(2011) 05 DEL CK 0065

In the Delhi High Court

Case No : FAO (OS) No''s. 67-68 of 2011, C.M. No''s. 2672-73 of 2011 and 3433 of 2011

Fedders Lloyed Corporation Ltd. APPELLANT

Vs

Sportinapayce Infrastructure Pvt. Ltd. and Another RESPONDENT

Date of Decision : 11-05-2011

Acts Referred:
Arbitration and Conciliation Act, 1996 — Section 11
Civil Procedure Code, 1908 (CPC) — Order 29 Rule 1, Order 29 Rule 2

Citation : (2011) 6 AD 238 : (2011) 124 DRJ 137

Hon'ble Judges : M.L. Mehta, J;A.K. Sikri, J

Bench : Division Bench

Advocate : Sandeep Sethi and P.S. Bindra, for the Appellant; Nikhil Rohtagi, for the Respondent

Judgement

M.L. Mehta, J.—This appeal is filed against the impugned order dated 2nd February, 2011 of learned Single Judge in CS(OS) No. 2208/2009, whereby the Appellant''s application being IA No. 14978/2009, under Order XXXIX Rules 1 and 2 Code of Civil Procedure, was rejected and simultaneously application being IA No. 15460/2009, under Order XXXIX Rule 4 CPC of the Respondent No. 1 was allowed.

2. The Appellant/Plaintiff filed a civil suit for declaration, cancellation and mandatory injunction in respect of bank guarantee which was furnished by the Appellant/Plaintiff in favour of Respondent No. 1 for a sum of Rs. 50,00,000/- on 3rd June, 2009. The Respondent No. 1 was awarded a contract by Delhi Development Authority (hereinafter, referred to as "DDA") for construction of swimming pool, training hall, fitness centre and athletic track at Commonwealth Games Village for a total value of Rs. 63 crores. A part of the said work was sub-contracted by Respondent No. 1 to Appellant for a sum of Rs. 6 crores. According to the Appellant, it completed almost 80% of the work and submitted bills in the sum of Rs. 4,46,64,473/- to Respondent No. 1, but the latter released a sum of Rs. 3,38,53,704/- leaving outstanding of Rs. 1.08/- crores which was not cleared

despite repeated requests. A specific request was also made vide letter dated 3rd August, 2009 in this regard.

3. DDA was also allegedly complaining to Respondent No. 1 regarding the slow progress of work on account of lack of planning and because of non-deployment of the agreed financial resources. A specific letter dated 24th July, 2009 was written by DDA complaining the execution of only 40% work as against expected 75%. Eventually, for being dissatisfied with the work carried out by Respondent No. 1, DDA terminated the contract vide letter dated 30th October, 2009. The work which was being performed by the Appellant/Plaintiff was specifically awarded by the DDA to it vide letters dated 12th November, 2009 and 19th November, 2009. It was in this background that Respondent No. 1 sought to encash the bank guarantee.

4. It appears that there were some talks of settlement and since the bank guarantee was about to expire it was got extended by the Appellant/Plaintiff uptill 22nd January, 2010 vide its letter date 16th October, 2009. On account of termination of contract, petition u/s 11 of Arbitration and Conciliation Act was also filed by the DDA for reference of dispute with Respondent No. 1 to arbitration. It appears that since there was no head way in the settlement, Respondent No. 1 invoked the bank guarantee on 17th November, 2009. The Appellant/Plaintiff amended the plaint by incorporating some averments relating to fraud against Respondent No. 1. The Appellant/Plaintiff sought to restrain the Respondents from invoking the bank guarantee on the grounds, namely, fraud, irretrievable injustice and special equity.

5. With regard to fraud, the Appellant/Plaintiff averred that the very basis of getting the work from DDA was based on the fraud committed by Respondent No. 1 since its share capital was merely Rs. 10,00,000/- and it has no reserves, surplus or fixed assets. It had received loans to the tune of Rs. 9.42 crores and had given loans to the extent of Rs. 9.48 crores for the year ending 31st March, 2009 and suffered losses to the tune of Rs. 34,922/- and that if these facts were disclosed to DDA, the latter would not have awarded contract to Respondent No. 1. It was also averred that various other contractors have also not been paid their dues by Respondent No. 1.

6. With regard to fraud, the learned Single Judge recorded finding that these facts cannot be said to constitute fraud because, admittedly, Respondent No. 1 had executed substantial portion of contract allocated to it worth Rs. 63 crores and that admittedly a sum of Rs. 3.36 crores was also received by the Appellant/ Plaintiff from Respondent No. 1. Even the share holding of Rs. 10,00,000/- only would not constitute fraud amounting to the nature of egregious. With regard to the plea of irretrievable injustice and special equity, the Appellant/Plaintiff averred that keeping in view the financial position of Respondent No. 1, if the money of the bank guarantee was released, the Appellant/Plaintiff will suffer irretrievable injustice inasmuch as in the event of it succeeding in the suit it will not be possible to recover the aforesaid amount from Respondent No. 1. It is

averred that since there were also other claimants of Respondent No. 1, the equities existed in favour of the Plaintiff and all such claimants. With regard to irretrievable injustice and special equities, the learned Single Judge recorded that the bank guarantee being an independent contractor could be invoked by Respondent No. 1 irrespective of any dispute that may arise between the Plaintiff and Respondent No. 1. The learned Single Judge held that the bank guarantee being irrevocable as also unconditional, the same was liable to be invoked at the option of Respondent No. 1. The learned Single Judge was of the view that the kind of irretrievable injustice as approved by the Apex Court in the case of Itek Corpn. V. First National Bank of Boston 566 Fed Supp 1210 was not made out in the present case.

7. The impugned order has been assailed on various grounds by learned Counsel for the Appellant/Plaintiff. The submissions as made before us by learned Counsel for the Appellant are more or less the same as made before the learned Single Judge based on the grounds of fraud, irretrievable injustice and special equity. In addition learned Counsel for the Appellant submits that the contract of Respondent No. 1 was terminated by DDA because of no fault of the Appellant/ Plaintiff, but due to mis-planning and inadequate labour by Respondent No. 1. Learned Counsel submits that at no point of time, neither DDA nor Respondent No. 1 ever complained against the progress of work of Appellant/Plaintiff. He submits that the contract came to be terminated only because of the acts of omission or commission of Respondent No. 1. He further submits that the award of contract to the Appellant/Plaintiff by DDA was itself a reorganization of the pace and quality of work done by the Appellant/Plaintiff. Learned Counsel submits that the learned Single Judge in the impugned order has also recorded a finding of fact that DDA cancelled the contract of Respondent No. 1 only in account of mis-planning and delay in execution of project. The learned Single Judge specifically recorded that the cancellation of contract by the DDA cannot be attributed to any act on the part of Plaintiff/Appellant and so the Appellant/ Plaintiff cannot be held responsible for cancellation of contract of Respondent No. 1 by DDA. The learned Counsel submits that the financial position of Respondent No. 1 was poor, in the sense that as per its balance-sheet as on 31st March, 2010 it had secured and unsecured loans of about Rs. 18,30,12,970/- whereas during the same financial year it had incurred losses to the tune of Rs. 14,46,16,640/-. Further its share capital being merely Rs. 10 lakhs and there being no reserves or surplus or fixed assets, if the bank guarantee is permitted to be enchased it shall cause irretrievable injury to the Appellant inasmuch as it will never be able to retrieve the same amount from Respondent No. 1. Learned Counsel also brought to our notice some of the letters purported to have been written by other sub-contractors claiming various amounts from Respondent No. 1 in respect of different works executed by them for the same project. Based on all these pleas and submissions, the learned Counsel for the Appellant/Plaintiff submits that invoking of the bank guarantee needs to be restrained immediately.

8. On the other hand, learned Counsel for Respondent No. 1 submits that what

has been averred and submitted by and on behalf of Appellant/Plaintiff did not call for restraining of invoking the bank guarantee which was unconditional and unqualified. The leaned counsel for Respondent No. 1 relies on the cases, namely, Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another, ; Hindustan Construction Co. Ltd. Vs. State of Bihar and Others, ; Intertoll ICS Cecons O and M Company P. Ltd. Vs. National Highways Authority of India, ; Dwarikesh Sugar Industries Ltd. Vs. Prem Heavy Engineering Works (P) Ltd., and another, ; State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another, and Bolivinter Oil SA v. Chase Manhattan Bank (1984) 1 All ER 351.

9. To discuss the matter further, it may be necessary to examine the bank guarantee furnished by Appellant/Plaintiff in favour of Respondent No. 1. The same has also been reproduced in the impugned order. The relevant portion of the bank guarantee, which has a bearing on our findings, is as follows:

Whereas the Beneficiary and M/s Sportina Payce Infrastructure Pvt. Ltd. Entered into a Agreement dated 06 November 2008 for construction of commonwealth Games Village for common wealth Games Delhi 2010 near Akshardham Temple Off Road No. NH-24, in terms of the said agreement we "The Bank" agree to give this Bank Guarantee on request of M/s Fedders Lloy Corp. Ltd.

This Guarantee is issued subject to the condition that the liability of the Bank under this Guarantee is limited to a maximum of Rs. 50,00,000/- (Rs. Fifty Lacs Only) and this guarantee shall remain in full force up to an can be invoked only by a written demand or claim under this guarantee served on the bank by the beneficiary at the following address Commercial Branch Janpath, New Delhi by way of Registered Post or by hand delivery duly obtaining acknowledgment form "The Bank on or before.

We "The Bank" expressly agree that our liability and obligation under the guarantee:

(a) Shall be absolute, unconditional, irrevocable and payable on a mere demand made by the Beneficiary, without any demur, irrespective of any disputes or differences of whatsoever nature between the beneficiary and Fedders Lloyd Corp. Ltd.

(b) Shall not be discharged released, altered or otherwise effected in any manner by reason of any arrangement or compromise made between the beneficiary and Fedders Lloyd Corp. Ltd.

10. A plain reading of the above portion of the bank guarantee would show that it is not a performance bank guarantee but is an unconditional and irrevocable one. The bank has agreed to pay to the beneficiary, namely, Respondent No. 1 the amount so guaranteed without any demur or protest in case it is so demanded by this Respondent.

11. The question for consideration would be as to whether the averments and

allegations were sufficient enough to restrain invocation of unconditional bank guarantee, The learned Single Judge has referred to various judgments of this Court as also of the Apex Court and is of the view that the plea of fraud that has been set up by the Appellant/Plaintiff cannot be a ground for going to the root of execution of bank guarantee.

12. It is a matter of common knowledge that in the contracts of this nature, as in the instant case, the contractor normally gives performance guarantee to the employer for due fulfillment of its obligation. Normally such bank guarantees are couched in a language which are unconditional bank guarantees whereby the bank undertakes to give money to the beneficiaries on demand, without demur or protest. When such a demand is made the bank is not even permitted to probe into the disputes between the parties.

13. Infact, the principles relating to the bank guarantees have almost been settled from a series of judgments rendered by the Supreme Court from time to time. The position was summarized by the Supreme Court in paras 21 and 22 of its judgment in the case of Dwarikesh Sugar Industries Ltd. Vs. Prem Heavy Engineering Works (P) Ltd., and another, , after taking stock of its earlier judgments. These paras are as follows:

Para 21: Numerous decisions of this Court rendered over a span of nearly two decades have laid down and reiterated the principles which the courts must apply while considering the question whether to grant an injunction which has the effect of restraining the encashment of a bank guarantee. We do not think it necessary to burden this judgment by referring to all of them. Some of the more recent pronouncements on this point where the earlier decisions have been considered and reiterated are Svenska Handelsbanken Vs. M/s. Indian Charge Chrome and others, , Larsen and Toubro Limited Vs. Maharashtra State Electricity Board and others, , Hindustan Steel Workers Construction Ltd. Vs. G.S. Atwal and Co. (Engineers) Pvt. Ltd., , and U.P. State Sugar Corporation v. Sumac International Ltd. 1 (1997) CLT 195. The general principle which has been laid down by this Court has been summarized in the case of AIR 1997 1644 (SC) as follows: (SCC p.574, para 12).

The law relating to invocation of such bank guarantees is by now well settled. When in the course of commercial dealings an unconditional bank guarantee is given or accepted, the beneficiary is entitled to realize such a bank guarantee in terms thereof irrespective of any pending disputes. The bank giving such a guarantee is bound to honour it as per its terms irrespective of any dispute raised by its customer. The very purpose of giving such a bank guarantee would otherwise be defeated. The courts should, therefore, be slow in granting an injunction to restrain the realization of such a bank guarantee. The courts have carved out only two exceptions. A fraud in connection with such a bank guarantee would vitiate the very foundation of such a bank guarantee. Hence if there is such a fraud of which the beneficiary seeks to take the advantage, he can be restrained from doing so. The second exception relates to cases where allowing the encashment of an unconditional bank guarantee would result in irretrievable harm or injustice to one of the parties concerned. Since in most cases payment of money under such a bank guarantee would adversely affect the bank and its customer at whose instance the guarantee is given, the harm or injustice contemplated under this head must be of such an exceptional and irretrievable nature as would override the terms of the guarantee and the adverse effect of such an injunction on commercial dealings in the country.

Dealing with the question of fraud it has been held that fraud has to be an established fraud. The following observations of Sir John Donaldson, M.R. in Bolivinter Oil SA v. Chase Manhattan Bank (1984) 1 All ER 351 are apposite:

...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 the bank''s knowledge. It would certainly not normally be sufficient that this rests on the uncorroborated statement of the customer, for irreparable damage can be done to a bank''s credit in the relatively brief time which must elapse between the granting of such an injunction and an application by the bank to have it discharged.

The aforesaid passage was approved and followed by this Court in U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd., : The second exception to the rule of granting injunction, i.e., the resulting of irretrievable injury, has to be such a circumstance which would make it impossible for the guarantor to reimburse himself, if he ultimately succeeds. This will have to be decisively established and it must be proved to the satisfaction of the court that there would be no possibility whatsoever of the recovery of the amount from the beneficiary, by way of restitution.

14. In the case of State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another, the Supreme Court also clarified the position in the following manner:

The rule is well settled that a bank issuing a guarantee is not concerned with the underlying contract between the parties to the contract. The duty of the bank under a performance guarantee is created by the document itself. Once the documents are in order the bank giving the guarantee must honour the same and make payment ordinarily unless there is an allegation of fraud or the like. The courts will not interfere directly or indirectly to withhold payment, otherwise trust in commerce internal and international would be irreparably damaged. But that does not mean that the parties to the underlying contract cannot settle the disputes with respect to allegations of breach by resorting to litigation or arbitration as stipulated in the contract. The remedy arising ex contract is not barred and the cause of action for the same is independent of enforcement of the guarantee.

15. From the above principles as laid down by the Supreme Court in the

aforesaid cases it comes out to be that subsequent disputes in the performance of contract between the parties do not give rise to cause to issue an injunction against enforcing the guarantee. Though, fraud is made an exception and could be invoked to restrain invocation of bank guarantee, but various conditions to accept such a ground are, viz. (a) fraud has to be of egregious nature; (b) Further, while dealing with the question of fraud it is to be established that it is an established fraud. The evidence relating to this fraud must be clear, both with regard to the fact of fraud and to the bank''s knowledge.

16. In the case of Dwarikesh Sugar (supra) it was also held that while examining the allegations of fraud, the Court is precluded from embarking on the inquiry if by encashment of bank guarantee the beneficiary is trying to take enrichment since the principle of undue enrichment has no application in such cases.

17. The second exception that is available for restraining invocation of bank guarantee is of irretrievable injury which has to be of such circumstances as would make it impossible for the guarantor to reimburse himself, if he ultimately succeeds. Therefore, while examining this exception, the Supreme Court has laid down that the party seeking injunction will have to decisively establish/prove to the satisfaction of the Court that there would be no possibility whatsoever of the recovery of the amount from the beneficiary by way of restitution.

18. Now, coming back to the facts of the case, we are of the considered opinion that all that has been averred and submitted about fraud as a ground seems to be not attracted in the present case. The learned Single Judge has rightly recorded his findings in this regard and we do not see any reason to differ with him. With regard to irretrievable injury, the pleas which are sought to be taken are mainly with regard to the financial conditions of Respondent No. 1 and also demands of some outstanding dues by other contractors from Respondent No. 1.

19. From the entire factual matrix, as has been examined, it is seen that some disputes have arisen between the Appellant/Plaintiff and Respondent No. 1 on one side and also between Respondent No. 1 and the DDA on the other. The disputes have led to the filing of arbitration proceedings by DDA against Respondent No. 1. The present suit has also arisen because of Appellant''s dispute with Respondent No. 1.

As per the principles relating to bank guarantee, as noted above, the type of bank guarantee as executed by Respondent No. 2 bank in favour of Respondent No. 1 was an independent contract not depending upon any dispute that may arise between Appellant/Plaintiff and Respondent No. 1. If the restraint orders are issued, based on the plea that the company entitled to invoke the bank guarantee did not have reserve or surplus, then also the purpose of execution of bank guarantee would get frustrated. That was not the intent or the objective of bank guarantee furnished by the Appellant/Plaintiff in favour of Respondent No. 1. The bank guarantee being unconditional and unqualified was not dependent upon the performance or the financial condition of the parties. The Respondent

No. 1 was within its rights and authority to invoke bank guarantee and the bank was under an obligation to honour the same.

20. Having said, as above, we ought not to have interfered in the impugned order in the normal course. However, keeping in view some peculiar facts, which have emerged in this case as stated hereinabove, we are of the view that some condition is required to be put on the rights of Respondent No. 1 in invoking the bank guarantee. The factors for doing so are: (i) Undisputedly Appellant/Plaintiff submitted bills in the sum of Rs. 4,46,64,473/- to Respondent No. 1, but got release of Rs. 3,38,53,704/-, leaving outstanding of Rs. 1.08/- crores receivable from Respondent No. 1. This has not been controverted by Respondent No. 1 and infact remains uncontroverted till date; (ii) On our asking, learned Counsel for Respondent No. 1 admitted that so far no claim of any kind has been made by Respondent No. 1 against the Appellant/Plaintiff with regard to the said contract; and (iii) there is some prima facie evidence regarding outstanding claims of other contractors against Respondent No. 1. These factors not only make the move on the part of the Respondent No. 1 to invoke the bank guarantee a suspect, but more importantly show that there is a possibility of the Appellant/Plaintiff succeeding in establishing some monetary claim against the Respondent No. 1 resulting in the refund of bank guarantee amount as well. Even that alone would not have persuaded us to impose any condition. However, this assumes great importance and significance when we examine the peculiar financial health of the Respondent No. 1 in conjunction. The reflection of the Balance Sheet for the period ending 31st March, 2009 showed Respondent No. 1 having suffered some losses. This financial health was weakened considerably as can be discussed from the balance sheet for the period ending 31st March, 2010. In this year Respondent No. 1 had secured and unsecured loans of about Rs. 18,30,12,970/- and had incurred losses to the tune of Rs. 14,46,16,640/-. Further its share capital being merely Rs. 10 lakhs and there being no reserves or surplus or fixed assets, the financial position of Respondent No. 1 is apparently not sound but very shaky. These peculiar facts appear to be the cause of reasonable apprehension of the Appellant/Plaintiff and it seems to be rightly well founded, in as much as in the event of Appellant/Plaintiff succeeding in the present suit, the restitution may be difficult though not impossible given the overall state of affairs.

21. Influenced by all that has been noted above, we are tempted to put some reasonable condition on the right of Respondent No. 1 in invoking the bank guarantee against Appellant/Plaintiff to ensure that the right of latter remains protected in the event of its succeeding in the present suit.

This unusual course is adopted, in the peculiar facts, based on equity and in the interest of justice.

22. In the given circumstances, we are of the considered view that the impugned order needs to be maintained with a modification that Respondent No. 1 shall be entitled to invoke the bank guarantee, subject to its furnishing security of the same amount to this Court in terms of this order as indicated above. Respondent

No. 1 will be required to furnish security of the said amount to the satisfaction of the Registrar General of this Court. This security shall remain alive till the final disposal of the suit of the Appellant/Plaintiff.

23. The present appeal as well as all the pending applications, being C.M. Nos. 2672-73/2011 & C.M. No. 3433/2011, stand disposed of accordingly.

