

(2002) 10 BOM CK 0083
In the Bombay High Court
Case No : Arbitration Petition No. 351 of 2002

Crown Maritime Co. (I) Ltd.	Vs	APPELLANT
Econ Engineering Pvt. Ltd. and Another		RESPONDENT

Date of Decision : 07-10-2002

Acts Referred:

Arbitration and Conciliation Act, 1996 — Section 9

Citation : AIR 2003 Bom 163 : (2003) 1 ALLMR 717 : (2003) 1 ARBLR 580 : (2003) 1 BomCR 488 : (2003) 1 MhLj 193

Hon'ble Judges : D.Y. Chandrachud, J

Bench : Single Bench

Advocate : G. Vahanvati, General and V.K. Ramabhadran and Madhu M, for the Appellant; P.S. Pratap, for the Respondent

Judgement

D.Y. Chandrachud, J.—In these proceedings u/s 9 of the Arbitration and Conciliation Act, 1996, a declaration is sought by the petitioner that the invocation of a Bank Guarantee by the first respondent on 11th September 2002 is not in accordance with the terms of the guarantee and is mala fide, fraudulent and unlawful. Besides, a permanent injunction restraining the Bank of India, the second respondent, from paying over the proceeds of the Bank Guarantee to the first respondent is sought. In the submissions urged before the Court, no case of fraud or irretrievable injustice has been pressed and the only contention is that the invocation is not in terms of the Bank Guarantee.

2. Briefly stated, the facts are that Petronet India Ltd., a Government Company had upon invitation of tenders, awarded a contract for the construction of an LNG terminal at Dahej to a consortium consisting of a foreign Company by the name of Ballast Nedam International (BNI) along with two other Companies. In turn, the first respondent had been awarded a certain part of the work by BNI. On 8th August 2002, the first respondent awarded a sub-contract to the petitioner for carrying out dredging work at Alang Marine Shipyard, Gogha. Clause 9 of the letter awarding the contract provides for a reference of disputes between the

parties to arbitration. On 13th August 2002, a Bank Guarantee, styled as a guarantee for mobilisation advance, was issued by the Bank of India in favour of the first respondent. The Guarantee recorded that the first respondent having agreed to pay an interest free mobilisation advance of Rs. 50 lakhs to the petitioner for the sub contract of the dredging work at Gogha evidenced by the letter dated 8th August 2002, this amount being recoverable from the running bills of the petitioner in two installments, the first from the second invoice and the balance from the final invoice, the Bank was issuing the Bank Guarantee in question. The material clauses of the Bank Guarantee were as follows :

"We (Bank of India) having our Head Office at Express Towers, Nariman Point, Mumbai-400 021 (hereinafter referred to as "The Bank") do hereby undertake to pay Econ Engineering Pvt. Ltd., an amount of Rs. 5,000,000/(Indian Rupees: Five Million only) against any loss or damage caused to or would be caused to or suffered by Econ Engineering Pvt. Ltd. by Contractor's demand in writing explaining the reasons for the calling off this guarantee, but notwithstanding any contestation or protest by the Sub-contractor or by ourselves or by any other third party to recover the said mobilization advance of Rs. 5,000,000/- (Indian Rupees Five Million only) or part thereof or interest thereon we (Bank of India) do hereby undertake to pay the amount due and payable under the guarantee without any demur. And such demand made on the Bank shall be conclusive not only as regards to sub-contractor's failure but also as regards the amount due and payable by the Bank under this guarantee. However, our liability under this guarantee will be restricted to an amount of Rs. 5,000,000/- (Indian Rupees: Five Million only) as per the sub-contract."

Under the terms of the Bank Guarantee, a claim or demand was required to be made on or before 21st September 2002. On 17th August 2002, the second respondent extended the period of validity of the guarantee upto 26th September 2002.

3. On 24th August 2002, the first respondent informed the petitioner that BNI which was the main contractor had terminated the contract which had been entered into with the first respondent as a result of which the first respondent had been prevented from continuing the work under the contract. The first respondent stated that it was in the process of taking legal action against BNI since it was advised that the termination was wrongful but until the dispute with BNI was revolved, the first respondent was prevented from using the services of the petitioner under the sub-contract with the petitioner. The confirmation of the petitioner was sought that it had ceased further work since 22nd August 2002. On 27th August 2002, the first respondent addressed another letter to the petitioner stating that the sub-contract agreement between the petitioner and the first respondent stood terminated with effect from 22nd August 2002. The petitioner was informed that the first respondent was seeking redress against BNI and the petitioner was called upon to indicate the costs incurred by it since the first respondent intended to seek payment from BNI.

4. On 11th September 2002, the first respondent has invoked the Bank Guarantee issued by the second respondent recording that the sub-contract for the dredging work at Gogha has been terminated as a result of which the first respondent was invoking the Guarantee. The first respondent lodged a claim in the amount of Rs. 50 lakhs under the Guarantee.

5. The Arbitration Petition was filed on 17th September 2002. On 17th September 2002, an ad-interim order was passed by a Learned Single Judge in terms of prayer clause (c) restraining the second respondent from paying over the proceeds of the Guarantee to the first respondent. At that stage, the first respondent had not appeared before the Court and the ad-interim order was made effective until 24th September 2002. On 24th September 2002, the hearing of the Arbitration Petition was posted to 1st October 2002 in order to enable the first respondent to file its reply to the Arbitration Petition and the operation of the ad-interim order dated 17th September 2002 was extended until then. The Bank Guarantee upon its extension was due to expire on 26th September 2002. On 24th September 2002 after the hearing before this Court, a letter was addressed on behalf of the petitioner by their Advocate to the first respondent's Advocate confirming that the petitioner would renew the Bank Guarantee for a further period of three months from the date of its expiry. The Court is informed by the Learned Counsel appearing on behalf of the first respondent that no intimation that the Bank Guarantee had been renewed was received whereupon, on 26th September 2002 the first respondent addressed another letter of invocation to the second respondent. The letter records that the Bank Guarantee was issued in favour of the first respondent at the request of the petitioner for the mobilisation advance under the sub-contract in question. The first respondent stated that it was lodging its claim under the Guarantee and demanded the payment of Rs. 50 lakhs on the ground that the first respondent had terminated the sub-contract with the petitioner and had suffered loss and damages. The subsequent letter of demand dated 25th September 2002 was without prejudice to the previous letter dated 11th September 2002.

6. Learned Counsel appearing on behalf of the petitioner has submitted that the petitioner is entitled to the reliefs which have been prayed for in the Arbitration petition on the ground that the letter of invocation dated 11th September 2002 was not in terms of the Bank Guarantee. The Learned Counsel stated that the case of the petitioner for the grant of injunction is not based on any allegation of fraud or of irretrievable injustice, but on the ground that the Bank Guarantee was conditional and that the condition mentioned therein for the invocation of the guarantee has not been fulfilled. The second submission which was urged was that the first respondent was not entitled to invoke the Bank Guarantee after the first invocation dated 11th September 2002 and that the letter of invocation dated 25th September 2002 is of no consequence.

7. On the other hand, on behalf of the first respondent it has been urged that the letter of demand dated 11th September 2002 was entirely in terms of the Bank

Guarantee: The first respondent had paid to the petitioner a mobilisation advance at Rs. 50 lakhs in connection with the execution of the work of the subcontract which was awarded by the first respondent to the petitioner. The contract of the first respondent with BNI was itself terminated upon which there is no question of there being any performance of the contract awarded by the first respondent to the petitioner. The mobilisation advance was in the circumstances recoverable. The letter dated 11th September 2002 intimates to the Bank that the Guarantee was being invoked as the sub-contract awarded by the first respondent to the petitioner had been terminated. This was a sufficient reason for the invocation of the Bank Guarantee since what the guarantee stipulates is a demand explaining the reasons for the calling of the guarantee. Moreover, it was urged that the second letter of invocation dated 25th September 2002 was addressed by the first respondent to the second respondent since the Bank Guarantee was due to expire on 26th September 2002 and despite the petitioner's Advocate's letter dated 24th September 2002, there was no confirmation until 25th September 2002 that the Bank Guarantee had been renewed. In fact it has been stated by Learned Counsel appearing on behalf of the petitioner that the Bank Guarantee has not been renewed.

8. In considering whether a case has been made out for the grant of interim relief regard will have to be had to the terms of the Bank Guarantee. The terms of the Bank Guarantee provide that the second respondent has undertaken to pay to the first respondent an amount of Rs. 50 lakhs against any loss or damage caused to or that would be caused to or suffered by the first respondent upon a demand by the first respondent in writing explaining the reasons for the calling of the Guarantee. The Guarantee stipulates that notwithstanding any contestation or protest by the petitioner or by any other third party, to recover the mobilisation advance of Rs. 50 lakhs or any part thereof, the second respondent which is the issuing Bank undertook to pay the amount due and payable under the Guarantee without any demur. A demand made on the Bank was to be conclusive not only as regards failure of the petitioner, but also as regards the amount due and payable by the Bank under the Guarantee. The Guarantee was to be alive during the period that would be taken for the recovery of the loan and till all the amounts due had been fully recovered and the claim of the first respondent satisfied or discharged or until the first respondent certified that the amount outstanding under the advance has been fully recovered from the petitioner and discharged the Guarantee. The Guarantee required the first respondent while invoking it to explain the reasons for calling of the Guarantee. In the present case, in the letter of invocation dated 11th September 2002, the first respondent informed the Bank that the sub-contract for dredging had been terminated and that the guarantee has accordingly been invoked. I am of the view that having regard to the well settled position in law, it cannot be held that the invocation was not proper or that it was not in accordance with the terms of the Bank guarantee. The first respondent had awarded a sub-contract to the petitioner in pursuance of a contract which had been awarded by BNI to the first

respondent. BNI terminated the contract awarded to ,the first respondent and upon that termination, the first respondent terminated the contract to the petitioner with effect from 22nd August 2002. Upon the termination of the contract that was awarded by the first respondent to the petitioner, the amount of the Guarantee of Rs. 50 lakhs was invoked. Upon the termination of the contract between the petitioner and the first respondent, the first respondent has thus called back the payment of the mobilization advance of Rs. 50 lakhs. This demand is in accordance with the terms of the Bank Guarantee. The ground mentioned in the letter of invocation dated 11th September 2002 is a sufficient reason for the calling of the guarantee and it cannot be contended that the ground for invocation is not in terms of the guarantee. Rs. 50 lakhs was admittedly paid as a mobilisation advance to the petitioner by the first respondent. The sub-contract between the petitioner and the first respondent has been terminated because the contract awarded by B.N.I, to the first respondent stands terminated. Upon the termination of the sub-contract, the first respondent has invoked the guarantee which is conclusive upon the Bank. The Bank must pay without demur notwithstanding any protest by the petitioner.

9. Learned Counsel appearing on behalf of the petitioner sought to urge that the subsequent letter of invocation dated 25th September 2002 is unlawful because the Bank Guarantee would stand exhausted upon the issuance of the first letter of demand. That submission cannot be accepted. In the present case, a hearing took place before this Court on 24th September 2002 when the matter was adjourned to 1st October 2002 to enable the first respondent to file a reply. In the meantime, the guarantee was due to expire on 26th September 2002. On 24th September 2002 a letter was addressed by the Learned Advocate for the petitioner to the Learned Advocate for the first respondent stating that the Bank Guarantee would be renewed for a further period of three months. Counsel appearing on behalf of the petitioner, however, on seeking instructions informs the Court, that the Bank Guarantee could not be renewed in terms of that letter since the Bank was of the view that the matter was before the Court. In that view of the matter, it has been urged on behalf of the first respondent that since the guarantee was" to expire, a fresh letter of invocation was addressed to the Bank on 25th September 2002 without prejudice to the earlier letter. The submission of the petitioner that the second letter of invocation could not have been addressed on 25th September 2002 cannot be accepted. Essentially, the correctness of the subsequent invocation dated 25th September 2002 would not matter, once this Court has come to the conclusion that the first invocation dated 11th September 2002 is in order. However, since the point has been urged, it is being dealt with. The contention of the petitioner before the Court has not been that the invocation of the Bank Guarantee is either fraudulent or that it would result in irretrievable injustice. The contention of the petitioner is that the letter of invocation dated 11th September 2002 was not in terms of the Bank Guarantee. That being the position, in my view, even if the subsequent letter of invocation dated 25th September 2002 was addressed to the Bank with a view to

obviate a contention in regard to the alleged deficiency in the first letter of invocation that was sought to be urged, there was in my view absolutely no prohibition on the first respondent doing so. I have already come to the conclusion that there is no merit in the contention that the original letter of invocation dated 11th September 2002 was not in accordance with the terms of the guarantee but, even assuming that there was any defect in the invocation, that would not operate to prevent the first respondent from addressing an appropriate letter of invocation to the Bank strictly in compliance with the terms of the Bank Guarantee. The Bank Guarantee did not exhaust itself immediately upon the making of a demand thereunder and if the demand is found not to be strictly in accordance with the condition of the Bank Guarantee that does not bring the contract of Guarantee to an end. The reasons for the furnishing of the Bank Guarantee may still continue to subsist and so long as the period of validity of the Bank Guarantee has not expired and the Guarantee continues to remain effective, it would be open to the beneficiary to submit a fresh letter of invocation. Of course, in such a case, the party at whose behest the guarantee has been issued, is entitled to challenge the subsequent invocation and in a given case, the contention may well be that the subsequent invocation is colourable and fraudulent. That is not the case here and in fact, no ground of fraud is urged in the submissions of Counsel. I am of the view that as a matter of principle there was no prohibition on the invocation of the Bank Guarantee by the first respondent on 25th September 2002 and even if there were to be merit in the contention of the petitioner that the first invocation dated 11th September 2002 was not in accordance with the terms of the Guarantee, that would not prevent the first respondent from thereafter invoking the Bank Guarantee in terms of the conditions of the Guarantee. The terms of the second letter of invocation are also in accordance with the terms of the guarantee.

10. Learned Counsel appearing on behalf of the petitioner has sought to rely upon the judgment of the Supreme Court in *Hindustan Construction Co. Ltd. Vs. State of Bihar and Others*, . The Supreme Court held in that case that the invocation of a Bank Guarantee has to be in accordance with the terms of the Guarantee or else the invocation itself would be bad. In that case, the Bank Guarantee expressly referred to the fact that it was in accordance with Clause 9 of the contract relating to the advance mobilisation loan, that the Guarantee was being furnished. The Guarantee provided that the bank agreed to make payment thereunder in the event of the obligations expressed in the said clause not being fulfilled by the contractor giving the right of claim to the employer for the recovery of the whole or part of the advance mobilisation loan from the contractor under the contract. This part of the Bank Guarantee has been emphasised in paragraph 13 of the judgment of the Supreme Court and the Supreme Court in these circumstances, held as follows:

"This condition clearly refers to the original contract between HCCL and the defendants and postulates that if the obligations, expressed in the contract, are not fulfilled by HCCL giving to the defendants the right to claim recovery of the

whole or part of the "advance mobilisation loan", then the Bank would pay the amount due under the guarantee to the Executive Engineer. By referring specifically to clause 9, the bank has qualified its liability to pay the amount covered by the guarantee relating to "advance mobilisation loan" to the Executive Engineer only if the obligations under the contract were not fulfilled by HCCL or HCCL has misappropriated any portion of the "advance mobilisation loan". It is in these circumstances that the aforesaid clause would operate and the whole of the amount covered by the "mobilisation advance" would become payable on demand. The bank guarantee thus could be invoked only in lie circumstances referred to in clause 9 whereunder the amount would become payable only if the obligations are not fulfilled or there is misappropriation. That being so, the bank guarantee could not be said to be unconditional or unequivocal in terms so that the defendants could be said to have had an unfettered right to invoke that guarantee and demand immediate payment thereof from the Bank. This aspect of the matter was wholly ignored by the High Court and it unnecessarily interfered with the order of injunction, granted by the Single Judge, by which the defendants were restrained from invoking the bank guarantee."

In other words, this was a case where a specific term of the contract between the beneficiary of the Bank Guarantee and the party at whose behest the Bank Guarantee had been furnished, was expressly made a term of the Bank Guarantee. The Bank Guarantee could be invoked only upon a breach of that particular term, clause 9. On the other hand, in the present case, what the Bank Guarantee requires is that a demand has to be addressed by the first respondent explaining the reasons for the calling of the Guarantee, meaning thereby, the reasons for the invocation of the Bank Guarantee. That is what has been done by the first respondent in its letter dated 11th September 2002. The sufficiency of those reasons cannot be disputed by the Bank and indeed in this case, the Bank has not contested its liability to pay under the terms of the Bank Guarantee. The reason why the contract between BNI and the first respondent was terminated is again alien to the issue in this proceedings. The underlying disputes between the petitioner and the first respondent or between BNI and the first respondent cannot furnish any reason for injuncting the encashment of the guarantee. The judgment of the Delhi High Court in Harparshad and Co. Ltd. Vs. Sudarshan Steel Mills, Punjab National Bank, also lays down the same principle which has been enunciated by the Supreme Court in HCCL case supra and, therefore, does not require any separate discussion. On the other hand, I am of the view that the principle which has been laid down by the Supreme Court in a consistent line of decisions in U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd., , General Electric Technical, Services Co. Inc. v. Punj Sons(P) Ltd. (1994) 4 SCC 230 Svenska Handelsbanken Vs. M/s. Indian Charge Chrome and others, and Oil and Natural Gas Corporation Ltd. Vs. State Bank of India, Overseas Branch, Bombay, must be followed in the facts of this case, once it is found that the invocation is in terms of the Bank Guarantee. It is not the

submission of the Learned Counsel appearing on behalf of the petitioner that there is any case of fraud or of irretrievable injustice. The underlying disputes between the petitioner and the respondent, if any, cannot be a reason to injunct the invocation of the Bank Guarantee. There is no merit in the Arbitration Petition which is accordingly rejected. Stay refused.