

(2001) 04 KAR CK 0032

In the Karnataka High Court

Case No : Miscellaneous First Appeal No. 3873 of 1999 (CPC)

HVS Technologies Inc., United States of America

APPELLANT

Vs

Aeronautical Development Agency (ADA), Bangalore and
another

RESPONDENT

Date of Decision : 04-04-2001

Acts Referred:

Arbitration and Conciliation Act, 1996 — Section 9
Civil Procedure Code, 1908 (CPC) — Order 39 Rule 1

Citation : (2001) 4 KarLJ 211 : (2001) 3 KCCR 1832

Hon'ble Judges : D.V. Shylendra Kumar, J

Bench : Single Bench

Advocate : Mr. P.B. appaiah, for the Appellant; Sri Padubidri Raghavendra Rao
and Sri A. Venkatachalaiah, for the Respondent

Judgement

The Court

1. This Miscellaneous First Appeal is directed against the order dated 6-8-1999 passed on LA. No. I in Miscellaneous No. 75 of 1999 on the file of the VI Additional City Civil Judge, Bangalore City, rejecting the application which had been filed under Order 39, Rules 1 and 2 seeking for a restraint order against the respondents from giving effect to a bank guarantee which had been issued by the second respondent-Bank in favour of the first respondent at the instance of the appellant. The application having been rejected and the Trial Court having declined to grant a restraint order as prayed for, the petitioner in the miscellaneous petition is in appeal before this Court.

2. The brief facts leading to the above appeal are that:

The appellant and first respondent herein had entered into a contract inter alia for supply of IPD measurement system which is an equipment involved in the development of a combat aircraft. The contract provided for various terms of supply -- period, technical specifications and the like. The contract also provided

for furnishing of bank guarantees as per Article 5.65 of the contract by the appellant in favour of the first respondent. Pursuant to the contract and on such terms of the contract, the second respondent-Bank had issued two bank guarantees one for the value of US \$ 37,972.5 by way of performance guarantee and another US S 2,27,835/- towards securing the advance amount provided to the appellant.

3. As there is no dispute on facts leading to the filing of the above appeal, I do not propose to refer to in detail, the various factual aspects. It is sufficient for the purpose of this appeal to refer to some of the relevant developments which have led to the contract having not been performed within the agreed period.

4. Sri Appaiah, learned Counsel appearing for the appellant does not dispute that due to certain developments, the appellant could not perform the contract as per the stipulated terms. However, what the learned Counsel for the appellant submits is that the performance of the contract was dependant on the availability of the concerned defence equipments which were being purchased in the United States and in view of the bilateral diplomatic relations between our country and the United States having dipped, the American Government had imposed sanctions on export of such defence equipments from United States of America to India and this development over which the appellant did not have any control, came in their way of performing the contract within the stipulated time and as per the terms. The learned Counsel has submitted that this development is in the nature of vis major and has been provided for under Article 7.1 of the contract.

5. The first respondent, on noticing that the appellant had not performed as per the terms of the contract, issued notice dated 6-1-1999 apprising the appellant that in view of the inability on the part of the appellant to meet the immediate technical requirements spelt out by their technical team, they are constrained to encash the bank guarantee.

6. By a follow-up communication dated 21-1-1999, the appellants also called upon the bank-second respondent, who had issued the bank guarantees, to honour the same and make payment of the guaranteed amounts in total. It was at this stage that the appellant, being aggrieved by the action taken by the first respondent, approached the Trial Court by filing a petition u/s 9 of the Arbitration and Conciliation Act, 1986 ("the Act" for short) and in the said petition, filed an application under Order 39, Rules 1 and 2 to restrain the first respondent herein from enforcing the bank guarantee or in the alternative, as the first respondent had already called upon the bank to honour the guarantees restrain the bank from giving effect to the bank guarantee during the pendency of the petition.

7. It is the submission of the learned Counsel for the appellant that at the time of filing of the petition u/s 9 before the Trial Court, a notice for appointment of an arbitrator had already been issued by the appellant and the arbitration proceeding was in the offing. The application for temporary injunction under Order 39, Rules 1 and 2 was filed on the ground that the bank guarantee having

been issued for non-performance of the contract and the circumstances in which the contract could not be performed and also as to whether the subsequent developments had frustrated the contract, are all questions which are to be decided by the arbitrator in the arbitration proceedings and the bank guarantee being linked to the performance aspect and the performance or non-performance of the appellant being the subject-matter before the arbitrator, it was just and necessary to restrain the respondents from encashing the bank guarantee or giving effect to the bank guarantee during the pendency of the arbitral proceedings and the arbitral proceedings were yet to commence, the appellant had approached the Court seeking for such interim relief by filing the petition u/s 9 of the Act.

8. The petition as well as the application were resisted by the first respondent herein. The learned Trial Judge, in view of the rival pleadings, formulated three points as under:-

"1. Whether the petitioner has made out a prima facie case?

2. Whether the balance of convenience does lie in favour of the petitioner?

3. Whether irreparable loss or injury will cause to the petitioner if T.I. is not granted?

4. To what order?"

9. The Trial Court, having answered all the points against the appellant, rejected the application filed under Order 39, Rules 1 and 2. It is aggrieved by this order, the appellant is before this Court in appeal.

10. Sri Appaiah, learned Counsel for the appellant has reiterated the same grounds and has also urged that the first respondent is not justified in invoking the bank guarantee at this stage inasmuch as the breach of the contract by the appellant is yet to be established and at any rate, if the appellant has to be given the benefit of the terms envisaged under Article 17.1 of the main contract providing for special circumstances which may relieve the parties of the liabilities and obligations under the contract and that being an aspect which is now seized before the arbitrator Court is informed that during the pendency of this appeal an arbitrator has been appointed and the arbitration proceedings are already at an advanced stage, encashment of bank guarantee contrary to the terms of the contract will definitely amount to irretrievable injury and hardship to the appellant. It is also submitted by the learned Counsel for the appellant that Clause 8 of the bank guarantee provides for giving a clear 31 days time to the appellant before the guarantee could be enforced and 31 days time can be utilised by the appellant for making good the deficiencies and it is only if the appellant is unable to do that, then alone the bank guarantee can be enforced and in the instant case, the first respondent having called upon the bank within fifteen days" time of issue of notice to the appellant, invocation of the bank guarantee is not in order.

11. Sri Padubidri Raghavendra Rao, learned Counsel for first respondent has submitted that in the first instance the bank guarantee is a bipartite agreement between the bank and the first respondent and the appellant is in the position of a third party to such an agreement. The appellant has no right to seek an order of restraint either against the first respondent or the second respondent when the first respondent is trying to work out its rights under the bank guarantee as against the second respondent. It is the submission of the learned Counsel that in this view of the matter, the very petition u/s 9 of the Act is not maintainable. It is also submitted that the arbitration proceedings before the arbitrator being only concerned with the breach or otherwise of the contract between the parties and the bank guarantee being not subject-matter before the arbitrator, a petition u/s 9 of the Act for seeking interim order in its favour by a Civil Court in respect of a non-existing matter before the arbitrator in itself is not maintainable.

(emphasis supplied)

12. I am of the view that this submission of the learned Counsel for the first respondent is of substance. Section 9 of the Act provides for a situation where a party to an arbitration proceedings, at any time before or during arbitral proceedings or after the making of the award and before it becomes enforceable as per the Act, may apply to a Civil Court for appropriate orders to secure the subject-matter of the arbitration proceedings. This is provided for under the Arbitration Act inasmuch as the arbitrator himself does not have such a power and in the event the subject-matter of the arbitration does not survive the arbitration proceedings by taking suitable steps, the entire arbitration proceedings may be rendered ineffective or infunctuous.

13. In the instant case, the two bank guarantees are not directly subjects before the arbitrator as being subjects of any dispute between the parties. In such a situation, maintainability of a petition u/s 9 of the Act prima facie is not tenable.

14. This aspect apart, insofar as the bank guarantee being a bipartite agreement between the bank and the beneficiaries, the law is very well-settled by a series of decisions by the Apex Court and the High Courts that such a bank guarantee could be said to be void only in two situations namely (1) where the main contract between the parties for the performance of which the bank guarantee is furnished itself is vitiated by fraud and the main contract has been brought about by practising fraud by one of the parties to the contract and (2) where the enforcement of bank guarantee would lead to arbitrariness or irretrievable injury and hardship to the parties against whom the bank guarantee is enforced.

15. In the instant case, admittedly there is no averment of fraud in the bringing about of the contract between the parties. In fact, it is the case of the appellant that he had been prevented from performing his part of the contract due to certain subsequent developments which were not within his control.

16. Encashment of bank guarantee by a beneficiary is not determinative of rights between the parties and the amount encashed under the bank guarantee cannot

be said to belong to the beneficiary as a matter of right for all times to come. It is only because of agreement between the parties to provide for in a certain situation as an interim measure. Ultimately the rights and liabilities are to be determined in the arbitration proceedings. If that is so, the bank guarantee amount even if it is encashed in fact is only towards adjustment on the final award being passed by the arbitrator. In a commercial transaction of this nature where loss is as much an incident as making profits, the mere fact that certain amounts will be at the disposal of the first respondent till the disposal of the arbitration proceeding, cannot be said to be a situation resulting in irretrievable injury and hardship to the appellant.

17. Sri Padubidri Raghavendra Rao, learned Counsel for the first respondent, in this regard has relied upon the decisions of the Apex Court rendered in the case of Dwarikesh Sugar Industries Ltd. Vs. Prem Heavy Engineering Works (P) Ltd., and another, and Ansal Engineering Projects Ltd. Vs. Tehri Hydro Development Corporation Ltd. and Another, .

18. Following the ratio laid down in these decisions by the Apex Court and in the light of the facts as discussed above, this appeal is to be dismissed as without merit. Appeal is dismissed. No costs.