationary pressures than expected.[110] This has had and continues to have a profoundly negative impact on the business operations and, importantly, the cash flow of South African businesses. This is especially true of the construction industry in which cash plays a vital role in the completion of existing projects as well as the pursuit of other projects.[111]

Against this background, we argue that the security requirements of banks are not advantageous to the parties in the guarantee market, especially in the current economic climate in South Africa. Prospective applicants of guarantees are more likely to consider an issuer whose security requirements will have less of an impact on its cash flow.[112] Insurance companies have accordingly emerged as a viable option in this regard. The typical security requirements of insurance companies do not entail upfront capital. In fact, it appears that the general approach of insurance companies is to avoid cash deposits and collateral requirements as far as possible.[113] The premium attached to guarantee policies, moreover, is a critical aspect to the success of insurance companies in the guarantee market.

4.2 The significance of the premium

The concept of premium is unique to an insurance contract. As mentioned earlier,[114] a premium is recognised as one of the *essentialia* of these nominate contracts. It is also a distinguishing feature of a guarantee policy from a bank-issued guarantee. As indicated earlier, banks require the full cash deposit amount of capital in the granting of an independent guarantee. However,

109 See Stats SA “South African GDP grows by 1.6%”, https://www.statssa.gov.za/?p=15991 (accessed on 22 February 2023), which reports an economic growth of 1.6% in the third quarter of 2022 after a contraction of 0.7% in the second quarter of the same year.

110 Organisation for Economic and Co-operation Development 2022:206.

111 See Andrews & Millet 2011:622.

112 The same conclusion is reached in Apio “Bank guarantees versus insurance guarantees”, https://www.apio.co.za/2019/09/26/bank-guarantees-vs-insurance-guarantees/ (accessed on 20 February 2023).

113 Lombard Insurance, for example, makes the following statement in relation to guarantees on their official website: “Burdensome collateral requirements (if any) are kept to a minimum.” See Lombard Insurance “Service beyond just guarantees”, https://www.lombardins.com/guarantees/construction-guarantees/ (accessed on 22 February 2023).

114 See section 3.2.2 above.

by contrast, insurers issuing guarantee policies provide a viable option in the case where upfront capital is not possible. Insurers offer these policies to policyholders at a price (and usually with additional security attached to the policy itself) in the form of a premium, thus allowing the policyholder to have the guarantee but at the option of paying monthly premiums for such an offering.

The premium implies several benefits for the parties to the guarantee. Before venturing into these benefits, however, it is necessary to explain in more detail the concept of premium. The starting point in this regard is the definition of an insurance contract. In *Lake v Reinsurance Corporation Ltd*,[115] it was stated that it is

> [a] contract between an insurer (or assurer) and an insured (or assured) whereby the insurer undertakes in return for the payment of a price or premium to render to the insured a sum of money, or its equivalent, on the happening of a specified uncertain event in which the insured has some interest.[116]

From this definition, it is evident that insurance policies are distinguished as such by reference to the cover provided by the insurer, the risk, and the premium. Insurers are willing to take on a particular risk at a specific price. In the case of guarantee policies, the insurer will be willing to provide such cover to the policyholder, once they have understood the risks associated with the project, accepted such risks, and then determined the price at which they are willing to accept such risks.

The 2017 *Insurance Act* defines premium as "any direct or indirect, or partially or fully subsidised, consideration given or to be given in return for an undertaking to meet insurance obligations".[117] Modern insurers determine the amount or rate of the premium with reference to many factors, including, importantly, the risk or risks involved. They base their calculation of premium rates on actuarial principles and usually measure the risks presented by groups of insured rather than that of an individual insured, but that is not a requirement for the legal validity of the insurance contract. In the context of guarantee policies, insurers will assess the risk presented by the prospective policyholder with specific reference to the ability of the policyholder to pay the premium and provide other security, the experience of the policyholder within their field, and the principal price of the policy itself.

Clearly, an understanding of the risk is key to the premium calculation. The term 'risk' for the purposes of insurance refers to the possibility that an uncertain event or peril may occur.[118] It has been defined as "the possibility of the occurrence of an uncertain event leading to an undesirable consequence, such as damage or harm, whether patrimonial or not, to which the insured himself, his property or even his interests are exposed".[119] In insurance, the

115 *Lake v Reinsurance Corporation Ltd* 1967 3 SA 124 (W).

116 *Lake v Reinsurance Corporation Ltd*:480G.

117 *Insurance Act*:sec. 1(1).

118 Nagel 2019:357. Notably, peril, in turn, is the cause of the harm.

119 Millard 2013:85.

term 'underwriting' is used ubiquitously and refers to the process of evaluating the client and the risks that insurers are willing to take on.[120] Underwriting thus focuses on the concept of risk and the evaluation thereof. Therefore, in the issuing of guarantee policies, the underwriting stage will contribute significantly to the acceptance and transfer of the risk by the potential policyholder to the insurer. The insurer will consider the unique risks posed by the project and then also determine the premium attached thereto.

The premium implies the following benefits for the parties to the guarantee. First, it enables the policyholder to pay smaller, more manageable amounts over an extended period of time, in order to keep the guarantee alive. This ties in with the general concept of insurance relating to risk-pooling and a method of spreading the risk over a community of exposed persons.[121] This is in contrast to the case of banks where, as mentioned earlier, a significant amount of upfront capital is normally required before the guarantee is issued.

Secondly, the premium is directly linked to the risk and an insurer is a risk-assessment specialist. Like Lombard Insurance Ltd, insurers who specialise in the issuing of guarantee policies are equipped to understand and evaluate the unique risks posed by, for example, a construction guarantee. They work closely with experts such as engineers and architects to analyse and assess the risks at hand. So viewed, the beneficiary can rest assured that the premium calculated is an accurate representation of the risk posed by the transaction. This position, when compared with a bank, is not akin. Banks appear to be more generalised in this regard and do not necessarily understand or evaluate the risks associated with the underlying (construction) project. The reason is that they generally do not need to be specialists in this regard, since they get their full capital upfront and that security is sufficient for them.

Thirdly, premiums may increase or decrease periodically, depending on the assessment of the risk at a particular point in time. This means that insurers may review premiums and assess a project periodically to ensure that the premium being charged is still accurate. A decrease in the premium naturally will be advantageous to the applicant of the guarantee. For an insurer, periodic review and assessment of the premium and the risk ensures that it maintains the adequate price of the coverage in the guarantee. Insurers, moreover, are able to protect themselves in the case of a non-payment of a premium, by including a provision in the policy that states that, if the premium is not paid within a certain time limit, then the policy will lapse.[122]

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120 The term itself was derived from England, where marine insurance retained its prominent position for some considerable time. It was increasingly transacted at a coffee house in the City of London owned by a man call Lloyd. There developed the practice that the merchant wishing insurance would pass around to the people who were willing to provide it, a slip of paper on which he wrote the details of the ship, voyage, cargo, etc. Those willing to accept a portion of the risk initialled the slip. When the total amount of the risk was underwritten, the contract was complete. From this practice comes the term 'underwriter'.

121 Reinecke *et al* 2013:88.

122 Reinecke *et al* 2013:87. See also rule 6 of the 2017 Policyholder Protection Rules with regard to premiums and rule 15 with regard to periods of grace.

The final point to be made, in this instance, relates to the role of reinsurance in the issuing of guarantee policies. Reinsurance can be described as an insurance contract, in terms of which an insurer transfers the risk/s it has taken over under an insurance contract in whole or in part to another insurer.[123] In the case of a guarantee policy, this essentially means that the undertaking to pay is backed by another insurer. Thus, reinsurance can be viewed as a form of protection for the beneficiary.

4.3 Formulation of the guarantee

The drafting of the guarantee is an important aspect, since the transaction must be carried out in accordance with the terms and conditions of the guarantee. As indicated earlier,[124] independent guarantees encountered in the construction industry, irrespective of whether the issuer is a bank or an insurance company, are often based on the standard-form guarantees of the JBCC and GCC. But this is not always the case. Occasionally, bespoke or *ad hoc* guarantees are issued instead. The case of *Minister of Transport and Public Works, Western Cape v Zanbuild Construction (Pty) Ltd* is of particular interest in this regard. In this case, the Department of Transport and Public Works contracted with Zanbuild to construct two pathology laboratories. In accordance with the construction contracts, two construction guarantees were issued by Absa Bank in favour of the Department. It is important to note that these guarantees differed substantially from both the JBCC standard-form guarantee and the in-house guarantee called for by the Department. They were nevertheless accepted by the Department.[125]

Following certain issues with the work, the Department purported to cancel the construction contracts. Zanbuild accepted the cancellation as a repudiation by the Department, the contracts thus coming to an end before the projects could be completed. The Department then demanded payment from the bank in terms of the guarantees. The Department did not contend that it had an identifiable monetary claim against Zanbuild under the construction contract but maintained that the guarantees stood independent from the construction contracts, in a manner comparable to irrevocable letters of credit. The Department thus merely had to claim from the bank on the basis of the event specified in the guarantee. Zanbuild contended that the guarantees were inextricably linked to the construction contracts in a manner akin to a suretyship agreement, in which case the bank's liability would extend only as far as the Department could demonstrate a claim against Zanbuild under the construction contracts.

The court found that the language of the guarantees concerned accorded with the language associated with suretyships, and that, construing the guarantees as a whole, they gave rise to liability on the part of the bank akin

123 Reinecke *et al* 2013:504.

124 See section 2.1 above.

125 *Minister of Transport and Public Works, Western Cape v Zanbuild Construction (Pty) Ltd*:par. 4.

to suretyship.[126] Hugo submits that the outcome of this case would have been different, if the guarantee had been a JBCC or GCC standard-form guarantee.[127]

The case of *Schoeman v Lombard Insurance Co Ltd* is also relevant. In this case, a demand guarantee, which was the in-house guarantee of Sasol (the beneficiary), was issued in terms of a facility agreement. Additional security was provided in the form of a counter-indemnity to indemnify Lombard (the issuer) against any claim against it arising from the guarantee, suretyships executed in favour of Lombard securing Golden Sun's (the indemnifier) debt against Lombard under the counter indemnity, and two other suretyships executed on behalf of a trust in favour of Lombard.[128]

Clause 1 of the guarantee stated that "[p]ayment shall be made under this guarantee upon receipt by the guarantor, at the above stated address, of the beneficiary's first written demand".[129] The only address appearing above clause 1 was Sasol's business address.[130] The parties subsequently entered into a dispute and Sasol called up the guarantee, by presenting its demands to Lombard's business address, where they were, in fact, received by Lombard.[131] Lombard examined the demands, found them to be "good and compliant", and duly honoured them.[132] After Golden Sun failed to pay Lombard's claims in accordance with the counter-indemnity and the facility agreement, respectively, Lombard sought payment from the sureties pursuant to the suretyship agreements. The sureties' defence, in this regard, was that the demand made by Sasol constituted a non-conforming demand, with the result that Golden Sun's obligation to pay in terms of the counter-indemnity was not triggered.[133]

On appeal, the Supreme Court of Appeal found that the court *a quo* "correctly concluded that the demands had been properly presented, with the result that the guarantor's obligation to pay was effectively triggered".[134] This litigation would, in all probability, we submit, have been avoided if the guarantee had been issued subject to a standard-form guarantee.

These two cases support the view that guarantee issuers in South Africa seem to be flexible in the formulation of guarantees.[135] This is especially true of insurance companies. The following statement appears on the official website of Lombard Insurance, arguably the leading construction guarantee issuer

126 *Minister of Transport and Public Works, Western Cape v Zanbuild Construction (Pty) Ltd*:par. 19.
127 Hugo 2016:443.
128 *Schoeman v Lombard Insurance Co Ltd*:paras. 1, 2, 4, and 19.
129 *Schoeman v Lombard Insurance Co Ltd*:par. 26.
130 *Schoeman v Lombard Insurance Co Ltd*:par. 27.
131 *Schoeman v Lombard Insurance Co Ltd*:par. 28.
132 *Schoeman v Lombard Insurance Co Ltd*:par. 33.
133 *Schoeman v Lombard Insurance Co Ltd*:par. 7. The other defence raised by the sureties related to the premium and guarantee fees. It is not necessary to deal with this defence, in this instance.
134 *Schoeman v Lombard Insurance Co Ltd*:par. 29.
135 See also *Raubex Construction (Pty) Ltd v Bryte Insurance Company Ltd* [2019] *ZASCA* 14 (20 March 2019).

in South Africa: "We cater for standardised *and employer-specific, bespoke guarantee wordings*. All wordings issued provide the best protection to all parties involved."[136] Another insurance service provider similarly boasts on their official website in providing "[b]espoke and flexible insurance solutions to suit [their] customers' unique risk requirements".[137] Guarantee practice indicates that the increasing flexibility of insurance companies in the formulation of guarantees is appealing to especially the prospective beneficiary, since it may be afforded an opportunity to provide its own in-house guarantee or determine the terms and conditions of the new guarantee.

From the case laws discussed earlier, however, it is also clear that bespoke or *ad hoc* guarantees may sometimes create confusion in the interpretation of the guarantee. Poor drafting may, indeed, lead to misconstruing an independent guarantee as an accessory guarantee and vice versa, which may give rise to serious unintended consequences. We offer the following suggestion in conclusion. Parties should insist on using standard-form guarantees rather than bespoke or *ad hoc* guarantees,[138] irrespective of whether the issuer is a bank or an insurance company. However, if there is good reason not to use standard-form guarantees, then all the relevant parties must pay meticulous attention in the drafting of the guarantee, specifically to the terms and conditions relating to the circumstances under which a call may be made on the guarantee. This also applies to in-house guarantees.

5. CONCLUSION

Internationally, banks can be viewed as the primary issuers of independent guarantees. In South Africa, however, insurance companies have emerged as prolific issuers of these instruments, particularly in the construction industry, where guarantees are used to secure the interests of either the employer or the contractor. This is especially apparent from case law. In this article, we have identified three factors as constituting the main contributors to this development in South Africa. First, the security requirements of insurance companies generally have hardly any to no impact on the cash flow of prospective applicants, in stark contrast to the security requirements of banks which tend to be cash-oriented. Secondly, the premium attached to guarantee policies implies several benefits for the parties. Finally, insurance companies are increasingly flexible in the formulation of guarantee policies, which is an attractive offering to especially prospective beneficiaries.

When these factors are considered in tandem, it becomes clear that, in the provision of guarantees, insurance companies are more pragmatic and financially viable than banks. Insurance companies are, therefore, likely to dominate the guarantee market in South Africa for the foreseeable future, especially given the volatility of the South African economy.

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136 Lombard Insurance "Service beyond just guarantees", https://www.lombardins.com/guarantees/construction-guarantees/ (accessed on 22 February 2023) (our emphasis).

137 Apio "Our solutions", https://www.apio.co.za/our-solutions/ (accessed on 22 February 2023).

138 See Hugo 2016:442.

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