

(2005) 11 DEL CK 0113

In the Delhi High Court

Case No : OMP No. 213 of 2005 and is No. 5872 of 2005

Hindustan Construction Co. Ltd. and Another

APPELLANT

Vs

Satluj Jal Vidyut Nigam Ltd.

RESPONDENT

Date of Decision : 24-11-2005

Acts Referred:

Arbitration and Conciliation Act, 1996 — Section 9

Civil Procedure Code, 1908 (CPC) — Order 39 Rule 1, Order 39 Rule 2, 151

Citation : AIR 2006 Delhi 169 : (2006) 1 ARBLR 16 : (2006) 1 CTLJ 239

Hon'ble Judges : Swatanter Kumar, J

Bench : Single Bench

Advocate : Ashok K. Desai, Samir Parekh, Pritesh Kapur, Sonali Basu, D.P. Mohanty and Sumeet Lall, for the Appellant; Mukul Rohatgi Uttam Datt and Neeraj Malhotra, for the Respondent

Final Decision : Disposed Off

Judgement

Swatanter Kumar, J.—The Satluj Jal Vidyut Nigam Limited, formerly NJPC Ltd, had engaged M/s. Hindustan Construction Company Limited-applicants for completion of a part of civil work for raising head tunnel Stn. 1642m to Stn. 2729m including shaft to its on-going project of hydro-electric project in terms of contract No. 2.2 dated 26th May, 1993. Under the terms of this contract, the applicants had to furnish one performance and 17 retention money guarantees under clause 10 and clause 60 of the general conditions of contract. The said bank guarantees relating to performance and retention money respectively were required to be returned to the petitioners after 12 months from the date of substantial completion of works. These bank guarantees were furnished by the applicants and were accepted by the respondent at the relevant time. It is the case of the applicants that, during the currency of the contract under various interim payment certificates or final and binding decisions of the Disputes Review Board (DRB), the respondent had paid to the petitioners sums aggregating to Rs. 53.76 crores under various heads unconditionally and without protests. The payments were made between 15.11.1995 and 08.04.2002. Upon completion of

the work, a certificate of substantial completion was issued by the Engineer in charge on 06.08.02. As per the terms of the contract, as amended from time to time, the bank guarantees were to be returned to the applicants on 07.07.2003, i.e., after one year of the maintenance period which commenced on 8th July, 2002. However, the respondent without giving any notice, arbitrarily and illegally purported to invoke all the said bank guarantees furnished by the applicants on 07.07.2003, i.e., the last date for that purpose. The letter dated 07.07.2003 reads as under:

The Chief Executive Officer State Bank of India Overseas Branch New Delhi.
Subject: Encashment of Bank Guarantee No. 99/202 dated 21.10.1999. Dear Sir, This has reference to the Bank Guarantee No. 99/202 dated 21 October, 1999 extended vide letter dated 16th Dec. 1999, and its subsequent amendment dated 14 Jan, 2003, issued by your Frankfurt Branch on behalf of Joint Venture of M/s IMPREGILO S.P.A. 120099.Sesio San Giovanni (Milano)-Italy and M/s Hindustan Construction Co. Ltd. Mumbai 400 038, in favor of Satluj Jal Vidyut Nigam Ltd. (formerly Nathpa Jhakri Power Corporation)Power Corporation Ltd.) for INR 230,427,162 (Indian Rupees Two hundred thirty million four hundred twenty seven thousand one hundred sixty two) only US \$ 2,435,522 (US Dollars two million four hundred thirty five thousand twenty two only and four thousand seven hundred seventy seven only) (i.e. equivalent EURO 1,446,314.19) (EURO One Million Four Hundred Forty Six Thousand Three Hundred Fourteen Point One Nine Only) The provision of Bank Guarantee provides that serving of the Notice for Invocation of the above-said Bank Guarantee will construe as valid notice served on your Frankfurt Branch i.e. issuing branch.

With issue of this letter, we hereby invoke Bank Guarantee and raise our demand for the full amount of above-mentioned Bank Guarantee amounting to INR 230,427,162 (Indian Rupees two hundred thirty million four hundred twenty seven thousand one hundred sixty two only), US \$ 2,435,522 only (US Dollars two million four hundred thirty five thousand five hundred twenty two only) and It. Lira 2,800,454,777 (Italian Lira two billion eight hundred million four hundred four thousand seven hundred seventy seven only) (i.e. equivalent EURO 1,446,314.19) (EURO One Million Four Hundred Forty Six Thousand Three Hundred Fourteen Point One Nine Only).

The amount of INR 230,427,162 (Indian Rupees Two hundred thirty million four hundred twenty seven thousand one hundred sixty two).

US \$ 2,435,522 (US Dollars two million four hundred thirty five thousand twenty two only and four thousand seven hundred seventy seven only)

It. Lira 2,800,454,777 (Italian Lira two billion eight hundred million four hundred four thousand seven hundred seventy seven only)

EURO 1,446,314.19) (EURO One Million Four Hundred Forty Six Thousand Three Hundred Fourteen Point One Nine Only)

is to be credited immediately to our Current Account No. 01000001047 of Satluj Jal Vidyut Nigam Ltd. with State Bank of India, CAG Branch, Barakhamba Road, Vijya Building, New-Delhi, India, under intimation to us.

Thanking you, Yours faithfully, For & on behalf of Satluj Jal Vidyut Nigam Ltd.
(O.N. Singh) Director (Finance)

2. The payments were made to the petitioners from time to time including under the decisions of the DRB. The respondent in an arbitrary manner, that too for the first time, stated that some payments had been made erroneously and were liable to be recovered. The threat of invocation had already been made in terms of the letter dated 07.07.2003 and in view of the unreasonable threat and duress applied by the respondent the applicants submitted an undertaking on 9th July, 2003 stating that performance was not to be considered complete till such time advance ad hoc payments remain unadjusted, and that the bank guarantees would be kept in force and further that they could invoke the bank guarantees without need to prove or show grounds for such invocation. In view of the undertaking submitted by the petitioners, encashment of the bank guarantee was put on hold by the respondent and vide letter dated 20th September, 2003, the banks were informed accordingly by the respondents. It is specifically pleaded by the applicant that before the original time for completion of contract was to expire, i.e., 23-04-1998, at the instance of the World Bank, which was funding the Project, respondent appointed a renowned firm of consultants to examine the issue of extension of time. This was done particularly because the respondents conveyed their difficulty in settling the claims on the ground that their officers were not having the requisite experience and skill and were not conversant in handling such claims based upon FIDIC conditions. On the recommendation of Consultants, respondents granted to the petitioner an interim extension of time of 25 months, i.e., an extension up to 30th June, 1997 and it was thereafter that the interim payment of Rs. 35.98 crore was also released by the respondents as partial compensation of additional cost arising from the prolongation of the works. Subsequently, the respondents unilaterally set up an internal Claims Review Committee and sought to reduce the additional time and additional compensation awarded to the petitioner. This was a mala fide act on the part of respondents and without giving any opportunity to the applicant, they decided to deviate from the report which was submitted by an expert consultant concern of international repute. The petitioners, in terms of modified clause 67 of the General Conditions of Contract, made a protest and asked for the disputes to be referred, in addition to the earlier disputes, to the DRB, which was constituted in terms of the contract. The procedure of detailed hearing and opportunity to both the parties was followed by the said Board, which gave its detailed report with the following conclusions:

On an incisive analysis of delays under individual heads and of the impacts on time for completion, the ADRB considers the following as the entitlements of NJJV:

1.Extension of time as per Clause 44 of the GCC of 50.53 months, i.e., up to 8th July, 2002.

2.Extension of time for the purpose of compensation of 38.04 months, i.e., up to 25th June 2001.

3.EOT related cost compensation for 38.04 months based on actual costs of various items.

3. In view of the above, applicants were entitled to the grant of extension as well as to various benefits in relation thereto. On the other hand, it was held that the applicants were entitled to Rs. 41 crore over and above Rs. 35.98 crore already paid by the respondents and it was also held by the Board that the applicants were not liable for any liquidated damages. However, vide letter dated 05.04.2005, a part of the findings recorded by the Board was not accepted by the respondents and they intended to invoke the arbitration clause. The relevant part of the letter dated 21st April, 2004 reads as under:

It is intimated that the final recommendation of the ADRB on the claim for Time extension and Cost Compensation are not acceptable to SJVN as such. Therefore, SJVNL invokes arbitration under para 1 of Clause 67 of general conditions of contract on the points/issues which are not acceptable to SJVNL."

4. The petitioner replied to the said letter on 28th April, 2005, pointing out that until the points/issues raised are finally decided by the arbitral forum, the recommendations of the Board are pro tem binding on the parties and, as such, no steps should be taken to prejudice the interest of the petitioner by encashment of the bank guarantee. The respondents intended to claim liquidated damages of Rs. 73.44 crore, being the 10 per cent of the contract value, in addition to the claim of Rs. 35.98 crore, which was paid as ad hoc amount to the petitioner/applicant. This was so raised by the respondents vide their letter dated 07/06/2005. The respondents claimed totally a sum of Rs. 104 crore and they were threatening to invoke the bank guarantees amounting to Rs. 123.97 crore. It is also the case of the applicant that various extensions, as prayed by the applicants, were granted by the respondents except on the last occasion in the year 1998 and in view of the findings recorded by the Board, the respondents cannot be permitted to invoke the bank guarantees in a most arbitrary method, which is opposed to the specific terms of the contract as it would cause serious prejudice to the interest of the petitioners. The respondent themselves have accepted the decisions of the Board in regard to part of the extended period while other part is being questioned by the said respondent without any basis and justification. The applicants had extended the bank guarantees as and when demanded for by the respondent. After the bank guarantees had been extended by the applicants, the respondents themselves have written a letter of encashment of bank guarantee issued on 7th July 2003 and this was done on the basis of an undertaking given by Mr. Gautam Ray on behalf of the applicants asking for the confirmation that the validity of the bank guarantee is extended up

to 23rd July, 2004. The respondents themselves wrote to the applicant that the bank guarantees issued against retention money were to expire on 31st May, 2005 and keeping in view the undertaking given, the validity of the bank guarantees should be extended minimum for a period of three months and the respondents be informed accordingly. This renewal of bank guarantees was submitted by the applicants vide their letter dated 12th May, 2005 and it was stated that the bank guarantees have been extended till 30th September, 2005.

5. In the light of the averments made above by the applicants and while relying upon the recent judgments of Courts, it is prayed on behalf of the petitioners in the present petition u/s 9 of Arbitration and Conciliation Act, 1996 (hereinafter referred to as the Act) that the respondent be restrained from encashing the bank guarantees bearing (No. 900/5204, 900/5125, 900/5203, 900/5260, 900/5346, 900/5408, 900/5420, 900/5430, 900/5454, 900/5468, 900/5484, 900/5485, 900/5559, 900/5574, 900/5591, 900/5640 and 900/5665 issued by Bank San Paolo IMI SPA and No. 99/202 issued by State Bank of India, Frankfurt Branch,) during the pendency of the arbitral proceedings, which, in fact, have already been invoked by the parties, amongst others, mainly on the following grounds:

(a) The invocation of bank guarantees by the respondents is intended to overreach the adjudicative process, provided under the terms of the agreement. This is a fraudulent attempt on the part of the respondent;

(b) The invocation of bank guarantees is contrary to the terms of the bank guarantee;

(c) The facts and circumstances of the case clearly demonstrate special equities in favor of the petitioners so as to justify grant of an injunction order; and

(d) The petitioners shall suffer irretrievable injustice and injury in the event the bank guarantees are permitted to be encashed.

6. Besides the above submissions it is also the contention of the applicants that in similar matters where the respondents were invoking similar bank guarantees by adopting the same methodology, the Courts have already granted interim stay. In this regard learned counsel appearing for the petitioners has heavily relied upon the judgment of this court in the case of Jaiprakash Hyundai Consortium v. Satluj Jal Vidyut Nigam Ltd., OMP No. 251/2003 decided on February 25, 2003, where the Court held as under:-

This position was reiterated with approval by the Supreme Court in subsequent cases i.e. Dwarikesh Sugar Industries Ltd. Vs. Prem Heavy Engineering Works (P) Ltd., and another, and in Daewoo Motors India Ltd. Vs. Union of India (UOI) and Others, . In the last case the Supreme Court held that for encashment of bank guarantee the bank cannot have any valid resistance, except of course, in case of fraud. The bank guarantee furnished by the Bank is an unconditional and absolute bank guarantee. Therefore, the bank has not case to resist the

encashment of the bank guarantees. The Supreme Court further held that it is true that the bank guarantees has to be read in conjunction with the terms of the contract but when the bank guarantee itself is in absolute terms, the agreement between the company and the first respondent would be of no avail to the bank.

17. Mr. R.K. Anand, learned senior counsel representing the petitioner has not and perhaps could not possibly dispute the above legal proposition but he has strongly argued that the said legal position has not application to the facts and circumstances of the present case more particularly so because firstly the respondent has not yet approached the bank to enforce the bank guarantees and obtaining the payment thereof but vide a communication dated 30.5.2003 has only threatened to do so in case the amount of ad hoc payment received by the petitioner is not restored to them. This factual position is borne out from the record and this explains the reason why the bank has not been arrayed as a party in the present proceedings. Therefore, the role of the bank in accepting the request of the respondent or otherwise has not yet come into picture, though the application of the legal position to the facts of the present case cannot be denied.

18. This Court has noted in detail various conditions subject to which the respondent had released various amounts of ad hoc payment to the petitioner and the conditions subject to which the petitioner was to refund the said payment back to the respondent. One of the conditions was that the refund would be sought by the respondent only after final adjudication of the claims between the parties. Admittedly as on date, the claims of the petitioner and counter claims have not been finally adjudicated and the same are pending before the DRB and ADRB and the extent of those claims is stated to be more than Rs. 300 crores. During the hearing of the petition, the Court was informed that vide an award dated 8.12.2004 the ADRB has awarded a sum of Rs. 68.49 crores in favor of the petitioner/contractor towards EOT cost under contract along with interest @ 10% p.a. compounded monthly for the extended period from 1.1.1998 to 31.12.2002 and simple interest @ 10% on the above amount after 31.12.2002. This is a significant development and has a great bearing on the question with which we are concerned in the present proceedings i.e. the right of the respondents to invoke the performance guarantees and retention money bank guarantees furnished by the petitioner. Assuming for the sake of arguments that the respondents have right to enforce the bank guarantees in view of their absolute and unconditional nature and having regard to the terms and conditions of the contract, still the award of ADRB has brought a significant change in the situation because as per respondent's own case, they have no other money of the petitioner lying with them, except the amount of bank guarantees, to fall back for the recovery of the amount of ad hoc payment made to the petitioner. In fact, on earlier occasion the respondent has given a credit of about Rs. 3.00 crores to the petitioner on the basis of an earlier award and adjusted the said amount towards ad hoc payment thereby reducing the net payable amount to Rs. 53.12 crores from 56.32 crores. What it would show? It would show that the respondent had agreed to adjust the amount of ad hoc payment received from

the petitioner from any amount payable by them to the petitioner under any award. Today the petitioner has an award of more than Rs.68.00 crores with interest in their favor and Therefore any haste on the part of the respondent to enforce the bank guarantees furnished by the petitioner is not understandable.

7. It is apparent that the above decision certainly helps the applicants to a great extent. It is clear from the record before the Court that the applicants had raised claims worth Rs.115 crores out of which Rs. 53 crores have been paid and the dispute of the applicants remain for the balance amount of Rs. 62.85 crores. The applicants had furnished a bank guarantee to the extent of 10%, in terms of the contract between the parties, which is still alive. The applicants had also furnished a performance guarantee. The main dispute between the parties relates to extension of period. The applicants claimed extension of 50.53 months out of which 39.97 month's extension was accepted. The claim of the applicants was partially accepted by the respondents themselves, while the other contentions of the applicants have been accepted by the Disputes Review Board (DRB). The respondent invoked the bank guarantees for the first time, on 7th July, 2003.

8. It is the pleaded case of the applicants that they had in terms of the contract completed the work satisfactorily and the period of maintenance was to end on 8th July, 2003, but one day prior to the expiry of the said period i.e. on 7th July, 2003 the respondents invoked all the bank guarantees furnished by the petitioners amounting to a total of Rs.123.97 crores. Being compelled and having been left with no alternative, the applicants accepted the conditions imposed by the respondent and submitted an undertaking on 9th July, 2003, as per the dictate of the respondent. Resultantly, the bank guarantees were not encashed, however, they were extended. Even in relation to performance security bank guarantee which was due to expire on 23rd July, 2004 and retention money bank guarantees which were due to expire on 18th July, 2004, the bank guarantees were, in terms of the directions of the respondent kept alive. It was even thereafter that the request for extension, as already noticed, was accepted by the respondent and this was to the extent of 39.97 months, and for the remaining period of 10.56 months the request was declined. The respondents insisted on imposition of liquidated damages, despite the fact that the decision of ADRB was clear that there was no delay. The respondents, as late as on 7th May, 2005, had asked the applicants to extend the bank guarantees, though they were initially invoked as back as on 7th July, 2003. In response to this, the applicants have been extending the bank guarantees, which are stated to be in force, even as of today.

9. The Contractor in terms of Clause 67 had the right to approach the Engineer in charge on any matter in connection with, or arising out of the contract, or for carrying out of the work. The request of the Engineer in charge was to be decided and instructions given within a period of 30 days of such request. If such a decision was against or if the Engineer in charge failed to give his instructions

and decisions, the Contractor had a right to file a written appeal with the CMD, NJPC (renamed as SJVNL), stating clearly and in detail, the basis for objection and CMD was to consider the appeal and convey his decision in writing to the contractor. If the contractor was still dissatisfied with this decision, then within a period of 15 days of the receipt of this decision of the CMD, the Contractor was to convey his intention to refer the matter to the Dispute Review Board (DRB) and within 15 days was to formally file an appeal before the Board. The Board was to adopt its own procedure and give its decision. The dispute involving 50 millions shall be binding on NJPC and the Contractor and in the event the disputes exceeds the said amount and any of the parties is dissatisfied, they could invoke the arbitration proceedings within 30 days thereafter with their intention to refer the matter to arbitration, failing which the view and decision of DRB would become final.

10. The learned counsel appearing for the applicants while relying upon the judgments in the cases of Hindustan Construction Co. Ltd. Vs. State of Bihar and Others, and Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another, has emphasized that the respondent has acted contrary to the terms of the contract and the prescribed performance period having not expired, they have no jurisdiction to encash the bank guarantees and they are causing irretrievable injustice and injury to the plaintiffs/applicants by invoking those guarantees. In fact, such actions, if permitted to mature would entirely frustrate the determinative findings recorded by the prescribed Forums. All this being a fraudulent act of the respondents, they would be liable to be enjoined and the applicants would be entitled to the protection by grant of an interim order.

11. On the contrary, the learned counsel appearing for the respondent while relying upon the judgments in Daewoo Motors India Ltd. Vs. Union of India (UOI) and Others, Federal Bank Ltd. Vs. V.M. Jog Engineering Ltd. and Others, Dwarikesh Sugar Industries Ltd. Vs. Prem Heavy Engineering Works (P) Ltd., and another, AIR 1997 1644 (SC) , Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another, and a judgment of Delhi High Court in the case of Neeman Medical International v. Dr. Guillermo Rodriguez Gomez and Ors. in CS(OS) No. 2193/2003 dated 13th August, 2004 strongly contended that bank guarantee is an independent contract between the beneficiary and the bank. The bank guarantee is unconditional and the respondent has already invoked the same, thus, the obligation on the part of the bank to pay the amount on demand is absolute and the case of the applicants does not fall in the exceptions carved out in the case of AIR 1997 1644 (SC) . It is also contended that the terms of the bank guarantee have to be examined with the letter invoking the bank guarantee and reference to other documents would be unnecessary. The petitioners have not pleaded any fraud in connection with the execution of the bank guarantee or the principal contract and the respondent has invoked the bank guarantee in its terms. The commitment of the bank has to be honoured free from the interference by the court and in any case, the case of the petitioners does not fall even in the classes stated by the Supreme Court in the case of Hindustan

Steelworks Construction Ltd. (supra). While relying upon this judgment, it is also contended that even if the disputes have been referred to arbitration and are pending adjudication then it cannot be stated that amounts are not due and payable by the contractor to the respondent until pronouncement of the award.

12. The various judgments relied upon by the learned counsel appearing for the parties would show that the law in relation to encashment of bank guarantee has attained wider dimensions with the passage of time. Originally, the only exception carved out to encashment of bank guarantee unconditionally was, fraud. However, subsequent judicial pronouncements have extended this scope by adding other class of cases which would fall in this exception - Cases of irretrievable injury, fraud, extraordinary special equities and invocation of bank guarantee being not in terms of the bank guarantee itself. It is very difficult to draw any straitjacket formula which would universally apply to all the cases. The Court would have to examine each case in order to find out whether the case falls in any or more of the afore-stated classes.

13. In the case of Hindustan Steelworks Construction Ltd. (supra), the Supreme Court stated the principle that in case of an unconditional bank guarantee, the nature of obligation of the bank is absolute and not dependent upon any dispute or proceeding between the party at whose instance the bank guarantee is given and the beneficiary. The only two exceptions were - fraud, which was not pleaded in that case, and the other was special equities. Special equities were claimed on the basis as to who had committed breach of the contract. Determination of disputes was stated to be not a factor which would be sufficient to make the case as exceptional case justifying interference by the court restraining invocation of the bank guarantee.

14. In the case of Ansal Engineering Projects Ltd. Vs. Tehri Hydro Development Corporation Ltd. and Another, , the Supreme Court further added the principle of irreparable injury by proof of special equity to the existing two classes of cases where the court could restrain the encashment of a bank guarantee. It was also stated that at the stage of invocation of bank guarantee, the need for final adjudication and decision on the amount due and payable by the petitioner would not be a condition precedent as it would run contrary to the terms of the special contract i.e. the bank guarantee.

15. In the case of UP State Sugar Corporation (supra), the Supreme Court after detailed discussion of the law on the subject while spelling out the principles guiding invocation of bank guarantee and the circumstance where the court would or would not grant an injunction held as under:-

There are only two exceptions to this rule. The first exception is a case when there is a clear fraud of which the bank has notice. The fraud must be of an egregious nature such as to vitiate the entire underlying transaction. Explaining the kind of fraud that may absolve a bank from honouring its guarantee, this Court in the above case quoted with approval the observations of Sir John

Donaldson, M.R. In *Bolivinter Oil SA v. Chase Manhattan Bank* (1984) 1 All ER 351 : (at SCC p. 197)

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 charged.

This Court set aside an injunction granted by the High Court to restrain the realisation of the bank guarantee.

13. The same question came up for consideration before this Court in *Svenska Handelsbanken Vs. M/s. Indian Charge Chrome and others*, . This Court once again reiterated that a confirmed bank guarantee/irrevocable letter of credit cannot be interfered with unless there is established fraud or irretrievable injustice involved in the case. Irretrievable injury has to be of the nature noticed in the case of *Itek Corpn. v. First National Bank of Boston* 566 F S 1210. On the question of fraud this Court confirmed the observations made in the case of *U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd.*, and stated that the fraud must be that of the beneficiary, and not the fraud of anyone else.

14. On the question of irretrievable injury which is the second exception to the rule against granting of injunctions when unconditional bank guarantees are sought to be realised the court said in the above case that the irretrievable injury must be of the kind which was the subject-matter of the decision in the *Itek Corpn.* Case 566 FS 1210. In that case an exporter in USA entered into an agreement with the Imperial Government of Iran and sought an order terminating its liability on stand by letters of credit issued by an American Bank in favor of an Iranian Bank as part of the contract. The relief was sought on account of the situation created after the Iranian revolution when the American Government cancelled the export licenses in relation to Iran and the Iranian Government had forcibly taken 52 American citizens as hostages. The US Government had blocked all Iranian assets under the jurisdiction of United States and had cancelled the export contract. The Court upheld the contention of the exporter that any claim for damages against the purchaser if decreed by the American Courts would not be executable in Iran under these circumstances and realisation of the bank guarantee/letters of credit would cause irreparable harm to the plaintiff. This contention was upheld. To avail of this exception, Therefore, exceptional circumstances which make it impossible for the guarantor to reimburse himself if he ultimately succeeds, will have to be decisively established. Clearly, a mere apprehension that the other party will not be able to pay, is not enough. In *Itek case* 566 FS 1210 there was a certainty on this issue.

Secondly, there was good reason, in that case for the Court to be prima facie satisfied that the guarantors i.e. the bank and its customer would be found entitled to receive the amount paid under the guarantee.

15. Our attention was invited to a number of decisions on this issue/ among them, to Larsen and Toubro Limited Vs. Maharashtra State Electricity Board and others, and Hindustan Steel Workers Construction Ltd. Vs. G.S. Atwal and Co. (Engineers) Pvt. Ltd., as also to National Thermal Power Corporation Ltd. Vs. M/s. Flowmore Private Ltd. and another, . The latest decision is in the case of State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another, where this Court has summed up the position by stating: (SCC p.741, para 13)

The rule is well established 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 contractu is not barred and the cause of action for the same is independent of enforcement of the guarantee."

The other recent decision is in Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another,

16. Clearly, Therefore, the existence of any dispute between the parties to the contract is not a ground for issuing an injunction to restrain the enforcement of bank guarantees....

16. In the case of Dwarikesh Sugar Industries Ltd. v. Prem Heavy Engineering works (P) Ltd. and Anr. (supra), the Supreme Court held as under:-

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 AIR 1997 1644 (SC) The general principle which has been laid down by this Court has been summarised in the case of AIR 1997 1644 (SC)

The law relating to invocation of such bank guarantees is by now well settled. When 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 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, CA 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.*, .

22. 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.

17. In the case of *Hindustan Construction Co. Ltd.* (supra), the Supreme Court while specifying the need for invoking the bank guarantee strictly as per terms of the bank guarantee and by the authority competent to do so held as under:-

8. Now, a bank guarantee is the common mode of securing payment of money in

commercial dealings as the beneficiary, under the guarantee, is entitled to realise the whole of the amount under that guarantee in terms thereof irrespective of any pending dispute between the person on whose behalf the guarantee was given and the beneficiary. In contracts awarded to private individuals by the Government, which involve huge expenditure, as for example, construction contracts, bank guarantees are usually required to be furnished in favor of the Government to secure payments made to the contractor as "advance" from time to time during the course of the contract as also to secure performance of the work entrusted under the contract. Such guarantees are encashable in terms thereof on the lapse of the contractor either in the performance of the work or in paying back to the Government "advance", the guarantee is invoked and the amount is recovered from the bank. It is for this reason that the courts are reluctant in granting an injunction against the invocation of bank guarantee, except in the case of fraud, which should be an established fraud, or where irretrievable injury was likely to be caused to the guarantor. This was the principle laid down by this Court in various decisions. In *U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd.*, the law laid down in *Bolivinter Oil SA v. Chase Manhattan Bank* (1984) 1 All ER 351 was approved and it was held that an unconditional bank guarantee could be invoked in terms thereof by the person in whose favor the bank guarantee was given and the courts would not grant any injunction restraining the invocation except in the case of fraud or irretrievable injury. In *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.*, , *National Thermal Power Corporation Ltd. Vs. M/s. Flowmore Private Ltd. and another*, *State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another*, , *Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another*, as also in AIR 1997 1644 (SC) the same principle has been laid down and reiterated.

9. What is important, Therefore, is that the bank guarantee should be in unequivocal terms, unconditional and recite that the amount would be paid without demur or objection and irrespective of any dispute that might have cropped up or might have been pending between the beneficiary under the bank guarantee or the person on whose behalf the guarantee was furnished. The terms of the bank guarantee are, Therefore, extremely material. Since the bank guarantee represents an independent contract between the bank and the beneficiary, both the parties would be bound by the terms thereof. The invocation, Therefore, will have to be in accordance with the terms of the bank guarantee, or else, the invocation itself would be bad.

21. As pointed out above, bank guarantee constitutes a separate, distinct and independent contract. This contract is between the Bank and the defendants. It is independent of the main contract between HCCL and the defendants. Since the bank guarantee was furnished to the Chief Engineer and there is no definition of "Chief Engineer" in the bank guarantee nor is it provided therein that "Chief

Engineer" would also include Executive Engineer, the bank guarantee could be invoked by none except the Chief Engineer. The invocation was thus wholly wrong and the Bank was under no obligation to pay the amount covered by the "performance guarantee" to the Executive Engineer.

18. Still further, in the case of Federal Bank Ltd. (supra), the Supreme Court while cautioning the court not issuing injunction restraining encashment of a bank guarantee, specified the same principles i.e. fraud and irretrievable damage as exception to the Rule and further clarified that relationship between the bank issuing letter of credit or paying bank is that of principal and agent. It was affirmed that to bring the case within the exception of fraud, the averment should be clear and that there was knowledge to the bank of the fraud played.

19. In the case of Daewoo Motors India Ltd. (Supra), the Supreme Court held that for encashment of bank guarantee, the bank cannot have any valid resistance, except of course, in a case of fraud. The bank guarantee furnished by the bank is an unconditional and absolute bank guarantee. It was also stated that once it becomes apparent that there was default to fulfill its obligation as specified in the bank guarantee, invocation of bank guarantee would be proper.

20. On the analysis of the above law laid down by the Supreme Court in its different judgments, it is clear that injunction against encashment of bank guarantee is an exception and not the rule. Cases of such exceptions would have to be evidenced by documents and pleadings on record and compulsorily should fall within any of the following limited categories:-

i) If there is a fraud in connection with the bank guarantee which would vitiate the very foundation of such guarantee and the beneficiary seeks to take advantage of such fraud.

ii) The applicant, in the facts and circumstance of the case, clearly establishes a case of irretrievable injustice or irreparable damage.

iii) The applicant is able to establish exceptional or special equities of the kind which would prick the judicial conscience of the court.

iv) When the bank guarantee is not invoked strictly in its terms and by the person empowered to invoke under the terms of the guarantee. In other words, the letter of invocation is in apparent violation to the specific terms of the bank guarantee.

21. The exceptional cases would be few but it could never be stated as an absolute proposition of law that under no circumstances the court could injunct encashment/invocation of a bank guarantee which might have been furnished by a party as an independent contract. A beneficiary is not vested with an unquestionable or unequivocal legal right to encash the bank guarantee on demand. The obligation of the bank furnishing the bank guarantee to pay would be subject to a limited exceptional circumstance afore-noticed. As a matter of rule, the bank would be under obligation to encash the bank guarantee, once it is

invoked in its terms. The exceptions afore-noticed are merely indicative of the kind of cases where the court may injunct encashment of a bank guarantee. It is neither possible nor permissible to exhaustively classify the cases where the court would not interfere and where the court would judicially intervene in such matters. Every case would have to be decided keeping in view its peculiar facts and circumstances. Despite the principal contract and bank guarantee being *Ejusdem negotii*, the bank guarantee is an independent and self-contained contract enforceable on its own terms. Except in the exceptional cases where definite material is available before the court to *prima facie* satisfy itself that on the basis of the pleadings of the parties; documents supporting has such a plea; the case falls in one or more of the categories afore-indicated, the bank guarantee would be encashable *per se*. It has an obligation which is not dependent upon adjudication of main disputes. The concept of irretrievable injustice, or damages, or special equities would come into play where the parties to a contract having been provided with internal adjudicative mechanism, attempts to frustrate results of such an internal adjudication by recourse to encashment of bank guarantee, particularly when under the terms and conditions of the contract, including the terms of the guarantee, such determination is "final", of course subject to the limitations spelled out in such contracts. An attempt to over-reach the process of adjudication with intent to cause irreparable prejudice to the other side would be a circumstance which would influence the decision or tilt the special equities in favor of the applicant before the Court.

22. In light of the above principles, it will be now proper to revert back to the facts of the present case. There is no dispute to the fact that the contracted work had been completed by the applicant. Correspondence have been placed on record to show that the work had been completed and the performance period had commenced which was to end on 8th July, 2003. It can also not be disputed that the bank guarantee in question was sought to be invoked just a day prior to the expiry of the performance period.

23. Firstly, the respondent had invoked the bank guarantees vide letter dated 7th July, 2003 which were admittedly put on hold vide letter dated 20th September, 2003. The said letter reads as under:-

"No. SJVNL/F&A/A-IV/2003/ Dated:20.09.2003 To Bank Sao Paolomi Piazza Cordusio. 2 20121 Milan (Italy) Fax NO. 00390288046598 Sub.: Confirmation of Bank Guarantee-reg: Dear Sir, The letter of encashment of BGs issued by the Director (F), SJVNL vide letter No. SJVN DF-503.2445 to SJVN.DF-5.03-2461 dated 07.07.2003 was put on hold through letter No. DF-5-2462(B)-03 dated 09.07.03. In this regard, it is to intimate that, such action was taken on the basis of an undertaking given by Sh. Gautam Ray (Authorised Signatory of NJJV), A-137, defense Colony, New Delhi-110024 to defer the decision of invocation of Bank Guarantees.

A copy of said undertaking is enclosed for your reference and record.

Kindly acknowledge receipt of the same & also confirm the validity of BGs atleast up to 23rd July, 2004 as per the enclosed statement through return fax on any of the following fax Nos. 009117825234122, 00911782275549.

An early confirmation is solicited.

Thanking you, Yours faithfully, For & on behalf of SJVN Ltd. (S.N. Ghosh) Dy. G.M.

24. The respondent had also called upon the applicants to submit an undertaking which was submitted on 9th July, 2003 stating that the Contractor's performance under the contract shall not be considered as complete till such time the advance ad-hoc payments mentioned above remained unadjusted or unresolved. It was also stated that SJVNL shall have the full liberty to invoke the bank guarantees and to recover the advances/ ad-hoc payments without need to prove or show grounds or reasons for their demand. To some extent, the element of undue pressure of bias in the action of the respondent cannot be ruled out. During the entire period of performance, it appears that the respondent did not take any action, but they seem to have woken up at a time when the performance period was about to expire. As already noticed, the parties have invoked the contract in relation to settlement of their claims and disputes by the prescribed Forums. The claims up to 5 crores as decided by the DRB would have to be treated as final determination of dispute between the parties. However, in excess of such amount, the party aggrieved would have a right to invoke the arbitration clause. During the course of hearing, it was stated that the respondents have already invoked the arbitration clause in regard to the claims in excess of Rs. 5 crores and with which findings the respondents are dissatisfied. The Additional Dispute Review Board (ADRB) in terms of clause 2.2 had submitted its report, particularly in regard to extension of time and associated costs on 16th July, 2004. Accepting the case of the applicant, the said Forum decided as under:-

Conclusions and Recommendations

The incisive analysis of delays under individual heads and of the impacts on time for completion, the ADRB considers the following as the entitlements of NJJV;

1.Extension of time as per clause 44 of the GCC of 50.53 months, i.e., up to 8th July, 2002.

2.Extension of time for the purpose of compensation of 38.04 months, i.e., up to 25th June 2001.

3.EOT related cost compensation for 38.04 months based on actual costs for:

Vehicle licenses, taxes

All risk insurance

CPE insurance

Motor vehicles insurance

Credit insurance

Bonds and Bank Guarantees

Financing Costs

And based on Sealed Envelope costs for:

Staff Expatriates

Staff Indian

Labour

Food Allowances

Site general Expense

Radio, telephone, telex

Road, camp and site maintenance

Office in Kotla and Delhi.

General Expenses-vehicle running costs

Main office expenses

NJJV will be entitled to price adjustment per Clause 70 of the GCC.

NJJV will also be entitled to simple interest on the net amount due, inclusive of escalation, at 10% per annum up until the time that payment is made.

While determining the net amount due to NJJV, the time-related cost compensation already paid on the basis of recommendations of the DRB, through the extra BOQ quantities and items and as provisional payments as well as price adjustments already made should be taken into account to eliminate duplication in payments.

As per the assessment made by the ADRB (see Annex 1), the net amount due to NJJV amounts to approximately Rs. 41 crores including an estimate of escalation and interest. The details of this are shown in the annexes attached as part of this Report. The payments as per Contract Agreement in different currencies would be Rs. 225.54 million plus US\$ 3.35 million plus ITL 4,083.95 millions. SJVN and NJJV will have to check these calculations (in respect of escalation and interest) and make any necessary adjustments.

What follows hereafter comprises acknowledgments , Appendices and Annexures. Consequently, the members of the ADRB sign their names to this Report unanimously, hereunder:

Mr. S. R. Narasimhan

Chairman of the ADRB.

25. It was contended on behalf of the applicants that even the claims which are of the value of less than Rs. 5 crores and have been determined by the internal determinative process prescribed under the terms of the contract, have not been honoured by the respondents. On the contrary, the respondents have acted with greater vehemence on grant of claims. It is also indicated that special experts, including foreign persons, were appointed to examine the version of the applicants at site and all such reports are favorable to the applicants and does not in any way help the unjustified and unfair attitude adopted by the respondents. Once the parties have opted for providing of an internal determinative forum or adjudicative mechanism, then it is obligatory and is expected from each one of them that they shall not only abide by such terms but would honour the decision of such Forum in its spirit and substance. The parties should essentially abide by these terms and should not disrespect or hinder or cause to hinder the result of such determination. The conduct of a party in this regard would be a relevant factor to be considered by the court, while deciding such interim applications. The expression "extraordinary special equities" or "irretrievable injustice/injury" are not defined expressions. They are to have such connotation and meaning as may be justified with reference to the facts and circumstances of each case. The court has to give such construction which would avoid reduncing, hardship or even repugnancy. The clauses of the agreement between the parties would have to be construed in their simple language so as to implement the essence of the contract. There is no doubt that court has to look into the terms of the bank guarantee and letter of invocation primarily for the purposes of deciding the fate of a prayed injunctive relief. The undue influence and pressure caused by the respondents on the applicant in extracting extensions, undertakings may not be completely proved on record at this stage of the proceedings, but this is a relevant factor to determine the extent of irretrievable injustice/injury to which the applicant would be exposed, if the encashment of the bank guarantee is permitted. There is an apparent attempt on the part of the respondents to frustrate the findings recorded by the internal determinative adjudicating machinery i.e. CMD's findings as well as the finding of DRB, as afore-referred. Once these findings are against the respondents and it has been held that the applicant is entitled to extension of period, it will be more than unfair to permit the respondents to invoke the bank guarantees at this stage of the proceedings. The cumulative effect of the above analysis of the case is that the respondents have not invoked the bank guarantees in terms of the clause, the action of the respondent in insisting upon encashment of bank guarantees is bound to cause irretrievable injustice and injury to the applicants, who otherwise have a case of special equities in their favor. Another very relevant factor is that after invoking the bank guarantees on 7th July, 2003, the respondents themselves have always agreed not to invoke the bank guarantees on the condition that the applicants would keep the bank guarantees alive. This is true even as on July 2004, when the respondents wrote a letter dated 20.09.2003. Thus, no injustice would be caused to the respondents if the bank guarantees are not permitted to be encased at this stage, subject to the

condition that they are kept alive by the applicants. This course of action would even balance the equities between the parties and would be least prejudicial to the interest of any of the parties. But, if such bank guarantees are permitted to be invoked/encashed, the applicant would suffer an irretrievable injustice and injury because they may not even be able to bear such a financial imbalance, particularly when their claims against the respondents have been allowed by the domestic adjudicating process prescribed under the terms of the contract.

26. For the reasons afore-stated, this petition u/s 9 of the Arbitration and Conciliation Act, 1996 is allowed. The respondents are hereby restrained from invoking or encashing the Bank Guarantees No. 900/5204, 900/5125, 900/5203, 900/5260, 900/5346, 900/5408, 900/5420, 900/5430, 900/5454, 900/5468, 900/5484, 900/5485, 900/5559, 900/5574, 900/5591, 900/5640 and 900/5665 issued by Bank San Paolo IMI SPA and No. 99/202 issued by State Bank of India, Frankfurt Branch, and from acting or taking any steps pursuant to the letters dated 13.4.2004 and 7.6.2005, subject to the condition that the applicants would keep the above mentioned bank guarantees alive and would not discharge the same without specific leave of the Court, or the Arbitral Tribunal, as the case may be. However, in the facts and circumstances of the case, parties are left to bear their own costs.

27. is No. 5872/2005 (under Order 39 Rule 1 and 2 read with Section 151 of the Code of Civil Procedure) also stands disposed of.