
(1997) 12 DEL CK 0031

In the Delhi High Court

Case No : OMP No.126/96 and is No. 9767/96

Essar Oil Limited

APPELLANT

Vs

Oil India Limited and Another

RESPONDENT

Date of Decision : 19-12-1997

Acts Referred:

Citation : (1999) 95 CompCas 181 : (1998) 71 DLT 302 : (1998) 44 DRJ 238

Hon'ble Judges : D.K. Jain, J

Bench : Single Bench

Advocate : Mr. Mukul Rohatgi and Mr. Sandeep Sethi, for the Appellant; Mr. V.P. Singh Mr. P.K. Ganguly and Mr. Pramod Aggarwal, for the Respondent

Judgement

D.K. Jain, J.—This is a petition u/s 9 of the Arbitration and Conciliation Act, 1996 (hereinafter referred to as the Act), seeking to restrain respondent No.1 - M/s Oil India Ltd., from encashing the bank guarantee No.95/2, dated 15 May 1995 for Indian rupees equivalent to US \$ 2,221,563 issued on behalf of the petitioner by the Bank of Baroda, Bhubaneswar Branch, Bhubaneswar, respondent No.2 herein, in favor of the first respondent and restraining the said bank from paying any amount under the said guarantee. is 9767/96 is for grant of ad interim relief to the same effect.

2. The facts relevant for the controversy involved are as under:

Pursuant to an open tender, vide agreement dated 8 May 1995, respondent No.1 awarded to the petitioner the work of providing its drill ship "ESSAR DISCOVERER" along with material, services and personnel to enable it to drill three off-shore exploratory wells in Arabian Sea and one off-shore well in the Bay of Bengal, on turnkey basis.

3. Under Article 28 of the said agreement the petitioner was required to furnish to respondent No.1 a performance bond in the form of a bank guarantee for the affronted amount, representing 7.5% of the estimated value of the tender. In compliance thereof the petitioner furnished to respondent No.1 the affronted

bank guarantee from respondent No.2 bank. The relevant portion of the bank guarantee reads as under:

".....AND WHEREAS, one of the terms and conditions of THE AGREEMENT is that THE CONTRACTOR shall furnish a Performance Guarantee to the extent of UNITED STATES DOLLAR 2,221,563.00 in Foreign Exchange as specified in THE AGREEMENT, NOW Therefore, in consideration of the promise aforesaid and at the request of THE CONTRACTOR, We, Bank of Baroda, a Bank registered under the laws of India having its registered office at Mandvi, Baroda, herein- after called THE BANK, so as to bind ourselves and we condition- ally undertake and guarantee to pay to you on an amount not exceeding UNITED STATES DOLLARS 2,221,563.00 against any loss or damage caused to or suffered or would be caused to or suffered by THE OPERATOR by reason of any breach by THE CONTRACTOR of any terms and conditions contained in THE AGREEMENT.

WE, Bank of Baroda do further hereby irrevocably undertake to pay to you, THE OPERATOR the amount due and payable under this guarantee in equivalent Indian rupees at BC Selling rate of Exchange applicable on the date of settlement by the bank without any demur or disputes merely on a demand from THE OPERATOR stating that the amount claimed is due by way of loss or damage caused to or would be caused to or suffered by THE OPERATOR by reasons of any breach by THE CONTRACTOR of any of the terms and conditions in THE AGREEMENT or by reason of THE CONTRACTOR'S failure to perform THE AGREEMENT. Any such demand made on THE BANK shall be conclusive as regards the amount due and payable by THE BANK under the guarantee. However, our liability under this guarantee shall be registered to an amount not exceeding UNITED STATES DOLLARS 2,221,563.00 provided, however, that in any event the obligation of the surety under the Performance Bond shall apply only to any failure or default of THE CONTRACTOR occurring as evidenced by a claim in writing on or before the termination or expiration of said AGREEMENT of 30.11.1996, whichever comes earlier, excluding 14(fourteen) days claim period and not applied to any such failure or default occurring after said date at which time Performance Bond shall expire....."

4. Under the contract the petitioner was required to drill three oil wells off the Saurashtra coast in Arabian Sea, referred to in the contract as Wells No.L-2, L-3 and L-4. The petitioner claims that each of the three wells were satisfactorily drilled by it and its performance was duly accepted by respondent No.1. The last well to be drilled i.e., L-1 was located off North-East coast in the Bay of Bengal, off the Coast of Paradeep in Orissa. For it, under the contract, the drill ship was required to move from Saurashtra coast to North-East coast within 15 days of completion of drilling of three wells in the Saurashtra coast. According to the petitioner, respondent No.1 required it to give a presentation on petitioner's preparedness for drilling L-1, which was given on 26 August 1996. Vide its letter dated 3 September 1996 the petitioner claims to have informed respondent No.1 that they were moving the drill ship ESSAR DISCOVERER to location L-1 and all

the associated services were likely to reach the site on or about 20 September 1996 and thereafter continued to keep respondent No.1 informed about the movement of the drill ship to said location. It seems that respondent No.1 asked the petitioner to obtain requisite clearance from the concerned Naval authorities, which was objected to by the petitioner on the ground that obtaining the said clearance was not the responsibility of the petitioner. It is, however, averred that the petitioner did write to the Eastern Naval Command, Vishakhapatnam, seeking their clarification in the matter, who informed the petitioner that they should approach the Naval Headquarters at New Delhi for obtaining the requisite No Objection Certificate for the said drilling operation. It is alleged that sometime in early September 1996 the defense Research & Development Organisation (for short the DRDO), a departmental undertaking of the Ministry of defense, Government of India, wrote to respondent No.1 that no drilling could be done at location L-1 as it fell within the Missile Testing Range and it called upon respondent No.1 to forthwith cease and desist from taking any action in the matter as there was a complete ban on it. Having come to know that the DRDO had refused permission to respondent No.1 for drilling at location L-1, the petitioner, on 26 September 1996, wrote a letter to respondent No.1, calling upon it to clarify the matter immediately and furnish the requisite clearances sought from time to time by the petitioner.

5. It appears that vide its letter dated 1 October 1996, respondent No.1 asked the petitioner to bring the drill ship to Paradeep for inspection of the rig and its components before undertaking drilling, further advising the petitioner that as the drill ship had already moved to location L-1, the petitioner should spud (start operation) the well immediately after obtaining all necessary clearances. Controverting the allegations leveled in respondent No.1's said letter, the petitioner wrote back to respondent No.1 clarifying that there was no contractual or procedural requirement for the petitioner to go to Paradeep for inspection and hence the drill ship had proceeded directly to location L-1. The petitioner claims to have also informed respondent No.1 that anchoring and puddling could be commenced only after security clearance was obtained, which was the responsibility of respondent No.1 and it had not been obtained by that time.

6. It is further averred that having come to know about some disputes between respondent No.1 and DRDO, the petitioner, vide its letter dated 8 October 1996, clarified its position that it had been waiting in vain for respondent No.1 to obtain the requisite security and other clearances and warned that if the well L-1 is abandoned due to respondent No.1's inability to obtain DRDO permission, the petitioner will claim full well completion charges irrespective of the stage up to which the well shall have been drilled.

7. It appears that not being satisfied with the performance of the petitioner, respondent No.1 terminated the contract on 12 October 1996. The relevant portion of the letter, terminating the contract reads as follows:

"Whereas you are incompetent and incapable of performing your obligations

under the aforesaid contract, please take notice that Oil India Ltd., hereby terminates the above contract in terms of the relevant conditions thereof with immediate effect.

This is without prejudice and in addition to all other rights and contentions which Oil India Ltd., has against you under the aforesaid contract and in law."

8. The petitioner objected to the termination of the contract, terming it mala fide and for extraneous reasons and causes.

9. Simultaneously respondent No.1 invoked the affronted bank guarantee by addressing a letter, dated 12 October 1996, to respondent No.2. It would be necessary to re-produce the letter invoking the bank guarantee:

"Bank of Baroda

Bhubaneshwar Branch,

Bhubaneshwar

Sub:Invocation of Bank Guarantee-

Bank Guarantee for US \$ 22,22,563.00

executed by you on 15th May, 1995.

Sirs,

We entered into an agreement with M/s Essar Oil Ltd. on 8th May'95. M/s Essar Oil Ltd., has failed to perform the agreement.

We, Therefore, invoke the above performance guarantee and demand from you the sum of US \$ 22,21,563/- to be paid to us immediately on receipt of this letter.

Yours faithfully,

OIL INDIA LIMITED

sd/-

(R.Sircar)

Chief Manager(P)

Bay Exploration Project"

10. Aggrieved by the decision of respondent No.1 to rescind the contract and invoke the bank guarantee, the petitioner filed the present petition for interim injunction against the invocation of the bank guarantee.

11. It is alleged that the invocation of the bank guarantee is not in its terms and is fraudulent, apart from being inequitable, amounting to unjust enrichment on the part of Oil India Ltd., because:(a) the demand does not state, as required by the bank guarantee, that "..... the amount claimed is due by way of loss or

damage caused to or would be caused to or suffered by the Operator by reasons of any breach by the contractor of any of the terms and conditions in the agreement...."; and (b) respondent No.1 has actively and with mala fide intent concealed and suppressed the true and correct position from respondent No.2 apparently in an attempt to unjustly enrich itself by the sum guaranteed under the bank guarantee and thereafter pressurise the petitioner to submit to respondent No.1's illegal terms, which being down right and ex facie fraud, cannot be permitted.

12. When the matter came up for hearing on 16 October 1996, while directing the respondents to file a reply to the application, by means of an unusual interim order, respondent No.2 was restrained from clearing the banker's cheque issued by it in respect of the bank guarantee in question and also restrained respondent No.1 from encashing the banker's cheque and receiving the amount as it was brought to the notice of the Court by counsel for respondent No.1, who was present at the time of motion hearing, that the bank guarantee having been invoked on 12 October 1996, a banker's cheque, covering the amount envisaged by the bank guarantee had been received by respondent No.1 from the bank. The said ad interim injunction still continues.

13. The petition is opposed by respondent No.1. While denying any communication to the petitioner regarding successful drilling of L-2, L-3 and L-4, a brief synopsis of the events which took place between the date of award of contract and the movement of the drill ship from Saurashtra coast has been given in the reply in an attempt to demonstrate that the petitioner was incompetent to drill L-1, off North-East coast and as a matter of fact had no intention to drill the same. It is pointed out that though the entire contracted work on all the four wells was to be completed by 7 June 1996, even the last well in Saurashtra coast was completed only on 16 July 1996; the drill ship, which was required to move within 15 days from the completion of work at Saurashtra coast, left the said location site on 6 September 1996 and reached the North-East coast site on 24 September 1996, that too without entire operator's equipment, and in the process there was delay of 70 days on the part of the petitioner in this movement. It is thus, alleged that the petitioner had failed and neglected to bring in the unit at the North-East coast together with all supporting services, as per the contract and had committed a breach of the agreement entitling the respondent to invoke the bank guarantee. It is claimed that the bank guarantee has been invoked strictly in its terms. Allegation of any fraud or suppression of true and correct position from respondent No.2 has also been denied.

14. In the rejoinder, while denying that the petitioner had committed any breach of contract, the delay in movement of drill ship to site L-1 is attributed to inclement weather conditions and delay in anchoring at site to contesting respondent's failure to obtain naval clearance and DRDO permission.

15. I have heard Mr. Mukul Rohatgi, learned Senior counsel for the petitioner and

Mr. V.P.Singh, learned Senior counsel for contesting respondent No.1 at considerable length.

16. As noticed above, invocation of the bank guarantee is challenged on the grounds: (a) invocation is not in accordance with the terms of the guarantee and (b) a fraud allegedly perpetrated by respondent No.1 on the petitioner and the bank. Elaborating on it Mr. Rohatgi has contended that the guarantee being conditional one, in invoking the same, it was incumbent for the respondent to state in the letter invoking the bank guarantee and to satisfy the bank as to in what manner the petitioner had failed to perform the agreement and what was the loss or damage which had been caused/suffered or would be caused/suffered. Learned counsel contends that the letter invoking the bank guarantee is silent in all these details and, therefore, the invocation of the guarantee merely on the ground that the petitioner has failed to perform the agreement is not in terms thereof. In support, reliance is placed on *Puri International (P) Ltd. Vs. National Building Construction Co. Ltd.*, holding that in case the bank guarantee is not invoked in accordance with the terms or the requirements of the guarantee, no invocation and/or encashment of the same is permissible under the law and *U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd.*, wherein at page 184, it was observed that where a bank had given a performance guarantee, it was required to honour it according to its terms. On the second aspect of alleged fraud, it is urged that respondent No.1 had failed to obtain mandatory Naval clearance, which they obtained only on 18 October 1996 and the D.R.D.O. permission, which was also granted only on 1 October 1996 for a limited period up to December 1996, making it impossible for the petitioner to complete the contracted work; and on the other hand the contract was terminated by it for extraneous considerations to cover its own lapses and to save the skin of its functionaries, who had failed to perform their part of the obligation. It is contended that to cover up it all and buy more time, respondent No.1 raised the issue of petitioner's failure to take the drill ship to Paradeep for inspection as respondent No.1 had failed to get the requisite clearances from Naval authorities and the DRDO. Besides, it is urged that respondent No.1 had asked the petitioner on 1 October 1996 to spud despite the fact that it did not have the requisite clearance/permission by that date. According to the counsel, respondent No.1 had not only misled the petitioner regarding various clearances at the time of entering into the agreement but it was also making mis-representations about them even during the execution of the contract, which clearly establishes that the said respondent had committed fraud at the inception as also subsequently during the execution of the contract, and under these circumstances it cannot be permitted to invoke the bank guarantee. Reliance is placed on a decision of the Supreme Court in *Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co.* and another, wherein it has been observed that the Courts may restrain invocation of bank guarantee where a demand by the beneficiary under the bank guarantee may become fraudulent not because of any fraud committed by the beneficiary while

executing the underlying contract but it may become so because of subsequent events or circumstances.

17. On the other hand, Mr. V.P.Singh, learned Senior counsel for respondent No.1 has submitted that since the letter invoking the bank guarantee clearly states that the invocation is by reason of petitioner's failure to perform the agreement, which is the second stipulated condition entitling the respondent to invoke the bank guarantee, in which loss or damage is implied, and merely because there is no specific mention of the words "loss or damage" in the letter, it cannot be said that the bank guarantee has not been invoked in its terms. As regards the allegation of fraud, he has urged that a mere raising of plea of fraud is not sufficient to stop the bank from honouring its obligation under the bank guarantee; it has to be specifically pleaded, established and above all the bank has to be aware of it. Relying on some documents, including the main agreement (clause 1.14), he has refuted the stand of the petitioner that there was no requirement of taking the drill ship to Paradeep for inspection or that the petitioner was in readiness to spud but could not do so because requisite clearances had not been obtained by the respondent. It was urged that under the contract only one statutory clearance under the Petroleum and Natural Gas Rules had to be obtained by the respondent which admittedly was available with it. Insofar as clearance/permission of Naval authorities and DRDO was concerned, counsel submitted that it was not the pre-condition under the contract that these must be obtained before commencing the drilling operations, besides these could be obtained by either of the parties. It is also urged that in any event, taking note of the fact that the drill ship had already moved to location L-1, vide letter dated 1 October 1996, the petitioner was advised to spud in the well immediately, meaning thereby that the respondent had waived the condition of inspection at Paradeep but still the petitioner could not commence its operations. He has contended that even assuming that the contract was wrongfully terminated by respondent No.1, it would not tantamount to fraud so as to interdict the bank from encashing the bank guarantee. In support of his contention that confirmed bank guarantee cannot be interfered with unless a case of established fraud is made out, learned counsel has placed reliance on the decisions of the Supreme Court in *National Thermal Power Corporation Ltd. Vs. M/s. Flowmore Private Ltd. and another*, *U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd.*, AIR 1997 1644 (SC), *Svenska Handelsbanken Vs. M/s. Indian Charge Chrome and others*, and *Dwarikesh Sugar Industries Ltd. v. Prem Heavy Engineering Works (P) Ltd. & Anr.*, JT 1997 (5) SCC 417.

18. It is well settled, as is ruled in series of authorities, that a bank guarantee is an independent contract whereby the bank undertakes to unconditionally and unequivocally abide by its terms and it cannot be affected by disputes between the parties to the underlying transactions. It creates an irrevocable obligation on the bank to perform the contract in terms thereof and on occurrence of the event mentioned therein the bank guarantee becomes enforceable. It is only in

exceptional cases like: (i) a case of established fraud (based on material evidence and not a bald plea in application for stay) of "egregious" nature of which the bank has the knowledge and (ii) allowing encashment would result in irretrievable injustice to one of the parties concerned that the Court may interdict the encashment of the bank guarantee. In all other cases the bank giving such a guarantee is bound to honour it as per its terms (See: U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd., , State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another, , AIR 1997 1644 (SC)).

19. In the latest decision rendered by the Supreme Court in Dwarikesh Sugar Industries Case (supra), while reiterating the general principles laid down in U.P.State Sugar Corporation's case(supra), the Apex Court re-affirmed the views expressed in Bolivinter Oil SA v. Chase Manhattan Bank, (1984)1 All ER 351 to the effect that the "wholly exceptional case where an injunction may be granted is where it is proved that the bank knows that any demand for payment already made or which may thereafter be made will clearly be fraudulent. But the evidence must be clear both as to the fact of fraud and as to bank's knowledge"

Applying the affronted principles, governing invocation of bank guarantees, I am of the view that both the contentions urged on behalf of the petitioner are untenable.

20. There is no gainsaying that the bank guarantee has to be enforced in terms thereof. But the question for consideration is as to who can raise the objection in that behalf. I am of the considered view that having regard to the affronted settled position in law that the bank guarantee is an independent contract between the bank and the beneficiary, creating an irrevocable obligation on the bank to perform the contract in terms thereof, it is only the guarantor bank who can raise the objection to the effect that the invocation is not in terms of the bank guarantee and at that stage the party at whose instance it has been furnished has no role to play, except if it so desires, to bring the relevant facts to the notice of the bank but the ultimate decision in this regard has to be by the guarantor bank. Even the scope of enquiry by the bank at that stage is very limited because on being informed about the non-observance of the contract, the bank cannot assume the role of an arbiter and ask the beneficiary to first establish whether or not he has suffered loss or damage. That is why the stipulation in the guarantee is that the bank will pay without demur or dispute, merely on demand stating that: (i) a breach of terms of the agreement causing loss or damage or its likelihood has occurred or (ii) the petitioner has failed to perform the agreement. Support to this view is lent by a recent Bench decision of this Court in National Building Construction Co. Ltd. v. Ircon International Ltd., (FAO (OS) 193/97, decided on 4 August 1997), wherein it has been observed that the decision of the Supreme Court in General Electric Technical Services Company Inc. Vs. M/s. Punj Sons (P) Ltd. and another, to the effect that the bank cannot be interdicted by the Court at the instance of the party, at whose instance the

bank guarantee was furnished, in the absence of fraud or special equities in the form of preventing irretrievable injustice between the parties does not leave much scope for argument on improper invocation.

21. As noted above, in the present case, the bank did not raise any objection to the invocation and as a matter of fact sent its cheque to respondent No.1 but before the bank could honour the cheque, it was interdicted from remitting the proceeds of the cheque. Thus the instant case falls in the category where the petitioner seeks injunction against the beneficiary as well as the guarantor. In my view the aforesaid contention urged by learned counsel for the petitioner that the bank guarantee was conditional to the beneficiary disclosing to the bank as to how and in what manner the damage had been caused or would be caused even on account of non-performance of the agreement to it and invocation only on the ground that the petitioner "has failed to perform the agreement" is not in terms of the bank guarantee, has to be decided in the light of the contract between the petitioner and respondent No.1 and in this behalf it will be expedient to make a reference to Article 28 of the agreement, providing for furnishing of a performance bond. Article 28.2 of the said agreement reads as follows:

"In the event of contractor failing to honour any of the commitments entered into under this contract and/or in respect of any amount due from contractor to operator, operator shall have an unconditional option under the guarantee to invoke the performance bond and claim the amount from the bank."

22. Under the said clause of the agreement the petitioner gave an unconditional bond to respondent No.1 to invoke the performance bond and claim the amount from the bank in the event of its failure to honour any of the commitments entered into under the contract. The said clause does not speak of any loss or damage which may occasion on account of non-performance of the agreement. In my view in the absence of any stipulation with regard to loss or damage in the said clause, the exercise of power by respondent No.1 under the said clause cannot be faulted with on the ground that the loss or damage, on account of non-performance of the agreement, had not been indicated in the letter invoking the bank guarantee.

23. For the view I have taken, it is unnecessary to deal with the decision of this Court in Puri International (P) Ltd's case (supra), relied upon by learned counsel for the petitioner, which is otherwise clearly distinguishable on facts. In the said case, the Court, after examining the contents of letter invoking bank guarantee, had found that the invocation was not in accordance with the terms of the guarantee, which, as observed above, is not the case here. Similarly, the affronted observations in Hindustan Steel Works Construction Ltd's case (supra) are not attracted in the instant case as I, prima facie, feel that there have been no misrepresentations by the first respondent as alleged by the petitioner.

24. As regards the allegation of fraud made in paras 38 of the petition, wherein it is stated that "the invocation of the bank guarantee is vitiated by fraud of such

egregious nature on the part of the respondent No.1 that it vitiates the entire contract" and in para 39, seemingly attempting to supply particulars of the alleged fraud, it is stated that "respondent No.1 has actively with malafide intent concealed and suppressed the true and correct position from the respondent No.1 apparently in an attempt to unjustly enrich itself to the sum guaranteed by the bank guarantee and thereafter pressurise the petitioner to submit to respondent No.1's illegal terms. This is down-right and ex facie fraud which cannot be permitted by this Court"; no other fact is averred or indicated in the entire petition to show as to how a fraud has been played by respondent No.1 on the petitioner either in entering into the agreement or in securing the bank guarantee of which the bank was aware. The circumstances mentioned in the contentions of learned counsel for the petitioner in support of the plea of fraud (not pleaded in the petition) are neither material nor established and are well controverted in the reply. Assuming for the sake of argument that obtaining permission/clearance of Naval authorities/DRDO was the responsibility of respondent No.1, though, it does not appear to be so from the terms of the agreement, and the said respondent had failed to procure it, can it be said that this action is tantamount to fraud? Obviously the answer has to be in the negative. It would at best be a case of wrongful termination of agreement and for its redressal the petitioner will have its remedy, which, it is understood, the petitioner has availed of by asking for arbitration. Non-performance of the obligation under the contract by any of the parties cannot be equated with the inherent fraud in the contract itself. The contentions raised in support of the plea of fraud are meritless.

25. As regards the question of irretrievable injustice on account of encashment of bank guarantee, it has neither been seriously urged for the petitioner nor anything is placed on record to satisfy the Court that there would be no possibility whatsoever for restitution of the amount so recovered after the disputes between the parties have been adjudicated by arbitration, for which a provision exists in the agreement. If the petitioner feels that the amount under the bank guarantee has been wrongly recovered by the first respondent it will be open to it to prefer a claim before the arbitrators.

26. As a result, I am of the view that the invocation of the bank guarantee - has been in accordance with its terms; the plea of fraud set up in support lacks particulars or proof necessary to interdict encashment of the guarantee. The main petition as also is 9767/96 fail and are accordingly dismissed with costs, quantified at Rs.5,000/-.

Interim order, dated 16 October 1996, made in is 9767/96, is hereby vacated.

Needless to say that the view expressed above, is tentative for the limited purpose of decision in this petition for injunction and shall not be construed as expression of opinion on merits of the controversy between the parties.