
(1996) 09 BOM CK 0014

In the Bombay High Court

Case No : Appeal No. 473 of 1994 in Notice of Motion No. 878 of 1989 in Suit No. 1056 of 1988

Kisan Sahakari Chini Mills Ltd.

APPELLANT

Vs

Richardson and Cruddas (1972) Ltd. and another

RESPONDENT

Date of Decision : 02-09-1996

Acts Referred:

Citation : (1999) 96 CompCas 776 : (1996) 2 MhLj 1010

Hon'ble Judges : M.S. Rane, J;B.P. Saraf, J

Bench : Division Bench

Advocate : Y.R. Naik, for the Appellant; J.J. Bhat and Ms. Anjali Chandurkar, for the Respondent

Judgement

Dr. B.P. Saraf, J.—This appeal is directed against the judgment and order of the learned single judge dated June 17, 1991, in Notice of Motion No. 78 of 1989 in Suit No. 1056 of 1988 restraining the appellants from invoking the bank guarantee furnished by respondent No. 1.

2. The material facts of the case relevant for deciding the controversy in this appeal, briefly stated are as follows : Respondent No. 1, Richardson and Cruddas (1972) Ltd., Bombay, had entered into an agreement dated October 27, 1985 ("the agreement") with the appellants, Kisan Sahakari Chini Mills Ltd, Shahjahanpur, Uttar Pradesh, for setting up a sugar plant at Lucknow for an aggregate price of Rs. 4.55 crores. To secure timely delivery, erection and commissioning of the plant and machinery, as provided in clause 15.1.1 of the said agreement, respondent No. 1 was required to furnish a bank guarantee to the appellants for a sum of Rs. 22.75 lakhs representing 5 per cent. of the contract price. The said bank guarantee was to endure till the successful completion of the trial operation of the plant as provided in clause 7.3 of the agreement. The plant was commissioned on December 8, 1987. The performance trial in terms of the above agreement was to take place up to the end of the second crushing season after the commissioning of the said plant which ended on

March 31, 1989. As respondent No. 1 failed to give the performance trial in terms of the agreement within the stipulated time, the appellants, by their letter dated March 27, 1989, invoked the above bank guarantee and requested the bank to pay a sum of Rs. 22.75 lakhs to them. On the other hand, respondent No. 1, through their advocate, served a notice on respondent No. 2-bank, which had issued the bank guarantee in favour of the appellants, informing them that the performance trial which they were required to give under the agreement to the appellants could not be given by them because of the failure of the appellants to make necessary arrangement for the said trial, and, as a result thereof, the bank guarantee stood lapsed. By the said letter, the bank was asked not to pay any amount to the appellants under the said guarantee in the event of the same being invoked by them. On receipt of the said notice, the bank did not pay the amount of Rs. 22.75 lakhs to the appellants in terms of the bank guarantee. respondent No. 1, thereafter, filed a suit in this court being Suit No. 1056 of 1988, for a declaration that the bank guarantee had lapsed and stood discharged and for restraining the appellants from invoking the same and respondent No. 2-bank from paying any amount to the appellants thereunder. A notice of motion was also taken out in the said suit for interim orders. The learned single judge by the impugned order dated June 17, 1991, passed in the notice of motion taken out by respondent No. 1 restrained the appellants from invoking the bank guarantee and respondent No. 2-bank from making any payment to the appellants in pursuance thereof. Hence, this appeal.

3. We have heard Y. R. Naik, learned counsel for the appellants, who submits that the learned single judge was not justified in passing the impugned order inasmuch as no case of irretrievable injustice or fraud could be made out by respondent No. 1 to justify issue of an order of injunction restraining the appellants from invoking the bank guarantee. Our attention was drawn by Naik to the following observations of the learned single judge in the impugned order :

"Under clause 7.3.1, the trial was to be conducted by a committee consisting of authorised representatives under the agreement and the first defendant were to give a notice and fix the date for the performance trial, and even in the absence of the plaintiff, it could have been carried out, which, of course, was not done in the present case. It is possible, both the parties were not in a position to fix a convenient date for the purpose of having a performance trial, but at the same time the parties have to be fair towards each other in enforcing the terms and conditions of the agreement. In other words, having regard to a given situation, if a party takes an unfair advantage to the detriment of the other side, prima facie, it could be said that such a conduct could be considered as fraud in law. If that is so, I must necessarily hold that the plaintiffs have made out a prima facie case in support of their claim for an injunction."

4. Mr. Naik contends that the learned single judge committed manifest error of law in interpreting the word "fraud" in the manner done by him and in holding that the invocation of the bank guarantee, in the facts and circumstances set out

in the above passage, amounted to "fraud". In support of this contention, our attention was drawn to the number of decisions of the Supreme Court, to which we shall refer a little later, where the Supreme Court has said what "fraud" means in the context of restraining the invocation of a bank guarantee.

5. Mr. J. J. Bhat, learned counsel for respondent No. 1, on the other hand, submits that in the instant case, the performance trial could not be given in the second crushing season after the date of commissioning of the plant because of the failure of the appellants to make requisite arrangements for the same. According to Mr. Bhat, in such a situation, under the terms of agreement, the plant is deemed to be taken over by the appellants, which has the effect of discharging the bank guarantee. Mr. Bhat further submits that the first respondent were always willing to carry out the performance trial in terms of the agreement and there was no default on their part. According to Mr. Bhat, it is the appellants who failed to make necessary arrangements for the purpose of carrying out the performance trial and that being so, they are not entitled to invoke the bank guarantee. Mr. Bhat, therefore, contends that, in the circumstances set out above, in the instant case, the learned single judge was justified in restraining the appellants from invoking the bank guarantee.

6. We have given our careful consideration to the rival submissions. Admittedly, the bank guarantee for Rs. 22.75 lakhs was given to the appellants by respondent No. 2, the State Bank of India, to ensure timely delivery, erection and commissioning of the plant and machinery and performance trial before the end of the second crushing season as provided in clause 15.1.1 of the said agreement. There is also no dispute about the fact that the performance trial did not take place before the end of the second crushing season as contemplated by the agreement and it was on that account that the bank guarantee was sought to be invoked by the appellants. The dispute, in fact, is in regard to the cause of the failure of respondent No. 1 to give the performance trial within the stipulated time. According to respondent No. 1, it is because of the failure of the appellants to make necessary arrangements for the performance trial as a result of which the trial could not take place, and in that view of the matter the appellants cannot be allowed to take advantage of their own default by invoking the bank guarantee. The case of the appellants, on the other hand, is that there was no such failure on their part. It is stated by the appellants that they had written to respondent No. 1 as far back as on December 19, 1988, that the performance trial would be conducted in the second fortnight of January, 1989, and requested them to indicate a convenient date for the purpose. It is respondent No. 1, who could not give a date in the second fortnight of January, 1989, but agreed to give the performance trial only on February 16, 1989. The appellants, thereupon, informed respondent No. 1 that the National Federation, which was one of the parties in terms of the agreement to certify the performance trial, had confirmed February 21, 1989, as the date for the performance trial. The performance trial was adjourned, thereafter, from time to time for reasons beyond the control of the appellants. The appellants, therefore, submit that it is wrong on the part of

respondent No. 1 to contend that the performance trial could not take place within the stipulated time because of the failure of the appellants to make necessary arrangement for the same. It is contended on behalf of the appellants that the controversy as to why the performance trial could not take place within the stipulated time or who was responsible for the same, pertains to the agreement between the appellants and respondent No. 1 and it has nothing to do with the agreement of bank guarantee between the appellants and respondent No. 2-bank, which is an independent agreement by which the second respondent bank had agreed to pay to the appellants on demand a sum of Rs. 22.75 lakhs without demur and without requiring them to invoke any legal remedy. Our attention was drawn to the clauses of the bank guarantee where it is specifically provided that the appellants shall be the sole judge of whether respondent No. 1 have committed any breach of the terms and conditions of the agreement and the extent of losses, etc., caused to or suffered by the appellants counsel for the appellants submits that in the instant case no case of irretrievable injustice and fraud has been made out by respondent No. 1 to justify any restraint on the appellants from invoking the bank guarantee.

7. We have considered the facts and circumstances of the case. Admittedly, the bank guarantee was given by respondent No. 2, State Bank of India, to the appellants at the instance of respondent No. 1 to secure the obligations of respondent No. 1 under the agreement entered into between the appellants and respondent No. 1. there is no dispute about the fact that the bank had agreed to pay to the appellants on demand and without demur the guaranteed amount. That is evident from clause 2 of the bank guarantee which reads as follows :

"The guarantor shall pay to the purchasers on demand the sum under clause 1 above without demur and without requiring the purchasers to invoke any legal remedy that may be available to them it being understood and agreed, firstly, that the purchasers shall be the sole judge of and as to whether the sellers have committed any breaches of the terms and conditions of the agreement and the extent of losses, damages, costs charges and expenses caused to or suffered by or that may be caused to or suffered by purchasers from time to time shall be final and binding on the guarantor and, secondly, that the right of the purchasers to recover from the guarantor any amount due to the purchasers under this guarantee shall not be affected or suspended by reason of the fact that any dispute or disputes have been raised by the sellers with regard to their liability or that proceedings are pending before any tribunal, arbitrator(s) or court with regard thereto or in connection therewith, and, thirdly, that the guarantor shall immediately pay the aforesaid guaranteed amount to the purchasers on demand and it shall not be open to the guarantor to know the reasons of or to investigate or to go into the merits of the demand or to question or to challenge the demand or to know any fact affecting the demand, and, lastly, that it shall not be open to the guarantor to require proof of the liability of the sellers to pay the amount, before paying the aforesaid guaranteed amount to the purchasers."

8. It is clear from the above clause that the right of the appellants to recover from the guarantor bank any amount due to them under the said guarantee is not effected or suspended by reason of the fact that any dispute has been raised by respondent No. 1 with regard to their liability nor is it open to the bank to know the reasons of or investigate into the merits of the demand or to know any fact affecting the demand or to require proof of the liability of respondent No. 1 to pay the amount before paying the guaranteed amount to the appellants. In clause 9 of the said bank guarantee, it is also mentioned that the invocation of the bank guarantee shall be by a letter signed by the purchasers and counter - signed by the managing director of the appellants there is no dispute between the parties in this case that the bank guarantee was invoked by the appellants in the manner set out in the above clause. It is also agreed that the performance trial did not take place as stipulated in the agreement. The only controversy is as to who is responsible for the same, the appellants or respondent No. 1 and whether in view of such controversy, the appellants can be allowed to invoke the bank guarantee or they can be restrained from doing so as has been done by the learned single judge.

9. We have given our careful consideration to this controversy. The law as to the contractual obligations under the bank guarantee has been well-settled by now by a catena of decisions of the Supreme Court. The first decision that may be referred to in this connection is the decision of the Supreme Court in U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd., . In that case, on a review of a number of important English and Indian decisions on this point, Sabyasachi Mukharji J. (as his Lordship then was) held :

"I reiterate that commitments of banks must be honoured free from interference by the courts. Otherwise, trust in commerce, internal and international, would be irreparably damaged. It is only in exceptional cases, that is to say, in cases of fraud or in case of apprehension of irretrievable injustice that the court should interfere."

10. In the above case, Sabyasachi Mukharji J. also referred to the decision of court of Appeal in England in Hamzeh Malas and Sons v. British Imex Industries Ltd. [1958] 2 QB 127 where it was emphasized that an elaborate commercial system had been built upon the footing that a confirmed letter of credit (which is similar to a bank guarantee) constituted a bargain between the banker and the vendor of the goods, which imposed upon the banker an absolute obligation to pay, irrespective of any dispute there might be between the banker and the vendor of the goods, which imposed upon the banker an absolute obligation to pay, irrespective of any dispute there might be between the parties whether or not the goods were up to contract. The principle was that commercial trading must go on on the solemn guarantee either by letter of credit or by bank guarantee irrespective of any disputes between contracting parties whether or not the goods were up to contract. The banks cannot be absolved of their responsibility to meet the obligations. The following views of Kerr J. in R. D.

Harbottle (Mercantile) Ltd. v. National Westminster Bank Ltd. [1977] 2 All ER 862 on the question of injunction in respect of a performance bond, were also noted with approval (page 291 of 65 Comp Cas) :

"Only in exceptional cases would the courts interfere with the machinery of irrevocable obligations assumed by banks. In the case of a confirmed performance guarantee, just as in the case of a confirmed letter of credit, the bank was only concerned to ensure that the terms of its mandate and confirmation had been complied with and was in no way concerned with any contractual disputes which might have arisen between the buyers and sellers. Accordingly, since demands for payment had been made by the buyers under the guarantees and the plaintiffs had not established that the demands were fraudulent or other special circumstances, there were no grounds for continuing the injunctions."

11. Reference was also made to the decision of the Court of Appeal in *Edward Owen Engineering Ltd. v. Barclays Bank International Ltd.* [1978] 1 All ER 976 where it was held by a Bench, consisting of Lord Denning M. R., Browne and Lord Geoffrey Lane LJJ., that where a bank had given a performance guarantee it was required to honour the guarantee according to its terms and was not concerned whether either party to the contract which underlay the guarantee was in default. The only exception to that rule was where fraud by one of the parties to the underlying contract had been established and the bank had notice of the fraud.

12. Referring to the contention of the learned single judge in that case that the injunction was not sought against the bank but it was an injunction sought against the party which seeks to invoke the bank guarantee, *Sabyasachi Mukharji J.* observed as follows (page 293 of 65 Comp Cas) :

"But the net effect of the injunction is to restrain the bank from performing the bank guarantee. That cannot be done. One cannot do indirectly what one is not free to do directly. But a maltreated man in such circumstances is not without remedy. The respondent was not to suffer any injustice which was irretrievable. The respondent can sue the appellant for damages. In this case, there cannot be any basis for the apprehension that irretrievable damages would be caused. I am of the opinion that this is not a case in which injunction should be granted. An irrevocable commitment either in the form of a confirmed bank guarantee or irrevocable letter of credit cannot be interfered with except in case of fraud or in case of apprehension of irretrievable injustice has been made out. This is a well-settled principle of the law in England. This is also a well-settled principle of law in India."

13. A number of decisions of various High Courts in India were also considered. On an analysis of the same, it was observed as follows (page 295) :

"It is not the decision that there should be a *prima facie* case. In order to restrain the operation either of an irrevocable letter of credit or of a confirmed letter of credit or of the bank guarantee, there should be serious dispute and there should

be a good prima facie case of fraud and special equities in the form of preventing irretrievable injustice between the parties. Otherwise, the very purpose of bank guarantees would be negative and the fabric of trading operations would get jeopardised."

14. Reference was also made to the decision of the Supreme Court in *Tarapore and Co. v. V/o Tractoroexport* [1696] 2 SCR 920 : [1970] 40 Comp Cas 447 where in the context of an irrevocable letter of credit it was observed that an irrevocable letter of credit has a definite implication. It is independent of and unqualified by the contract of sale or other underlying transactions. It is a mechanism of great important in international trade and any interference with that mechanism was bound to have serious repercussions on the international trade of this country. It was reiterated that the autonomy of an irrevocable letter of credit was entitled to protection and except in very exceptional circumstances courts should not interfere with that autonomy. These observations a fortiori apply to a bank guarantee.

15. The law was summed up by Sabyasachi Mukharji J. thus (page 297 of 65 Comp Cas) :

"On the basis of these principles, I reiterate that commitments of banks must be honoured free from interference by the courts. Otherwise, trust in commerce, internal and international, would be irreparably damaged. It is only in exceptional cases, that is to say, in cases of fraud or in case of apprehension of irretrievable injustice that the court should interfere."

16. In this concurring judgment in *U.P. Co-operative Federation Ltd. v. Singh Consultants and Engineers (P.) Ltd.* [1989] 65 Comp Cas 283 (SC), Jagannatha Shetty J., while dealing with the above general principles, quoted with approval the following observations of A. P. Sen J. in *United Commercial Bank Vs. Bank of India and Others*, :

".....the rule is well established that a bank issuing or confirming a letter of credit is not concerned with the underlying contract between the buyer and seller. Duties of a bank under a letter of credit are created by the document itself, but in any case it has the power and is subject to the limitations which are given or imposed by it, in the absence of the appropriate provisions in the letter of credit....."

17. The courts usually refrain from granting injunction to restrain the performance of the contractual obligations arising out of a letter of credit or a bank guarantee between one bank and another. If such temporary or a bank guarantee between one bank and another. If such temporary injunction were to be granted in a transaction between a banker and a banker, restraining a bank from recalling the amount due when payment is made reserve to another bank or in terms of the letter of guarantee or credit executed by it, the whole banking system in the country would fail. In view of the banker's obligation under an irrevocable letter of credit to pay, his buyer-customer cannot instruct him not to

pay."

17. Shetty J. also referred with approval to the following observations of Lord Denning M.R. in *Edward Owen Engineering Ltd. v. Barclay's Bank International Ltd.* [1978] 1 ALL FR 976 :

"A bank which gives a performance guarantee must honour that guarantee according to its terms. It is not concerned in the least with the relations between the supplier and the customer; nor with the question whether the supplier has performed his contractual obligation or not; nor with the question whether the supplier is in default or not. The bank must pay conditions. The only exception is when there is a clear fraud of which the bank has notice."

18. The nature of "fraud", which is a ground for refusing to honour the bank guarantee, was described by Shetty J. thus (page 303 of 65 Comp Cas) :

"The nature of the fraud that the courts talk about is fraud of an "egregious nature as to vitiate the entire underlying transaction". It is the fraud of the beneficiary, not the fraud of somebody else."

19. It was, however, made clear that the court should not lightly interfere in the operation of the irrevocable documentary credit and that in order to restrain the operation of an irrevocable letter of credit, performance bond or guarantee, there should be a serious dispute to be tried and there should be a good prima facie case of fraud.

20. The above decision in *U.P. Co-operative Federation Ltd. v. Singh Consultants and Engineers (P.) Ltd.* [1989] 65 Comp Cas 283 (SC) was followed by a three-judge Bench of the Supreme Court in *General Electric Technical Services Company Inc. Vs. M/s. Punj Sons (P) Ltd.* and another, . In the above case, the Supreme Court set aside the order of the Delhi High Court staying the encashment of the bank guarantee. While doing so, the Supreme Court observed (page 649 of 74 Comp Cas):

"The demand by GETSCO is under the bank guarantee and as per the terms thereof. The bank has to pay and the bank was willing to pay as per the undertaking. The bank cannot be interdicted by the court at the instance of respondent No. 1 in the absence of fraud or special equities in the form of preventing irretrievable injustice between the parties. The High Court, in the absence of a prima facie case on such matters, has committed an error in restraining the bank from honouring its commitment under the bank guarantee."

21. The Supreme Court had occasion to consider the very same controversy once again in *Svenska Handelsbanken v. Indian Charge Chrome* [1994] 79 Comp Cas 589: JT[1993] 6 189. A three-judge Bench of the Supreme Court, on consideration of the facts and circumstances of that case, observed :

"....it appears to us that the High Court totally misdirected itself in assuming that the present application for interim relief against the enforcement of bank

guarantee is not to be decided strictly on principles of injunction in relation to bank guarantees but general principles of injunction on lenders would be applicable and on that basis proceeded to decide the matter."

22. It was further observed (page 624) :

"The High Court totally ignored the irretrievable injury which will be caused to defendant No. 12 [Industrial and Development Bank of India] in not honouring the bank guarantee in the international market which may cause grievous and irretrievable damage to the interest of the country as opposed to the loss of money to the borrower plaintiff. There was no question of defendant No. 4 not making any demand. The installments for repayment of the loans had already been fixed and liable to be paid without demand by defendant No. 4 Defendant No. 12 is under a duty to pay the installments regularly on a fixed date without any demand to defendant No. 4."

23. It was reiterated (page 624) :

"In law relating to bank guarantees, a party seeking injunction from encashing of the bank guarantee by the suppliers has to show a prima facie case of established fraud and an irretrievable injury."

24. It is well-settled that irretrievable injury may be established by demonstrating that the party seeking a restrain on invocation of the bank guarantee has no adequate remedy at law. Reference may be made in this connection to the decision of the Supreme Court in National Thermal Power Corporation Ltd. v. Flowmore Pvt. Ltd. [1995] 84 Comp Cas 97 : JT[1995] 5 591. In that case, dealing with irretrievable injustice, it was observed by Sujata Manohar J. :

"....while irretrievable injustice should be of the kind arising in an irretrievable situation which was referred to in the U. S. case of Itek Corporation v. First National Bank of Boston 566 Fed Supp. 1210, the irreparable harm should not be speculative . It should be genuine and immediate as well as irreversible a kind of situation which existed in the case of Itek Corporation v. First National Bank of Boston 566 Fed Supp. 1210 where, on account of the revolution in Iran the American Government had cancelled all export contracts to Iran and had blocked all Iranian assets within the jurisdiction of the United States. Fifty-two Americans had been taken hostage in Iran. In this situation, the court felt that the plaintiff had no remedy at all and the harm to him would be irreparable. This kind of a situation is not a likely situation."

25. Her Lordship also referred to the decision of the Supreme Court in Svenska Handelsbanken v. Indian Charge Chrome [1994] 79 Comp Cas 589 where the court had cited with approval the observation in the case of U. P. Co-operative Federation Ltd. v. Singh Consultants and Engineers (P.) Ltd. [1988] 65 Comp Cas 283 (SC) to the effect that the court should not lightly interfere with a performance bond or guarantee unless there is fraud of the beneficiary and not

somebody else.

26. So far as established of fraud is concerned, it is well settled by the decision of the Supreme Court in *Svenska Handelsbanken v. Indian Charge Chrome* [1994] 79 Comp Cas 589 that mere pleadings do not make a strong case of prima facie fraud. The material and evidence has to show it. The Supreme Court, in the above case, referred with approval the observations of the Privy Council in *Narayanan Chettyar v. Official Assignee* AIR 1941 SC 93, to the effect that fraud like any other charge of a criminal proceedings must be established beyond reasonable doubt. A finding as to fraud cannot be based on suspicion and conjecture. To the same effect are the decisions of the Supreme Court in *National Thermal Power Corporation Ltd. v. Flowmore Pvt. Ltd.* [1995] 84 Comp Cas 97; JT[1995] 5 591 and *Larsen and Toubro Limited Vs. Maharashtra State Electricity Board and others*, .

27. On the question of fraud, the following observations of the Supreme Court in *The State Trading Corporation of India Ltd. Vs. Jainsons Clothing Corporation and another*, are also pertinent (page 478):

"The court should normally insist upon enforcement of the bank guarantee and the court should not interfere with the enforcement of the contract of guarantee unless there is a specific plea of fraud or special equities in favour of the plaintiff. He must necessarily plead and produce all the necessary evidence in proof of the fraud in execution of the contract of guarantee, but not the contract either of the original contract or any of the subsequent events that may happen as a ground for fraud."

28. It was held in the above case (page 477 of 85 Comp Cas) :

"The grant of injunction is a discretionary power it equity jurisdiction. The contract of guarantee is a trilateral contract under which the bank has undertaken to unconditionally and unequivocally abide by the terms of the contract. It is an act of trust with full faith to facilitate free flow of trade and commerce in internal or international trade or business. It creates an irrevocable obligation to perform the contract in terms thereof. On the occurrence of the events mentioned therein the bank guarantee becomes enforceable. The subsequent disputes in the performance of the contract do not give rise to a cause nor is the court justified on that basis to issue an injunction from enforcing the contract, i.e., the bank guarantee. The parties are not left with no remedy. In the event the dispute in the main contract ends in the party's favour, he/it is entitled to damages or other consequential reliefs."

29. In *National Thermal Power Corporation Ltd. v. Flowmore Pvt. Ltd.* [1995] 84 Comp Cas 97, it was reiterated by the Supreme Court that a bank guarantee which is payable on demand implies that the bank is liable to pay as and when a demand is made upon the bank by the beneficiary. The bank is not concerned with any inter se disputes between the beneficiary and the person at whose instance the bank had issued the bank guarantee.

30. In State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another, , on an analysis of law relating to bank guarantee, the following observation were made by the learned Chief Justice of India (page 28) :

"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."

31. The law in regard to enforcement of bank guarantee has been summed up by the learned Chief Justice thus (page 28) :

"The legal position, therefore, is that a bank guarantee is ordinarily as contract quite distinct and independent of the underlying contract, the performance of which it seeks to secure. To that extent, it can be said to give rise to a cause of action separate from that of the underlying contract."

32. Reference may also be made at this stage to a recent decision of the Supreme Court in Hindustan Steel Works Construction Ltd. Vs. Tarapore and Co. and another, . In that case, the Supreme Court repelled the contention that the law laid down in U. P. Co-operative Federation Ltd. v. Singh Consultants and Engineers (P.) Ltd. [1989] 65 Comp Cas 283 was that except in case of fraud and that too when it creates irretrievable injustice, the courts should not interfere by restraining the beneficiary from encashing the bank guarantee. On a detailed consideration of the above decision, it was observed by Nanavati J. (page 356) :

"In our opinion, that is not the ratio of the judgment. In the case, the court was not called upon to decide whether apart from fraud there can be any other valid ground for interference. Moreover, the said observations cannot be read like a text of a statute or out of context."

33. It was held (page 357) :

"Therefore, fraud cannot be said to be the only exception. In a case where the party approaching the court is able to establish that in view of special equities in this favour if injunction as requested is not granted then he would suffer irretrievable injustice, the court can and would interfere."

34. The law on the subject was summed up by Nanavati J. thus (page 360) :

"We are, therefore, of the opinion that the correct position of law is that commitment of banks must be honoured free from interference by the courts and it is only in exceptional cases, that is to say, in case of fraud or in a case where irretrievable injustice would be done if the bank guarantee is allowed to be encashed, the court should interfere."

35. The principles that emerge from the above decisions of the Supreme Court can be summed up thus :

(i) That a bank guarantee is ordinarily a contract quite distinct and independent of the underlying contract, the performances of which it seeks to secure and the bank is required to honour the guarantee according to its terms. 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 of guarantee itself. Once that document is in order, the bank giving the guarantee must honour the same and make payment.

(ii) The commitments of the banks under a bank guarantee must be honoured free from interference by the courts. Otherwise trust in commerce, internal and international, would be irreparably damaged.

(iii) It is only in exceptional cases, that is to say in the case of irretrievable injustice or fraud, that the court should interfere.

(iv) The nature of fraud is fraud of an egregious nature as to vitiate the entire underlying transaction. It is fraud of the beneficiary, not the fraud of somebody else. There must be a specific plea of fraud. The party alleging fraud must necessarily plead and produce all necessary evidence in proof of the fraud in execution of the contract of guarantee. Moreover, fraud like any other charge of a criminal proceedings must be established beyond reasonable doubt. A finding as to fraud cannot be based on suspicion and conjecture. The material and evidence have to show it.

(v) Irretrievable injustice should be of a kind arising in irretrievable situation. The irreparable harm should not be speculative. It should be genuine and immediate as well as irreversible. It should be a case where the party seeking restraint on invocation of the bank guarantee has no adequate remedy of law at all and the harm to him would be irreparable. The subsequent dispute in the performance of the contract does not give rise to cause nor the court would be justified on that basis to issue an injunction from enforcing a bank guarantee, because the party is not left without remedy in such a case. He is entitled to damages and other consequential reliefs.

(vi) The same principles will apply to cases where injunction is sought against a party seeking to invoke the bank guarantee because the net effect of such an injunction is to restrain the bank from performing the bank guarantee. That is so, because one cannot do indirectly what one is not free to do directly.

36. Applying the above principles to the facts of the instant case, it is abundantly clear that it is not a case where the bank should be restrained from honouring its commitment under the bank guarantee. Admittedly, the dispute between the appellants and respondent No. 1 in this case is whether respondent No. 1 have performed their contractual obligations under the underlying contract and if they

have failed, whether the appellants are responsible for the same. The bank is in no way concerned with the said dispute. In fact, the bank has categorically stated in the bank guarantee that its obligation thereunder is absolute which would not be affected by any dispute between the parties about the performance of the underlying contract. In terms of the bank guarantee, the appellant is the sole judge of and as to whether the other party has committed any breach of the terms and conditions of the underlying agreement and their decision is final and binding on the bank. It is categorically stated in the bank guarantee that it shall not be open to the guarantor to challenge the demand made by the appellant or to know the fact affecting the demand. The bank is also prohibited from asking the guarantor to produce proof of the liability of the other side to pay the amount before paying the guaranteed amount to the appellants on demand. Obviously, in the instant case, the bank has failed to fulfil its commitment under the bank guarantee. The learned single judge, in these circumstances, in our opinion, committed a grave error of law in restraining the appellants from invoking the bank guarantee and the bank from honouring the same. It is not a case where irretrievable injustice will be caused to respondent No. 1. Respondent No. 1 are not without any remedy in law. They may sue the appellants for damages if they have invoked the bank guarantee wrongly. There is no justification, whatsoever, in this case for an apprehension of irretrievable damage. So far as fraud is concerned, in the instant case, there is no case of fraud at all, not to speak of fraud single judge, in our view, erred in law in holding that invocation of the bank guarantee on the face of dispute between the p[arties in regard to fulfilment of the terms of the underlying contract amounted to fraud. That is not so. As the been held by the Supreme Court, it must be a fraud of an egregious nature as to vitiate the entire underlying transaction. That being so, the learned single judge should not have interfered with the bank guarantee.

37. In that view of the matter, this appeal is allowed. The judgment and order of the learned single judge dated June 17, 1991, is set aside and Notice of Motion No. 878 of 1989 is dismissed.

38. In the facts and circumstances of the case, there shall be no order as to costs.

39. Learned counsel for respondent No. 1 prays for stay of operation of this order for a period of ten weeks. We do not find any justification for granting stay for such a long time. However, we stay the operation of the order for a period of six weeks from today.

40. Certified copy expedited.