

Exclusion of set-off clauses and the UCTA “reasonableness” requirement

Introduction

1. The Singapore Court of Appeal in Koh Lin Yee v Terrestrial Pte Ltd and another appeal [2015] SGCA 6 expressed the view that a contractual clause excluding a right of set-off is capable of being subject to the requirement of reasonableness in the Unfair Contract Terms Act (“UCTA”).
2. On the facts of that case, the Court decided that the UCTA did not apply to no set-off clause found in the loan agreement; and even if the UCTA applied, the clause met the reasonableness requirement.

Summary of the Facts

3. The dispute before the Court of Appeal involved Koh Lin Yee (“Koh”), Allgo Marine Pte Ltd (“Allgo”) (collectively, “the Appellants”), and Terrestrial Pte Ltd (“Terrestrial”).
4. In 2009, Allgo agreed to sell a flat top barge to Terrestrial for \$1.2m. Terrestrial paid Allgo in full. However, Allgo failed to pay its barge builder an outstanding sum of \$350,000.
5. By a Loan Agreement, Terrestrial agreed to make two short term loans to Allgo of \$300,000 and \$50,000, so as to enable Allgo to pay its builder the outstanding sum. Koh, who was a director of Allgo, guaranteed Allgo’s obligation to repay the loans.
6. Clause 12.2 of the Loan Agreement provided that all repayments made by Allgo or Koh were to be made “without set-off, counterclaim, or condition”.
7. Following Allgo’s failure to repay the loans, Terrestrial served letters of demand on both Appellants. Terrestrial commenced legal proceedings and obtained summary judgment against the Appellants. The Appellants appealed to the Court of Appeal against the summary judgment.

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For any queries relating to this article,
please contact the following persons:

Christopher Tan
Partner – Litigation and Dispute
Resolution
DID: 6557 4618
christophertan@leenlee.com.sg

Authors:

Christopher Tan
(with thanks to Etsuko Lim)

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8. Allgo claimed that the Appellants were unable to repay the loans because Terrestrial had breached a separate contract and had failed to pay monies under that contract. The Appellants argued that the monies due under the Loan Agreement had to be set off against the sum owed to them under the separate contract.

The Court's Decision and Reasoning

9. The Court ultimately dismissed the Appellant's arguments.
10. One of the Appellant's arguments was that clause 12.2 should be interpreted to refer to only legal set-offs, and not equitable ones. The Court was of the view that clause 12.2 excluded all forms of set-off, with no distinction between the two.
11. The main argument the Appellant made, which the Court of Appeal discussed in detail, concerned the issues of whether the UCTA applied to clause 12.2, and if so, whether the clause met the reasonableness requirement in the UCTA.
12. On the facts, the Court decided that the UCTA did not apply:
 - (a) In the context of the Loan Agreement, the Appellants were not dealing with Terrestrial "as consumer" within the meaning of section 12 of the UCTA. The Loan Agreement was, in truth, a one-off transaction for both Allgo and Terrestrial.

Allgo's obtaining the loan from Terrestrial was, at its highest, merely incidental to Allgo's carrying on of its business. There was no "degree of regularity" which could have made the obtaining of a loan, a "clearly integral" part of Allgo's business.

Further, Terrestrial did not make the Loan Agreement in the course of its business; it was not in the business of making loans.

- (b) The Loan Agreement also did not contain any standard terms of business within the meaning of section 3(1) of the UCTA. Although the terms of the Loan Agreement could be commonly found in loan documents, the Loan Agreement was not part of Terrestrial's "standard terms of business". The Loan Agreement was drawn up specifically to deal with the circumstances that had arisen.

The UCTA can apply to exclusion of set-off clauses

13. The Court of Appeal expressed the view that if the threshold requirements of the UCTA were met, the reasonableness test in the UCTA could apply to an exclusion of set-off provision, inasmuch as the no set-off clause excludes or restricts any right or remedy in respect of liability and/or excludes or restricts the procedural rules as to set-off. In doing so, the Court disagreed with an earlier High Court decision.
14. The Court examined in detail a number of English cases, as well as academic text books, and considered the issue on the basis of logic and principle. The Court of Appeal was of the view that while a set-off is (in and of itself) a separate cause of action, a clause excluding a set-off can be viewed as "excluding or restricting any right or remedy in respect of liability [the party claiming or relying the set-off is subject to]" within the meaning of section 13(1)(b) of the UCTA.

Reasonableness of Clause 12.2

15. The Court of Appeal noted that the commercial sense of entering into a contract with a no set-off clause is important in the consideration of the reasonableness of the clause. The Court made reference to case law which articulated that:
- (a) The no set-off clause, which seeks to protect a supplier's entitlement to the price of goods or services without deduction, is common in many commercial contexts; and

(b) The no set-off clause is not particularly onerous in scope. Its application is confined to the payment of goods and services supplied, and as such, it seeks to protect one party's cash flow.

The Court recognized that there are legitimate commercial expectations of a claiming party to be paid in full without the need to litigate a cross-claim.

16. The Court also made the point that in the examination of the reasonableness of such a clause, the courts should not be too ready to focus on remote possibilities or to accept arguments that a clause fails the test by reference to relatively uncommon or unlikely situations.
17. The Court further pointed out that due regard must be given to the fact that a no set-off clause does not restrict or exclude liability in so far as the cross-claim is concerned. The cross-claim can continue as an independent cause of action.
18. The Court also confirmed that the Second Schedule of the UCTA would provide further helpful guidance in applying the reasonableness test.
19. On the facts, even if UCTA had applied to clause 12.2, the clause was reasonable. Clause 12.2 did not close the doors on the Appellant's claim for the alleged breaches under the separate contract, and the bargaining positions of the parties were not so unequally balanced.