

(1996) 07 BOM CK 0035

In the Bombay High Court

Case No : Appeal No. 25 of 1995 in Notice of Motion No. 323 of 1993 in Suit No. 599 of 1993

M/s. Dodsai Limited

APPELLANT

Vs

Krishak Bharati Co-op. Ltd. and Another

RESPONDENT

Date of Decision : 03-07-1996

Acts Referred:

Contract Act, 1872 — Section 126

Citation : AIR 1997 Bom 3 : (1997) 1 BomCR 102 : (1999) 96 CompCas 165 : (1996) 2 MhLj 619

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

Bench : Division Bench

Advocate : S. K. Cooper, instructed by Rajesh Shroff and Co, for the Appellant; Virendra Tulzapurkar and Virag Tulzapurkar, instructed by . Kanga and Co., for the Respondent

Judgement

Dr. B. P. Saraf, J.—This appeal is directed against the order of the learned Single Judge dated 20th December, 1994 rejecting the prayer of the appellants M/s. Dodsai Limited for an injunction restraining the respondent No. 1, Krishak Bharati Cooperative Limited, from invoking the bank guarantee and respondent No. 2, the State Bank of India, from performing the same.

2. Briefly stated, the material facts of the case are as follows : The appellants M/s. Dodsai Limited had entered into a contract with the respondent No. 1, Krishak Bharati Co-operative Ltd., for laying pipe lines. In terms of the contract, a performance guarantee for Rs. 35,75,888/- was given by the appellants to respondent No. 1. A further bank guarantee was given by the appellants to respondent No. 1 for the World Bank advance of Rs. 4.57 crores. The performance guarantee stood discharged in due course. The bank guarantee for advance payment, however, subsisted, though in course of time the amount thereof came down to Rs. 13,20,03,147/-. By its letter dated 22nd August, 1992, the respondent No. 1 lodged its claim for encashment of the above bank guarantee as per clause 1 read with clause 10 of the bank guarantee for a sum

of Rs. 1,11,29,059/-. A copy of the said, letter was also sent to the appellants. Later, the bank guarantee was invoked by the respondent No. 1 by its telex message dated 25th January, 1993. In the said telex message, it was stated that the claim for encashment was on account of outstanding advance/claims under the contract against the appellants M/s. Dodsai Limited as per cls. 1, 5, 9 and 10 of the bank guarantee. The appellants thereupon filed a suit in this Court, being Suit No. 599 of 1993, for permanent injunction against the respondent No. 1 from invoking the bank guarantee and against the bank from performing the same. A notice of motion was also taken out in the said suit for interim order which was rejected by the learned single Judge. Hence this appeal.

3. We have heard the learned counsel for the appellants Mr. S. K. Cooper, who submits that the respondent No. 1 is not entitled to invoke the bank guarantee for a sum of Rs. 1,11,29,059/-. According to him, the bank guarantee can be invoked only for a sum of Rs. 38,75,654/- which was the amount of outstanding advance. The contention of the appellants is that the bank guarantee did not cover loss of interest on advance. Mr. Cooper, therefore, submits that in that view of the matter, the invocation of the bank guarantee by the respondent No. 1 in the instant case is outside the scope and ambit of the bank guarantee and fraudulent. Mr. Tulzapurkar, learned counsel for respondent No.1 vehemently opposes the above submission of the counsel for the appellants. According to him, the above submission of Mr. Cooper is even factually incorrect. Our attention was drawn in this connection to Exh. 5 (at page 65 of the paper book) by which the original bank guarantee was extended for a sum of Rs. 1,30,03,147/- and to Exh. 15 (at page 79 of the paper book) which shows how the above amount had been arrived at. We have perused the above exhibits. Exhibit 15 clearly shows that the amount of Rs. 1,30,03,147/- was arrived at by including the interest recoverable on the amount of outstanding advance. Mr. Tulzapurkar submits that on the face of the above documents, there is no basis or justification for the appellants to contend that the bank guarantee did not cover interest on outstanding amounts. The learned counsel further submits that even if there is a dispute about the amount payable by the appellants to the respondent No. 1, that would not justify grant of injunction restraining the respondent No. 1 from invoking the bank guarantee or the bank from discharging its liability under the same. According to the learned counsel, in order to restrain the operation of bank guarantee, there should be good prima facie case of fraud and special equities in the form of preventing irretrievable injustice between the parties. Reliance was placed in support of this contention on a number of decisions of the Supreme Court with which we shall deal a little later. It was contended that these conditions are wholly non-existent in the instant case. The appellants, according to Mr. Tulzapurkar, have neither been able to establish a case of prima facie fraud nor to make out a case of irretrievable injustice. It is, therefore, not-one of those cases where the operation of the bank guarantee can be restrained. The counsel submits that the learned single Judge was, therefore, justified in the instant case in refusing to interfere with the invocation of the

bank guarantee.

4. We have carefully considered the rival submissions of the learned counsel for the parties in the light of the facts of this case. We have also perused the various decisions of the Supreme Court on this point. The law is well-settled by now in regard to invocation of bank guarantees and the limits of the powers of the Court to interfere with the same. In *U.P. Cooperative Federation Ltd. Vs. Singh Consultants and Engineers (P) Ltd.*, it was held by Sabyasachi Mukherjee, J. (as he then was) that in order to restrain the operation of bank guarantee, there should be a serious dispute and a good prima facie case of fraud and special equities in the form of preventing irretrievable injustice between the parties. It was observed that the commitments of the banks must be honoured free from interference by the Courts and it is only in exceptional cases, that is, in case of fraud or in cases of irretrievable injustice that the Court should interfere as otherwise the very purpose of bank guarantee would be negated and the fabric of trading operations would be jeopardised. The nature of the fraud that the Courts talk about, said Jagannath Shetty, J. in the same decision, is a fraud of an "egregious nature as to vitiate the entire underlying transaction". It is a fraud of the beneficiary, and not the fraud of somebody else.

5. Reference may also be made at this stage to the decision of the Supreme Court in *Svenska Handelsbanken Vs. M/s. Indian Charge Chrome and others*, where a three Judges Bench of the Supreme Court, while dealing with performance guarantees and guarantees against advances, observed that looking at the obligation assumed by the bank under such guarantees, the bank cannot be prevented by the party at whose instance the guarantee was issued from honouring the credit guaranteed. Since the bank pledges its own credit involving its reputation, it was no defence except in case of fraud or irretrievable injustice. Dealing with the question as to how a case of fraud can be established, it was observed:

"Merely pleadings do not make a strong case of prima facie fraud. The material and evidence has to show it."

In the above decision, the Supreme Court also quoted with approval the observations of the Privy Council in AIR 1941 93 (Privy Council) 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. Flow-more Pvt. Ltd* reported in JT (1995) 5 (SC) 591: AIR 1995 SCW 4306 and *Larsen and Toubro Limited Vs. Maharashtra State Electricity Board and others*, .

6. In *State of Maharashtra and another Vs. M/s. National Construction Company, Bombay and another*, , the learned Chief Justice of India, analysed the law relating to bank guarantee and observed (at p. 898 of AIR SCW) :

"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."

The law on the subject was summed up by the learned Chief Justice of India in the following words (at p. 898 of AIR SCW) :

"The legal position, therefore, in that a bank guarantee is ordinarily a 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."

7. Applying the law laid down by the Supreme Court in the above decisions, we are of the clear opinion that encashment of the bank guarantee cannot be interfered with by the courts except (i) in a case of fraud or, (ii) in a case where irretrievable injustice would be done if bank guarantee is allowed to be encashed.

8. The learned counsel for the appellant laid great emphasis on the judgment of the Supreme Court in *Larsen & Toubro AIR 1995 SCW 4134* (supra). We have already considered the said decision. We do not find that the ratio of the said decision is in any way different from the ratio of other decisions on the point.

9. We have also perused the decision of the Supreme Court in *General Electric Technical Services Company Inc. Vs. M/s. Punj Sons (P) Ltd.* and another, . In the above case a bank guarantee was obtained in favour of the contractor by the sub-contractor to secure the mobilisation advance of 25 per cent of the contract value. On failure of sub-contractor to execute the work as per required specifications within stipulated time despite repeated opportunities, the contractor sought to encash the bank guarantee. The sub-contractor sought to restrain contractor from encashing the bank guarantee. The Supreme Court held that encashment of guarantee could not be refused on the ground that the contractor has failed to make a reference, to mobilisation advance in the letter seeking encashment of the bank guarantee and it amounted to suppression of material facts, in the sense that the mobilisation advance was under the contract to be recovered from the running bills. Secondly, the Bank is not concerned with the outstanding amount payable by the contractor under the running bills. The right to recover the amount under the running bills has no relevance to the liability of the Bank under the guarantee. The liability of the Bank remained intact irrespective of the recovery of mobilisation advance or the non-payment under the running bills.

10. Applying the ratio of the above decisions to the facts of the present case, we are of the clear opinion that the learned Single Judge was fully justified in refusing to grant Injunction restraining respondent No. 1 from encashment of the bank guarantee and respondent No. 2-Bank from making payment in pursuance

thereof. The appellants, in our opinion, have miserably failed to make out a case of a prima facie fraud. Nor, there is anything to show that encashment of bank guarantee will cause any irretrievable injustice to the appellants. As earlier stated, in such cases, the Bank is not concerned with the dispute between the appellants and respondent No. 1 in regard to the amount which may be actually due to the respondent No. 1 from the appellants. Such dispute cannot be a ground for restraining the respondent No. 1 from invoking the bank guarantee or the Bank from discharging its obligation in terms thereof in the absence of fraud or special equities in the form of preventing irretrievable injustice between the parties. By the bank guarantee, the Bank having undertaken to indemnify the respondent No. 1 "without demur or protest or without reference to the contractor (appellant)" the amount set out therein being the amount of 100 per cent of the claim/balance amount of payment or such other unadjusted amount of the advance, it has to honour its commitment. It cannot be restrained from doing so on the "ground that there is some dispute between the parties in regard to the actual amount payable, because the bank guarantee is a contract quite distinct and independent of the underlying contract the performance of which it seeks to secure. To that extent, it gives rise to a cause of action separate from that of the underlying contract. The bank has to honour the guarantee according to its terms and it is not concerned whether either party to the underlying contract was in default.

11. In the instant case, except that a dispute is sought to be raised by the appellant in regard to the amount payable, we do not find the existence of any of the ingredients which may justify restraining the invocation of a bank guarantee. As earlier stated, on the ground of dispute in regard to the amount payable the courts cannot interfere with the enforcement of a bank guarantee. In such a situation, in our opinion, in the instant case, the learned Single Judge rightly refused to grant injunction and interfere with the enforcement of bank guarantee. We, therefore, do not find any merit in this appeal and the same is, therefore, dismissed, in the facts and circumstances of this case, we make no order as to costs.

12. The learned counsel for the appellant prays for stay of this order. The learned counsel for the respondent vehemently opposes this prayer. Considering the facts and circumstances of the case and the well-settled legal position, we are not inclined to grant any such stay. The learned counsel for the appellants, however, submits that the appellant wants to move the Supreme Court and in that view of the matter, some time should be granted to enable him to do so. He also makes a statement that the bank guarantee has been extended up to December, 1996. In that view of the matter, we stay the operation of this order till 22nd July, 1996.

Order accordingly.